House of Commons
International Development Committee

Tax in Developing Countries: Increasing Resources for Development

Fourth Report of Session 2012–13

Volume I: Report, together with formal minutes, oral and written evidence

Additional written evidence is contained in Volume II, available on the Committee website at www.parliament.uk/indcom

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The International Development Committee

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The Reports of the Committee, the formal minutes relating to that report, oral evidence taken and some or all written evidence are available in a printed volume.

Additional written evidence may be published on the internet only.

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Summary

Tax is an issue of fundamental importance for development. If developing countries are to escape from aid dependency, and from poverty more broadly, it is imperative that their revenue authorities are able to collect taxes effectively. The effectiveness of tax collection can be enhanced in a number of ways, including:

- with respect to the extractive industries, a heavier focus on taxing volumes of extraction or turnover (as opposed to taxing profits), since turnover-based taxation is more difficult to avoid or evade;
- improved collection of personal income taxation, VAT and local property taxation.

Underpinning all this is an urgent need to provide incentives for hitherto unregistered enterprises to join the formal (i.e. taxpaying) sector. Again, there are a variety of ways of doing this. Whilst neither this Committee nor the Department for International Development (DFID) seeks to prescribe policy to developing country governments, DFID should support developing country governments as they attempt to resolve these issues. DFID should also support a broader dialogue around tax policymaking in developing countries.

The capacity of developing country governments to collect tax is not, of course, conditioned solely by the policies which they themselves adopt. On the contrary, global-level regulatory issues play a major role. Requiring tax authorities to exchange information automatically with their counterparts in other countries would constitute a strong deterrent against cross-border tax evasion, whilst requiring corporations to report their financial information on a country-by-country basis would enable irregularities to be more readily detected. In the immediate future, the Government should enact unilateral legislation to achieve both these objectives: in the former case, the relevant section of the US Foreign Account Tax Compliance Act may serve as a model. In the medium term, the Government should also use its influence in international fora to persuade other countries to enact similar measures.

One of the principal forms of cross-border tax evasion is ‘transfer pricing abuse.’ This occurs when a large corporation (i.e. one with multiple divisions) engages in intra-corporation transactions at non-market rates, with a view to ‘transferring’ its profits into countries where they will be taxed less heavily (tax havens). The scale of such abuses is disputed, and profits are also transferred for reasons unrelated to tax avoidance, but it is nevertheless a significant problem. To help developing country revenue authorities to detect this, DFID should stress—in its dealings with these revenue authorities—the importance of requiring ‘related party transactions’ (i.e. transactions taking place within the same corporation) to be declared on annual tax returns.

Since there is a risk that its revised Controlled Foreign Companies rules will encourage
the transferring of profits into tax havens, the Government should conduct an analysis of the likely financial impact on developing countries. Depending on the outcome of this analysis, it should consider dropping its proposals. More broadly, the Government should be required to assess any new primary or secondary UK tax legislation against its likely impact on revenue-raising in developing countries, and should designate a DFID ministerial responsibility for the development impact of tax and fiscal policy.

The Extractive Industries Transparency Initiative (EITI), founded in 2002 by the UK Government, is an excellent tool for identifying corruption. However, if the Government hopes to persuade more developing countries to take part, it must be willing to lead by example by becoming an EITI candidate itself. Additionally, we recommend that the Government support a further broadening of EITI in the coming years, under which participating companies and governments be required to publish the contracts which exist between them. Such transparency would allow any contracts which are patently unfair to be identified as such.

DFID provides technical assistance to national revenue authorities in developing countries, as well as providing funding for technical assistance delivered by HM Revenue & Customs (HMRC). Much of this work has been greatly successful: DFID’s work in Rwanda is just one example. We recommend that DFID scale up its technical assistance work with developing country revenue authorities. HMRC should also be provided with additional funding to enable it to do likewise.
1 Introduction

1. Tax is an issue of fundamental importance for development. If developing countries are to escape from aid dependency, and from poverty more broadly, it is imperative that their revenue authorities are able to collect taxes effectively. Tax revenues represent a more predictable and sustainable source of revenue than aid flows ever can. In addition, the ability to collect taxes also has implications for the quality of governance. Taxpayers have a legitimate right to expect something in return—namely a functioning state—so are more likely to hold their governments to account if they underperform. Citizens or companies which fall outside the tax ‘net’ are much less likely to do this.

Country-level tax profiles

2. The position of tax revenues within the wider economy varies widely between countries. In developing countries, tax revenues as a percentage of GDP are generally significantly lower than in developed countries. Table 1 illustrates this:

Table 1: tax revenues by country category

<table>
<thead>
<tr>
<th>Country category</th>
<th>Average tax revenues (% of GDP)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low Income Countries (LICs)</td>
<td>13.0</td>
</tr>
<tr>
<td>Lower Middle Income Countries (LMICs)</td>
<td>17.7</td>
</tr>
<tr>
<td>Upper Middle Income Countries (UMICs)</td>
<td>20.7</td>
</tr>
<tr>
<td>High Income Countries (HICs) / OECD members</td>
<td>35.4</td>
</tr>
</tbody>
</table>

Data source: Ev w85

3. Moreover, the forms of taxation which predominate tend to be very different in developing countries vis-a-vis developed countries. Personal income taxation tends to constitute only a very small proportion of the tax take in developing countries, whilst customs duties and other forms of trade-based taxation constitute a much more significant share. Furthermore, as we were told by Dr Jonathan Di John, Senior Lecturer in Political Economy at the School of Oriental and African Studies (SOAS), local property taxation is “a very important tax because it would be the main source of funding for local government, and it is negligible in even middle-income countries, let alone poor ones.”

4. Our Report begins (Chapter 2) with a consideration of how the policies of developing country governments affect their ability to collect tax revenues. In Chapter 3, we consider how developing countries’ tax revenues are affected by legislation enacted beyond their borders. We make recommendations to the Government, both on measures it could take unilaterally, and on measures which need to be taken at intergovernmental level, and for

1 Q 41
2 Ev w86
3 Ev w85
4 Q 51
which it should advocate. In Chapter 4, we assess the work which the UK Government is presently conducting on tax in developing countries, and make recommendations as to how this could be improved.

5. As part of our inquiry, we conducted a case study of Zambia. Our reasons for choosing Zambia were various. Firstly, as illustrated by Table 2, it is a country whose economy is heavily dependent on copper mining:

Table 2: exports of fuels and mining products from Zambia

<table>
<thead>
<tr>
<th>Year</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exports of fuels and mining products (% of GDP)</td>
<td>29</td>
<td>31</td>
<td>28</td>
<td>27</td>
<td>37</td>
</tr>
</tbody>
</table>

Data source: adapted from WTO, World Bank

The size of the mining sector makes it a highly relevant case study, not only because a number of major multinational mining companies operate in Zambia, but also because resource-rich countries tend to face particular challenges in respect of taxation.5 Moreover, Zambia is no longer a Low Income Country (LIC), having been re-classified as a Lower Middle Income Country (LMIC) in 20116—so attention will naturally turn to the question of its graduation from aid, and the role taxation can play in this. Finally, it has a large DFID programme, including the provision of technical assistance to the Zambia Revenue Authority (ZRA).7

6. We received 37 pieces of written evidence from a wide range of organisations, and also held three oral evidence sessions. Witnesses at the oral evidence sessions included the Business and Industry Advisory Committee to the Organisation for Economic Co-operation and Development (OECD); leading academics from the London School of Economics (LSE), SOAS, and the Institute of Development Studies (IDS); as well as NGOs, corporations, DFID, HM Revenue & Customs (HMRC) and the Treasury. Finally, we visited Zambia in March 2012, holding meetings with the Ministry of Finance and the ZRA, and visiting the Copperbelt.

6 “Changes in Country Classifications”, World Bank, 1 July 2011, data.worldbank.org
7 Ev 93; DFID Zambia, Operational Plan 2011-2015 (updated June 2012)
2 Country-level tax policy

Forms of taxation

7. The appropriateness of a tax policy will always depend upon the precise circumstances of the country concerned; determining the tax policies of developing countries is a matter for the governments of the relevant countries. Nevertheless, if we are to assess DFID’s work on tax collection, we must begin by understanding the tax regimes of the countries in which it works. Table 3 sets out the respective importance of different forms of taxation in various Sub-Saharan African countries in 2008:

<table>
<thead>
<tr>
<th>Table 3: forms of taxation (% of GDP)</th>
<th>Botswana</th>
<th>Namibia</th>
<th>Nigeria</th>
<th>South Africa</th>
<th>Zambia</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total revenues (including non-tax revenues)</td>
<td>35.1</td>
<td>31.8</td>
<td>12.3</td>
<td>26.9</td>
<td>18.6</td>
</tr>
<tr>
<td>of which: revenues from extractive industries</td>
<td>13.8</td>
<td>3.2</td>
<td>10.3</td>
<td>data not available</td>
<td>1.48</td>
</tr>
<tr>
<td>Total tax revenues</td>
<td>21.6</td>
<td>29.4</td>
<td>12.3</td>
<td>26.3</td>
<td>17.5</td>
</tr>
<tr>
<td>of which: income tax</td>
<td>7.9</td>
<td>10.1</td>
<td>0.8</td>
<td>16.0</td>
<td>8.5</td>
</tr>
<tr>
<td>of which: VAT and sales tax</td>
<td>3.6</td>
<td>5.9</td>
<td>0.2</td>
<td>7.2</td>
<td>4.0</td>
</tr>
</tbody>
</table>

Source: IMF Article IV Reports. The figures from extractive industries revenues include revenue sources such as mineral royalties, which are regarded as non-tax revenues. These figures have been derived from IMF taxation data, and may be underestimates.

The remainder of this section aims to set out the advantages and disadvantages of each major form of taxation, drawing heavily on our case study of Zambia.

Non-corporate taxation

Personal income taxation

8. In his oral evidence to us, Dr Jonathan Di John reported that “in countries that do collect a lot of income tax, most comes from the PAYE system, so salaried workers contribute the vast majority of personal income tax”. We understood him to be implying that High Net Worth Individuals (HNWIs), who are often self-employed, may be relatively under-taxed. In the case of Zambia, however, Dr Di John acknowledged that “Zambia is one of the better tax collectors in sub-Saharan Africa: its tax collection is 17% or 18% of GDP, and it collects,
relatively, a fair amount of personal and corporate income tax, especially personal income tax.\textsuperscript{10}

If developing countries are to improve their collection of tax revenues, it is imperative that elites within those countries pay the correct amounts in personal income taxation, and—critically—are seen to do so.

\textit{VAT}

9. VAT is the principal form of indirect taxation—i.e. taxation levied on consumption rather than on income. Certain NGOs have raised concerns surrounding its allegedly regressive nature.\textsuperscript{11} As an example, Christian Aid argued that VAT “can be very regressive in terms of putting high cost on very low income earners.”\textsuperscript{12} Christian Aid do, however, recognise that this problem can be resolved by exempting key items from VAT (or ‘charging VAT at zero rate’ on such items)\textsuperscript{13}. Moreover, as highlighted by Professor Mick Moore, Professorial Fellow at the Institute of Development Studies:

\begin{quote}
It is far from clear that value added tax is a regressive tax. Yes, it falls on consumption, but in many developing countries, as in Britain, a large number of basic goods are zero-rated, so it is not clear that it is actually regressive, and research shows we do not know the answer. But the important thing about its alleged regressive nature is what tax this is actually replacing. In a situation where tax authorities find it very difficult to raise revenue at all, if you have a good instrument that is doing a very good job, I would keep it and concentrate on other things.\textsuperscript{14}
\end{quote}

\textit{Local taxation}

10. In its written evidence, the International Centre for Tax and Development (ICTD) argues that—whilst there has been considerable progress in building the capacity of national tax authorities—there has been relatively limited focus on taxation at regional and local levels. It claims that this represents a missed opportunity to enhance the autonomy and decision-making power of local authorities, and to make them more accountable to the public.\textsuperscript{15} Additionally, in many countries including Zambia, local government is increasingly responsible for the delivery of services, but lacks adequate resources to meet these responsibilities.\textsuperscript{16}

11. Local property taxation not only provides a valuable source of revenues for local governments; it also requires the development of land registries. Land registries lead to improvements in the security of property rights,\textsuperscript{17} and enable people to use property as

\begin{footnotes}
\item[10] Q 56
\item[11] Ev 58; Ev 78
\item[12] Q 5
\item[13] Ev 78
\item[14] Q 41
\item[15] Ev 91
\item[16] Taxation, Resource Mobilisation and State Performance, Crisis States Research Centre Working Paper no. 84 (Jonathan DiJohn, November 2010, \url{www.dfid.gov.uk/r4d}
\item[17] Q 51
\end{footnotes}
security against loans: the Committee was particularly impressed with DFID’s work on land registries in during its visit to Rwanda in 2011. The Department told us that the UK Land Registry had signed up to iFUSE, a scheme facility under which UK public bodies provide technical assistance to their developing country counterparts: we warmly welcome this development.

12. During our visit to Zambia, we were told that Mopani Copper Mines, which is majority owned by Glencore, was in dispute with the Municipal Council of Mufulira in respect of its local property tax bill. It was clear that the company’s relationship with the local community had been damaged by the dispute, and we hope it can be resolved swiftly.

13. In many developing countries, there is considerable room for improvement in the collection of non-corporate taxation. Given its usefulness in promoting land registries, an increased focus on local property taxation is likely to be especially fruitful. DFID should seek to support the national revenue authorities of developing countries as they attempt to improve the collection of personal income taxes, VAT and local property taxes. DFID should also encourage and support programmes that engage civil society and trade organisations, academics, journalists and parliamentarians in the tax policymaking process.

Corporate taxation

14. Corporate taxation represents an important source of government revenues. In setting their corporate taxation policies, governments must seek to strike a balance between the need to raise sufficient revenues, and the need to attract investment. Bearing this in mind, governments must decide on their preferred corporate tax rate, and must also decide whether to offer any tax incentives. Tax incentives divide opinion: some focus on their adverse impact in terms of tax revenues foregone, whilst many businesses consider them as a useful incentive to invest.

15. Whilst tax incentives can be useful if applied appropriately, arbitrary tax exemptions are generally damaging. Professor Mick Moore suggested to us that in many African countries, revenue authorities granted tax exemptions worth around 5% of GDP, which may be up to one-third of total tax revenues. ICTD told us that ‘tax holidays’ for new companies were often manipulated, citing the example of existing hotel / tourism companies which ‘re-constitute’ under a new name so as to ensure their continuing eligibility.

16. Our case study of Zambia allows us to explore these issues in more detail. Prior to 1997, the Zambian mining sector was nationalised, with the mines operated by the state-owned Zambia Consolidated Copper Mines (ZCCM). Between 1997 and 2004, the mines were

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18 Q 184 19 Ev 93 20 Ev 81; Ev w63, Ev w87 21 Ev 85 22 Q 41 23 Q 132 24 Ev 89
privatised\textsuperscript{25} (though ZCCM Investment Holdings, the successor company to ZCCM, is 87\% state-owned and retains a minority shareholding in the mines).\textsuperscript{26}

17. It is clear that private investment in the mining industry has brought many benefits to Zambia. We visited two mines in Zambia, one run by Mopani Copper Mines and one run by Konkola Copper Mines. Mopani Copper Mines employs 8,300 people, with another 8,000 contractors working on site. In a country where the national minimum wage is US$81 per month, even the most junior of Mopani employees earns US$508 per month.\textsuperscript{27} We were informed that both companies also operated schools and healthcare facilities.

18. However, whether the mining industry contributes an appropriate level of tax revenues is less clear. At privatisation a highly business-friendly tax regime was implemented.\textsuperscript{28} During a meeting held at the Zambian Ministry of Finance, we were told that ‘Development Agreements,’ including preferential tax terms, had been signed—initially with two mining companies, and subsequently with several more. By 2004, we were told, those mining companies which did not have development agreements had become resentful of those which did. The Government thus decided to ‘level the playing field’ by extending the same tax incentives to all mining companies.

19. By 2008, as Figure 1 indicates, the copper price had risen to an all-time high:

\begin{figure}[h]
\centering
\includegraphics[width=\textwidth]{copper_prices.png}
\caption{Copper prices}
\end{figure}

Data source: IMF data. Refers to LME spot price for copper (grade A cathode), CIF European ports.

\textsuperscript{25} Ev w53
\textsuperscript{26} Ev 89
\textsuperscript{27} Ev 127
\textsuperscript{28} Ev 89
Thus the profitability of the mining industry had increased. However, as a result of the tax arrangements it had made, the Government gained very little in terms of corporate tax revenues: copper exports stood at $2 billion per annum, yet tax revenues from these were only $30 million: an effective tax rate of 1.5%. Paul Collier has highlighted that according to World Bank estimates, if the Zambian tax regime had been akin to that of Chile (the other major copper exporter), tax revenues from the industry in 2008 would have been closer to $800 million.29 We note that Chile is a more mature economy than Zambia, but this example still demonstrates the potential for Zambia to increase the amount of tax it collects from the industry.

20. In 2008, the Government abolished the Development Agreements,30 and introduced a new tax regime. As well as introducing a new variable profits tax, this regime focused much more heavily on turnover-based taxation, i.e. taxing turnover rather than profits. Whilst turnover-based taxation may be perceived as less progressive than profit-based taxation, we were told during our visit that the former is much easier to collect (more difficult to avoid or evade). This is because profits can be shifted into low-tax jurisdictions (as discussed elsewhere in this report), whereas turnover cannot. In the case of the copper industry, turnover is relatively simple to verify, e.g. by multiplying the price of the raw material (as per the London Metals Exchange, or LME) by the quantity produced—though systems must be in place to ensure that physical quantities can be accurately measured.31 In the case of minerals whose price is not listed on the London Metals Exchange, of course, verifying turnover poses a greater challenge.

21. The 2008 tax regime expanded turnover-based taxation in two principal ways:

- It introduced a windfall tax, rates of which were to be determined by the LME copper price. (Indeed the tax did not apply at all if the copper price was below $2.50 per pound.)32
- It increased the mineral royalty rate from 0.6% to 3%.33 (The mineral royalty is calculated as a simple percentage of total turnover, with the LME price used to verify turnover as explained above.)

22. The windfall tax, however, was considered by the mining companies to be overly punitive: some claimed that they were under no obligation to pay, citing a ‘fiscal stability clause’ in the now-abolished Development Agreements.34 Ultimately the windfall tax was abolished in 2009;35 the mining companies who had disputed its legality finally paid their...
arrears in 2011. The unpopularity of the windfall tax amongst mining companies, and its consequent failure, was attributed largely to flaws in its design: the thresholds should have been set higher, whilst the amounts paid should have been deducted from companies’ taxable profits before the regular corporate tax was charged.

23. During our visit, we were told that—following a change of government in September 2011—the new Patriotic Front (PF) Government had come under considerable pressure to re-instate the windfall tax. Thus far it has resisted; it has, however, increased the mineral royalty rate from 3% to 6%.

24. Our case study of Zambia thus provides an insight into the thorny issues which surround corporate taxation. We recognise that turnover-based taxation is a blunt instrument, and in countries where the revenue authority has sufficient capacity to enforce a profit-based taxation regime, turnover-based taxes should not be used. However, for many revenue authorities with lower levels of capacity, imposing a turnover-based tax may be the only reliable method of collecting corporate taxes. In these circumstances, turnover-based taxes are most valuable.

25. For reasons of transparency, it is highly desirable for corporations’ annual audited accounts to be made readily available to citizens and civil society organisations in the countries in which those corporations operate. In the case of Zambia, accounts are—in theory—available to the public on request, for a fee of around $4. However, there is some disagreement as to whether this happens in practice. For example, whilst Mopani Copper Mines assured us that its accounts had been made available in accordance with regulations, ActionAid tells us that it and its partner organisations have been unable to access the accounts. Thus there appears to be something of a bottleneck. We urge DFID to stress—in its dealings with the national revenue authorities of developing countries—the importance of making corporate accounts available to the public. In Zambia, to test the allegations that the process is not working at present, DFID should request access to the accounts of some of Zambia’s main corporations, using channels available to the ordinary Zambian citizen. In its response to this report, the Government should notify us of the outcome of these requests.

26. The Government should encourage the OECD and other standard-setting fora to require the filing of public statutory accounts in all jurisdictions. The Treasury should also press Crown Dependencies to meet these standards.

Broadening the tax base

27. In many developing countries, informal economic activity—i.e. economic activity which falls outside the tax ‘net’—is extremely widespread. In 2009, for example, Senegal had a working population of 5 million, yet 4.5 million of these were in the informal
sector—either operating as sole traders and not registered for tax, or employed in unregistered enterprises, which pay no tax on their profits and whose employees pay no tax on their wages. Data from 2008 indicates a broadly similar situation in Benin, Cameroon and Ethiopia. The large size of the informal sector has gender implications: a recent study of non-agricultural sectors in three Least Developed Countries (LDCs) in Africa countries found that the female working population was employed almost entirely in the informal sector.

28. In the case of Zambia, the working population stood at 5.2 million in 2008, with the vast majority (4.7 million) in the informal sector. As well as constituting the lion’s share of the economy, the informal sector was found to be growing more quickly than the formal sector.

29. The level of formalisation within particular economies is determined by a number of factors. Of principal importance is the strength of the legal system: traders and enterprises which have faith in the legal system are significantly more likely to enter the formal economy than those which do not. The degree to which traders and enterprises have confidence in their governments to make effective use of tax revenues is also a factor.

30. Developing country governments might employ various strategies to bring unregistered traders and enterprises into the tax base. As an example, they might seek to offer incentives—such as distribution and marketing assistance, or micro-credit schemes—in return for registration. In some cases a purely financial incentive might be offered: the Parliamentary Under-Secretary of State for International Development, Mr Stephen O’Brien MP, told us that this approach had worked well in Sri Lanka. In Zambia, meanwhile, the Government is currently considering a different approach, namely to require all unregistered enterprises to pay for a ‘business licence’ at a flat rate. Additionally, governments can incentivise traders and enterprises to register by charging VAT at a relatively high rate. This incentivises registration because as well as charging VAT on their sales—registered businesses are able to reclaim the VAT they pay on their purchases.

31. In countries where the level of economic activity is extremely limited, the cost and administrative burden of broadening the tax base might outweigh the benefit. In most countries, however, the benefits will be enough to warrant such initiatives.

32. In many of the countries in which DFID works, informal economic activity—i.e. economic activity which falls outside the tax ‘net’—is extremely widespread. Formalising

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41 Ev w14
42 Ev w15
43 Ev w16
44 Q 47
45 Q 47
46 Q 181
47 Q 143
48 Q 41
49 Q41; “Introduction to VAT”, HM Revenue & Customs, www.hmrc.gov.uk/vat
the economies of developing countries would have significant implications, both in terms of increased tax revenues and in terms of governance: those who operate in the formal economy are much more likely to hold their governments to account. To encourage unregistered traders and enterprises to enter the formal economy, developing country governments might offer a variety of incentives: examples include distribution and marketing assistance, micro-credit schemes, or purely financial incentives. DFID should support the governments of developing countries as they seek to incentivise hitherto unregistered enterprises to join the formal, taxpaying economy.
3 Global level tax policy

33. The ability of developing countries to collect taxes is determined not only by their own governments’ policies, but also by policies and initiatives launched beyond their borders, either by individual developed countries, or at intergovernmental level. This section examines several such policies and initiatives, and makes recommendations to the Government: both on measures it could enact unilaterally, and on measures which need to be taken at intergovernmental level, and which it should advocate.

Automatic exchange of information

34. Capital flight from developing countries—the process by which assets are removed from a developing country and stored overseas—is a serious problem for developing countries. As DFID rightly highlights in its written evidence, capital flight does not necessarily imply illegality; it may simply represent a rational economic decision to invest assets overseas.\(^5\) However, capital flight may also occur as a result of tax evasion. Global Financial Integrity estimates that illicit capital flight from developing countries totals over $1 trillion per year.\(^51\)

35. In this context, if the tax authorities of a developing country wish to investigate possible tax evasion by one of its citizens or corporations, they may need to obtain information pertaining to the offshore activities of the relevant citizen or corporation from the tax authorities of the relevant offshore jurisdiction—most likely a tax haven. Until recently, the only way for developing country authorities to do this was by making a formal request via a bilateral agreement with the relevant jurisdiction.\(^5\) Bilateral agreements take one of two forms:

- Tax Information Exchange Agreements (TIEAs), and
- Double Taxation Treaties (DTTs): the principal purpose of DTTs is to prevent the same item of income being taxed in two separate jurisdictions. As a part of this, however, DTTs make (limited) provision for exchange of information.\(^53\)

Making such requests constitutes a high and sometimes unaffordable administrative burden for the tax authorities concerned.\(^54\)

36. Since 2009, developing countries have had another option: by joining the Convention on Mutual Administrative Assistance in Tax Matters (a multilateral treaty for the exchange of information), the need for bilateral treaties is removed. (The Convention originally dates from 1988, but until 2009 was open only to Council of Europe and OECD members.)\(^55\)

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\(^{50\text{ Ev}}\text{98}\)

\(^{51\text{ Ev}}\text{w26}\)


\(^{54\text{ Ev}}\text{75}\)

However, developing countries still have to go through a relatively complex process in order to join the Convention.\(^{56}\) Additionally, even under the Convention, the need to make a formal request—and the consequent administrative burden—still stands, unless two particular signatories to their convention sign an additional agreement to the contrary.\(^{57}\)

37. Under the US Foreign Account Tax Compliance Act (FATCA), by contrast, information is exchanged automatically, rather than just on request. If a US citizen or corporation (subject to certain exemptions) holds an account with a financial institution outside of the US, this financial institution is required to provide an annual report to the US authorities, covering information including the account balances, gross deposits and gross withdrawals.\(^{58}\)

38. There are no similar rules in place for non-US citizens or corporations. The EU Savings Directive is currently the closest equivalent to FATCA in the EU: if any EU resident holds an account in a member state other than his / her country of residence, there is a requirement for the tax authorities of his / her country of residence to be notified of any interest paid on this account. (Austria and Luxembourg are currently exempt from this obligation for a ‘transitional period.’) However, unlike FATCA, which applies to tax authorities outside of the US, the EU Savings Directive does not apply to tax authorities outside of the EU.\(^{59}\)

39. It has thus been argued by organisations ranging from Christian Aid to Glencore, the global commodities trader, that a system of automatic information exchange should be implemented more widely (rather than just in the US).\(^{60}\) In its written evidence, the Tax Justice Network argues that:

> automatic exchange has clear advantages over the ‘on request’ approach mentioned above in so far as it has a stronger deterrent effect—and will therefore work faster to shape a culture of tax compliance—and it is vastly easier and cheaper to implement.\(^{61}\)

In his oral evidence to us, Tim Scott, Global Head of Tax at Glencore, stated that “I think this [automatic exchange of information] is a good idea, and something that we would have no problem with.”\(^{62}\)

40. Whilst the Government claims to support automatic exchange of information in principle, it has expressed some concerns about the possible burden on businesses and financial institutions, and around taxpayer confidentiality.\(^{63}\) The Exchequer Secretary to

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58 Foreign Account Tax Compliance Act (FATCA): Proposed Treasury Regulations §1.1471 - §1.1474, as published by PwC, February 2012, [www.pwc.com](http://www.pwc.com) - see section 1.1471-4(d)(3)(ii-iii)
60 Ev 75; Ev 122-125; Ev w28; Q 22; Q 89
61 Ev 124
62 Q 89
63 Q 223
the Treasury, Mr David Gauke MP, also suggested that the UK should wait for an international consensus to emerge rather than acting unilaterally, since the UK has “less of a tradition of extraterritorial impositions” than the US.\textsuperscript{64} In respect of the possible burden on businesses, meanwhile, the Government’s concerns appear to be unwarranted: large businesses such as Glencore and brewing giant SABMiller have no opposition to the policy.\textsuperscript{65}

41. The capacity of a developing country tax authority to obtain information on the offshore activities of its citizens or corporations (i.e. information from foreign tax authorities) is critical to its ability to curtail illicit capital flight. Their capacity to obtain such information could be greatly enhanced by legislative measures: the US Foreign Account Tax Compliance Act (FATCA) is a welcome start, but it only affects US citizens or corporations. We recommend that the Government introduce legislation similar to the relevant section of the US Foreign Account Tax Compliance Act (FATCA), requiring tax authorities automatically to exchange information relating to UK citizens or corporations. The Government should also use its influence (via the OECD Tax and Development Task Force, and similar avenues) to persuade other governments to follow suit.

\textbf{Tackling transfer pricing abuse}

42. In order to maximise the proportion of their profit occurring in tax havens, and to minimise that occurring in high-tax jurisdictions, corporations which form part of a corporate group may engage in transactions with other corporations in the same group. For example, in a group which includes corporations in Luxembourg and Ghana, transactions may be conducted between the corporations with the sole aim of maximising the taxable profits of the Luxembourg division, whilst reducing those of its Ghanaian counterpart. The potential for corporations to reduce their tax bills in this way is vast—60% of world trade is intra-group,\textsuperscript{66} and large corporations are generally able to hire the most skilled accountants to facilitate such ‘tax planning.’\textsuperscript{67} According to ActionAid estimates, payments to Switzerland, the Netherlands and Mauritius from SABMiller’s subsidiaries in Africa and India resulted in a total tax loss to governments in those countries of £20 million, enough to put 250,000 children in school, and equivalent in Africa to almost one-fifth of the company’s estimated tax bill.\textsuperscript{68}

43. Under present OECD rules, this practice is not in principle illegal, and of course corporations frequently transfer profits for reasons unrelated to tax. For example, the commonly accepted way for a business to reward shareholders is through declaring a reasonable dividend, but sometimes local rules make it very difficult to declare a dividend. In these cases, businesses may look for other solutions—such as profit shifting or

\textsuperscript{64} Q 224
\textsuperscript{65} Q 89; Q 91
\textsuperscript{66} Transfer Pricing Service: Unravelling the Opportunities and Risks, Deloitte, 2009, \url{www.deloitte.com}
\textsuperscript{67} Ev 91
\textsuperscript{68} Ev 58
unjustified management fees. We believe that the acceptable and transparent method for businesses to reward shareholders is through the declaration and payment of reasonable dividends. Host countries can contribute to this by establishing straightforward taxation regimes for dividends. We therefore suggest that DFID’s work for revenue authorities includes technical support in this area, where appropriate.

44. Under present OECD rules, the price charged in intra-group transactions must be the same as that which would have been charged if the goods/services had been sold externally, i.e. at ‘arm’s length’.69 However, a number of NGOs have campaigned vigorously for these rules to be made more stringent: Christian Aid claims that there are “substantial questions on both the practicality and applicability”70 of the present rules. One of the suggestions is a system of ‘formulary apportionment,’ whereby a corporation’s taxable profits would be allocated based on the proportions of total property, payroll or sales in each country.71 Given the current lack of support for such legislation within the OECD,72 however, we do not consider formulary apportionment to be a workable option at present—unlike certain other areas of legislation discussed in this report, transfer pricing legislation by definition requires international agreement in order to be effective.

45. However, it is claimed that even the present OECD rules are often broken, with intra-group transactions taking place at non-market rates. This is what we mean by ‘transfer pricing abuse’—a form of tax evasion. Global Financial Integrity claims that Zambia lost over $4billion (an amount similar to its total external debt) during the period 2003–09 due to transfer pricing abuse.73 A report by PwC Zambia states that:

In Zambia transfer pricing legislation exists. Section 97A of the Income Tax Act introduces the arm’s length principle.... The enforcement of the legislation by the ZRA has however not been as aggressive as expected.74

46. Corporations from which we took evidence, including SABMiller and Glencore, assured us that their intra-group transactions took place at ‘arm’s length’ prices—and hence complied with the OECD guidelines.75 Rio Tinto suggested to us that corporations should be required to demonstrate their compliance by publishing information on intra-group transactions on their annual tax returns in developing countries, as is already the case in many developed countries.76 Graham Mackay, the Chief Executive of SABMiller, claimed that his business did not seek to minimise tax through intra-group transactions at all: in other words, that it eschewed even those methods which the OECD guidelines

69 Ev w9
70 Ev 75
72 Q 213
73 Ev w27
74 Ev 81
75 Q 99; Q 100
76 Ev w76
permitted. However, in its subsequent submission of written evidence to the Committee, ActionAid casts some doubt on this assertion, claiming that:

‘... SABMiller states in its written evidence that it has centralised the administration of its intellectual property management and its management services. In doing so, it has moved many of the higher-value activities of its business out of developing countries and into low-tax jurisdictions (on paper, the Netherlands and Switzerland). Regardless of the motivation for this centralisation, it not only affects the global distribution of SABMiller’s tax liability, but also the extent to which its investments result in positive spillovers such as knowledge transfers and economic linkages in the local economy.’

47. In its written evidence, the CBI told us that businesses had made “a number of offers” to engage with HMRC and explain the approach they take to transfer pricing issues.

48. ‘Transfer pricing abuse’—corporations selling goods or services at non-market rates to other corporations in the same corporate group—can seriously undermine developing countries’ capacity to collect the taxes they are due. OECD rules prohibit this practice, but it is often difficult to detect when these rules are breached. To help developing country revenue authorities to tackle transfer pricing abuse, DFID should stress—in its dealings with these revenue authorities—the importance of requiring ‘related party transactions’ (i.e. transactions taking place within the same corporation) to be declared on annual tax returns.

49. In order to understand the perspective of multinational businesses on transfer pricing issues, HMRC should meet the CBI to discuss the issue. HMRC should also seek the views of trade unions and civil society organisations. HMRC should report back to the Committee before the end of 2012 to advise us of the outcome of these discussions.

Implications of UK Finance Bill 2012

50. In the 2012 Finance Bill, the Government proposed a relaxation of its anti-tax haven laws: the so-called ‘Controlled Foreign Companies’ (CFC) rules. If the Bill is approved as it currently stands, the newly relaxed legislation will apply to accounting periods beginning on or after 1 January 2013.

51. Under the current system, prior to these revisions coming into force, if a UK-owned corporation reports profits in jurisdictions with lower corporate tax rates than the UK, (such as by transacting with its own subsidiaries to shift its profits from developing countries into low-tax jurisdictions) the UK Government is able to impose an extra tax charge on the corporation to ‘make up the difference.’ Profits shifted from developing
countries into tax havens, therefore, would still incur tax at UK rates: this may disincentivise such profit-shifting.\(^81\)

52. Under the new system, the UK will only be able to impose this extra levy if the profits in question have been shifted from the UK. Profits shifted from developing countries into tax havens, therefore, will incur tax at the tax haven rate, rather than at the UK rate—so the incentive to shift profits into tax havens will be significantly higher.\(^82\) A number of NGOs are campaigning vigorously against this legislative change. As an example, ActionAid states its concern that:

> the proposals will eliminate a significant deterrent that discourages UK-based companies from shifting profits from developing countries to tax havens. We estimate that the reforms may cost developing countries as much as £4 billion.\(^83\)

53. The Exchequer Secretary to the Treasury told us that he did not accept the £4 billion estimate; however, he did not deny that there would be a cost to developing countries. He stressed that the objective of the CFC rules was to protect UK tax revenues, not those of developing countries.\(^84\) Given that through DFID the Government is also seeking to support revenue collection in developing countries, such a comment indicates a lack of joined-up thinking between Departments.

54. In a recent joint report by the IMF, OECD, UN and World Bank, it was argued that where domestic policy reforms were likely to impact on revenue flows to developing countries, a ‘spillover analysis’ should be conducted to ascertain the magnitude of such impacts.\(^85\) In the case of the revision to CFC rules, such an analysis has not been conducted.

55. If approved, the newly-relaxed Controlled Foreign Companies (CFC) rules, proposed in the 2012 Finance Bill and due to come into force in January 2013, will incentivise multinational corporations to shift profits into tax havens. This is likely to have a significant detrimental impact on the tax revenues of developing countries. **As a matter of urgency, the Government should conduct or commission an analysis of the likely financial impact of the revised Controlled Foreign Companies rules on developing countries. Depending on the results of this analysis, the Government should consider whether to drop its proposals.**

56. **The Government should designate a DFID ministerial responsibility for the development impact of tax and fiscal policy. Furthermore there should be an administrative or legislative requirement for the government to assess new primary and secondary UK tax legislation against its likely impact on poverty reduction and**

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81 “The problem with a new tax loophole”, ActionAid, [www.actionaid.org.uk](http://www.actionaid.org.uk)
82 “The problem with a new tax loophole”, ActionAid, [www.actionaid.org.uk](http://www.actionaid.org.uk)
83 Ev 61
84 Q 207
86 Ev 60-61
revenue-raising in developing countries, and to publish that assessment alongside the draft legislation.

**Role of Extractive Industries Transparency Initiative (EITI)**

57. The Extractive Industries Transparency Initiative (EITI) was established in 2002 by the then UK Government, with the aim of combating corruption in the extractive industries. The EITI is governed by a Board, whose membership includes governments, corporations and civil society organisations. It is currently chaired by the Rt Hon Clare Short.87

58. The principle underlying the EITI is that governments disclose the amounts they receive from corporations in the extractive sectors (including payments of taxes, signature bonuses and royalties), whilst corporations operating in participating countries make a corresponding disclosure of the payments they make to the government. An ‘EITI report’ for the relevant country is then published, which reconciles the amounts paid by corporations with the amounts received by the government.88 Any discrepancy between the two amounts may indicate revenues falling into the hands of corrupt officials.

59. There are two stages of EITI accreditation: EITI candidate status, and EITI compliant status. To achieve EITI candidate status, a country must comply with five specific sign-up requirements. To achieve EITI compliant status, a country must complete its first EITI report within 18 months,89 as well as fulfilling various other criteria pertaining to independent verification within two-and-a-half years.90 EITI compliant countries are re-assessed every five years to ensure continuing compliance.91

60. Despite its involvement in founding EITI, the UK has not yet sought EITI candidacy itself.92 The Parliamentary Under-Secretary of State argued that the UK was not sufficiently resource-rich to warrant participation.93 However, whilst the UK extractive sector is not as large as it once was, we believe it remains significant enough to warrant EITI participation: as at April 2012, mining and quarrying constitutes approximately 16.4% of total UK production.94

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87 Ev 121  
88 Ev 121  
90 “EITI countries”, Extractive Industries Transparency Initiative, [http://eiti.org/countries](http://eiti.org/countries)  
92 Ev 120-121  
93 Q 190  
Table 4: countries currently participating in EITI

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<thead>
<tr>
<th>Countries with EITI ‘compliant’ status</th>
<th>Countries with EITI ‘candidate’ status</th>
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<td>Azerbaijan</td>
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<td>Yemen (suspended)</td>
<td>Madagascar (suspended)</td>
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<td>Sierra Leone</td>
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<td>Togo</td>
<td>Trinidad &amp; Tobago</td>
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<td>Zambia</td>
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Data source: EITI website. In addition, several other countries – including the US – have indicated their intention to become EITI candidate countries.

61. However, EITI has a number of weaknesses. Given that figures are published on an absolute basis (rather than as a percentage of the relevant country’s GDP, or as a percentage of mining industry profits in the relevant country), it is difficult to draw international comparisons. Additionally, EITI does not require the publication of contracts between mining companies and governments: it has been suggested by the ‘Publish What You Pay’ campaign that such publication would help to expose any contracts which are patently disadvantageous to the country concerned.95 Examples might include those contracts signed by the Zambian Government in 2000.96

62. The Extractive Industries Transparency Initiative (EITI), founded in 2002 by the UK Government, has had a promising first decade. The process of creating an ‘EITI report,’ which reconciles what corporations say they pay (in taxes, royalties and signature bonuses) with what governments say they receive, is of great help in identifying possible corruption. Whilst the UK extractive sector is not as large as it once was, it remains significant enough to warrant EITI participation. If the Government genuinely hopes to encourage more developing countries to sign up for EITI, it must be willing to lead by example. Given that the UK was involved in founding the Extractive Industries Transparency Initiative (EITI), we feel that it should now become an EITI candidate itself. Additionally, the UK should encourage EITI to broaden its scope: EITI should require participating corporations and governments to publish the contracts which exist between them, and

96 In most countries, including Zambia, minerals are deemed to be the property of the government, until such point as a mining company buys ‘prospecting rights’ – i.e. the right to search for, and claim ownership of, mineral deposits. See Paul Collier, The Plundered Planet (London, 2010), p 51-52; and Robert F. Conrad, Zambia’s Mineral Fiscal Regime, in Adam, Collier & Gondwe (eds.), Zambia: Policies for Prosperity (Oxford, forthcoming).
should also require the publication of percentage figures in addition to absolute figures.

**Country-by-country reporting**

63. At present, international accounting standards do not require corporations to present financial information on a country-by-country basis.\(^{97}\) Such information can be presented on an aggregate basis. Many have advocated the implementation, by the International Accounting Standards Board (IASB), of a standard requiring country-by-country reporting.\(^{98}\) Christian Aid argues that:

> The potential for the private sector to drive development is vast, as DFID has recognised, but this can only provide real benefits for those living in poverty if the returns from the private sector are shared. Therefore, there is a clear need as DFID increasingly promotes private sector led development to also promote mechanisms by which the contribution of the private sector to development can be more effectively assessed, such as a Country-by-Country reporting standard.\(^{99}\)

64. More specifically, the European Network on Debt and Development (Eurodad) suggest that multinational corporations should be required to present the following items of information for each country in which they operate:

- the names of all the companies they own in each country;
- their financial performance in each country;
- their tax liability in each country;
- details of the cost price and carrying value of physical fixed assets in each country, and
- details of gross and net assets for each country.\(^{100}\)

65. The Parliamentary Under-Secretary of State for International Development assured us that he supported the passage of EU legislation requiring some degree of country-by-country reporting, but was unwilling to introduce such measures unilaterally if agreement within the EU was not reached, for fear of damaging the UK’s competitiveness.\(^{101}\) Evidence we received suggest that—if country-by-country reporting were to be mandated—the extra costs for businesses would be very modest.\(^{102}\) Mining companies such as Rio Tinto and Glencore do not oppose the measure (indeed, Rio Tinto already report much financial

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97 Ev w28
98 Ev w28; Ev w68
99 Ev 76
100 Exposing the lost billions: How financial transparency by multinationals on a country by country basis can aid development. Eurodad report, November 2011, [eurodad.org](http://eurodad.org)
101 Q 196
102 Q 130
information on a country-by-country basis voluntarily), whilst the Chair of the OECD’s Business and Industry Advisory Committee is also broadly supportive.

66. Requiring multinational corporations to report financial information on a country-by-country basis would constitute both a means of detecting tax avoidance and evasion, and a conspicuous deterrent. Given that corporations such as Rio Tinto already report financial information on a country-by-country basis voluntarily, we anticipate that others could follow suit at minimal inconvenience. Irrespective of whether EU-level agreement is reached, the Government should enact legislation requiring each UK-based multinational corporation to report its financial information on a country-by-country basis. Such information should include the names of all companies belonging to it and trading in each country, its financial performance in each country, its tax liability in each country, the cost and net book value of its fixed assets in each country, and details of its gross and net assets in each country. Additionally, the UK should continue to support the progress of similar legislation at EU level.
4 UK Government’s work on tax in developing countries

68. The previous chapter showed how UK policy choices impact on revenue collection in developing countries. In addition, the UK Government also has some more direct involvement with the tax affairs of developing countries. CDC, a development finance institution wholly owned by DFID, is closely affected by the tax policies of developing countries, since its investee companies operate in countries across the developing world. Additionally, both DFID and HMRC provide technical assistance to the national revenue authorities of developing countries. This chapter will examine each of these issues.

CDC

69. In our report on CDC, published last year, we recommended that when investing in tax havens, CDC should follow best practice guidelines, which were at that time being developed.\footnote{International Development Committee, Fifth Report of Session 2010-12, The Future of CDC, HC 607, para 60} The Parliamentary Under-Secretary of State for International Development informed us that there had been significant progress in this respect.\footnote{Q 194} We welcome this.

70. We also recommended that the tax payments made by CDC’s fund managers and investee companies should be published annually on a country-by-country basis.\footnote{International Development Committee, Fifth Report of Session 2010-12, The Future of CDC, HC 607, para 60} The Parliamentary Under-Secretary of State was non-committal when we asked him about this.\footnote{Q 196}

71. We re-iterate our earlier recommendation, made in our Report on CDC last year, that the tax payments made by CDC’s fund managers and investee companies should be published annually on a country-by-country basis. If certain fund managers or investee companies are unwilling to agree to this, CDC should use alternative companies which are willing to be more co-operative.

Technical assistance provided by DFID

72. DFID provides technical assistance to the national revenue authorities of developing countries, with a view to building their capacity and enhancing their ability to collect revenues. This is generally a demand-led process: assistance is provided in response to specific requests from developing countries. DFID spent around £97 million on helping to improve revenue collection between 2006–07 and 2010–11.\footnote{Ev 92}

73. Many of these projects have been extremely successful, As an example, DFID supported the Rwanda Revenue Authority over a 10-year period: supporting its foundation, and helping to organise its office building and management systems. Revenues
collected increased six-fold during the period of DFID support. DFID tells us that the Authority “reached a point where it was collecting the full £24 million value of DFID’s support programme every three weeks.”\footnote{Ev 92} The programme has also been praised by organisations including the Trade Union Congress (TUC) and the Chartered Institute of Taxation (CIOT).\footnote{Ev w9; Ev w86} We received a number of written submissions which argued that DFID should scale up its technical assistance work with revenue authorities, including a joint submission from the CBI, ActionAid and Christian Aid.\footnote{Ev 72}

74. In Zambia, DFID had a large-scale project providing technical assistance to the ZRA, beginning in 2000. This came to an end in 2006;\footnote{Ev 102} presently, the ZRA receives technical assistance from the Norwegian Agency for Development Cooperation (NORAD).\footnote{Ev 82} Since 2011, however, DFID has re-engaged with ZRA through the Public Expenditure Management and Financial Accountability (PEMFA) programme—a technical assistance programme funded jointly by multiple donors, and to which DFID is providing £2.2 million between 2011 and 2013. The programme is particularly concerned with improving administration at ZRA, with a view to improving the collection of non-mining tax, which has been in decline.\footnote{Ev 93; Ev 102} Additionally, DFID has contributed £200 000 to a separate pooled fund in support of the Ministry of Mines, with the aim of improving land registries (important for the issue of exploration licences), reviewing legislation, supporting EITI, and supporting the physical inspection of mineral exports.\footnote{Ev 110}

75. DFID’s technical assistance work with developing country revenue authorities has, by and large, been greatly successful. Its work in Rwanda, where it supported the revenue authority for its first decade of operation, is just one example. \textbf{We recommend that DFID scale up its technical assistance work with the national revenue authorities of developing countries.}

**Additional tax-related initiatives funded by DFID**

76. DFID is funding the International Centre for Tax and Development (ICTD), to the tune of £3.5 million until 2015;\footnote{Ev 94} additional funding is provided by NORAD.\footnote{Ev 90} DFID describes ICTD as a research institute which “will generate knowledge to help developing countries to mobilise domestic resources efficiently effectively and equitably, and develop tax systems that promote pro-poor economic growth and good governance.”\footnote{Ev 94}
77. Furthermore, DFID has supported the creation of the African Tax Administrators Forum (ATAF), an umbrella group of national revenue authorities from across Africa.\textsuperscript{120} The creation of ATAF is rightly seen as a positive step,\textsuperscript{121} and we commend DFID for providing support.

**Technical assistance provided by HMRC**

78. HM Revenue & Customs (HMRC) also supports projects to enhance the capacity of tax administrations in developing countries, delivering assistance on a bilateral basis and through multilateral forums.\textsuperscript{122} These may be funded by DFID, or in the case of smaller projects, from HMRC’s own budget.\textsuperscript{123} In either case, however, it is recorded as Official Development Assistance (ODA).\textsuperscript{124} HMRC told us that it had sufficient capacity to increase its work in this area, if DFID provided the funding.\textsuperscript{125}

79. Many organisations have stressed the importance of this work to us, including the CBI, RioTinto, Christian Aid, ICTD, and the Chair of the Business and Industry Advisory Committee to the OECD.\textsuperscript{126} In some cases, this assistance is even more successful than that provided by DFID, since HMRC understands the culture of revenue authorities,\textsuperscript{127} and is able to impart its own experience and understanding to its developing country counterparts.\textsuperscript{128}

80. Given its unique expertise, and its inherent understanding of the culture of revenue authorities, HMRC is an extremely important source of technical assistance for developing country revenue authorities. **We recommend that HMRC be provided with additional funding, to allow it to scale up its own technical assistance work with developing country revenue authorities.**

81. **The UK Government should improve its reporting on its technical assistance on tax and development, reporting cross-departmentally and at a project level on work in this area.**

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120 Ev 110  
121 Ev w9  
122 Ev 93  
123 Ev 120; Q 165  
124 Ev 120  
125 Q 214-215  
126 Ev 59; Ev 72; Ev 87; Ev 91; Ev w76  
127 Q 61.  
128 Ev w76
Conclusions and recommendations

Country-level tax policy

1. If developing countries are to improve their collection of tax revenues, it is imperative that elites within those countries pay the correct amounts in personal income taxation, and—critically—are seen to do so. (Paragraph 8)

2. DFID should seek to support the national revenue authorities of developing countries as they attempt to improve the collection of personal income taxes, VAT and local property taxes. DFID should also encourage and support programmes that engage civil society and trade organisations, academics, journalists and parliamentarians in the tax policymaking process. (Paragraph 13)

3. We urge DFID to stress—in its dealings with the national revenue authorities of developing countries—the importance of making corporate accounts available to the public. In Zambia, to test the allegations that the process is not working at present, DFID should request access to the accounts of some of Zambia’s main corporations, using channels available to the ordinary Zambian citizen. In its response to this report, the Government should notify us of the outcome of these requests. (Paragraph 25)

4. The Government should encourage the OECD and other standard-setting fora to require the filing of public statutory accounts in all jurisdictions. The Treasury should also press Crown Dependencies to meet these standards. (Paragraph 26)

5. DFID should support the governments of developing countries as they seek to incentivise hitherto unregistered enterprises to join the formal, taxpaying economy. (Paragraph 32)

Global Level tax Policy

6. We recommend that the Government introduce legislation similar to the relevant section of the US Foreign Account Tax Compliance Act (FATCA), requiring tax authorities automatically to exchange information relating to UK citizens or corporations. The Government should also use its influence (via the OECD Tax and Development Task Force, and similar avenues) to persuade other governments to follow suit. (Paragraph 41)

7. To help developing country revenue authorities to tackle transfer pricing abuse, DFID should stress—in its dealings with these revenue authorities—the importance of requiring ‘related party transactions’ (i.e. transactions taking place within the same corporation) to be declared on annual tax returns. (Paragraph 48)

8. In order to understand the perspective of multinational businesses on transfer pricing issues, HMRC should meet the CBI to discuss the issue. HMRC should also seek the views of trade unions and civil society organisations. HMRC should report back to the Committee before the end of 2012 to advise us of the outcome of these discussions. (Paragraph 49)
9. As a matter of urgency, the Government should conduct or commission an analysis of the likely financial impact of the revised Controlled Foreign Companies rules on developing countries. Depending on the results of this analysis, the Government should consider whether to drop its proposals. (Paragraph 55)

10. The Government should designate a DFID ministerial responsibility for the development impact of tax and fiscal policy. Furthermore there should be an administrative or legislative requirement for the government to assess new primary and secondary UK tax legislation against its likely impact on poverty reduction and revenue-raising in developing countries, and to publish that assessment alongside the draft legislation. (Paragraph 56)

11. Given that the UK was involved in founding the Extractive Industries Transparency Initiative (EITI), we feel that it should now become an EITI candidate itself. Additionally, the UK should encourage EITI to broaden its scope: EITI should require participating corporations and governments to publish the contracts which exist between them, and should also require the publication of percentage figures in addition to absolute figures. (Paragraph 62)

12. Irrespective of whether EU-level agreement is reached, the Government should enact legislation requiring each UK-based multinational corporation to report its financial information on a country-by-country basis. Such information should include the names of all companies belonging to it and trading in each country, its financial performance in each country, its tax liability in each country, the cost and net book value of its fixed assets in each country, and details of its gross and net assets in each country. Additionally, the UK should continue to support the progress of similar legislation at EU level. (Paragraph 66)

**UK Government’s work on tax in developing countries**

13. We re-iterate our earlier recommendation, made in our Report on CDC last year, that the tax payments made by CDC’s fund managers and investee companies should be published annually on a country-by-country basis. If certain fund managers or investee companies are unwilling to agree to this, CDC should use alternative companies which are willing to be more co-operative. (Paragraph 71)

14. We recommend that DFID scale up its technical assistance work with the national revenue authorities of developing countries. (Paragraph 75)

15. We recommend that HMRC be provided with additional funding, to allow it to scale up its own technical assistance work with developing country revenue authorities. (Paragraph 80)

16. The UK Government should improve its reporting on its technical assistance on tax and development, reporting cross-departmentally and at a project level on work in this area. (Paragraph 81)
Formal Minutes

Monday 16 July 2012

Members present:

Sir Malcolm Bruce, in the Chair

Hugh Bayley
Richard Burden
Richard Harrington

Mr Michael McCann
Fiona O’Donnell

Draft Report (Tax in Developing Countries: Increasing Resources for Development), proposed by the Chair, brought up and read.

 Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 81 read and agreed to.

Summary agreed to.

 Resolved, That the Report be the Fourth Report of the Committee to the House.

 Ordered, That the Chair make the Report to the House.

 Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

Written evidence was ordered to be reported to the House for printing with the Report, together with written evidence reported and ordered to be published on 22 and 28 February, 6 March and 24 April in the previous session of Parliament and 10 and 15 May, 13 and 26 June, 10 and 16 July.

[Adjourned till Wednesday 12 September at 10.00 am]
Witnesses

Tuesday 28 February 2012

Martin Hearson, Policy Adviser, Economic and Social Development Team, ActionAid UK, Joseph Stead, Senior Economic Justice Adviser, Christian Aid, and Savior Mwambwa, Executive Director, Centre for Trade Policy and Development

Professor Mick Moore, Professorial Fellow, Institute of Development Studies, Professor Tim Besley, School Professor of Economics and Political Science, London School of Economics, and Dr Jonathan Di John, Senior Lecturer, Department of Development Studies, School of Oriental and African Studies

Tuesday 24 April 2012

Tim Scott, Global Head of Tax, Glencore International plc, Emmanuel Mutati, Board Chairman, Mopani Copper Mines Plc, Graham Mackay, Chief Executive, SABMiller plc, and Christopher Lenon, Chairman, Tax and Fiscal Affairs Committee, Business and Advisory Committee to the Organisation for Economic Co-operation and Development

Eddie Rich, Deputy Head and Regional Director (Southern and Eastern Africa and the Middle East), Extractive Industries Transparency Initiative, Dr Odd-Helge Fjeldstad, Research Director, International Centre for Tax and Development, and John Christiensen, Director, Tax Justice Network

Tuesday 15 May 2012

Mr Stephen O’Brien MP, Parliamentary Under-Secretary of State, Department for International Development, Justine de Davila, Governance Adviser, DFID, Simon Whitfield, Policy Adviser, DFID, and Stephen Sharples, Senior Governance Adviser, DFID

David Gauke, Exchequer Secretary, HM Treasury, Steven Effingham, Deputy Director, International Tax Team, HM Treasury, Peter Steeds, Deputy Director, Head of Transfer Pricing, Business International, and Alison Shallard Brown, Head of International Relations, HM Revenue & Customs
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Oral evidence

Taken before the International Development Committee on Tuesday 28 February 2012

Members present:

Rt Hon Malcolm Bruce (Chair)

Hugh Bayley
Richard Burden
Mr Sam Gyimah
Pauline Latham
Jeremy Lefroy
Mr Michael McCann
Chris White

Examination of Witnesses


Q1 Chair: I bid you good morning and thank you for coming to give evidence. It is a slightly more formal engagement than last night, but it is good to see you here. Perhaps for the record you would first introduce yourselves.

Savior Mwambwa: My name is Savior Mwambwa and I am from Zambia. I work with a group called Centre for Trade Policy and Development on tax and development issues.

Joseph Stead: I am Joseph Stead. I am a senior economic justice adviser at Christian Aid.

Martin Hearson: I am Martin Hearson and I manage ActionAid UK’s Tax Justice campaign.

Q2 Chair: Thank you very much. This is the first evidence session of this inquiry, which is focusing on tax and development and how to raise revenue. We are looking in particular at mineral resources and the taxes that are or are not adequately levied on them, with Zambia being a case study. It is good to have you here to enlighten us, or indeed to direct us on the questions we should ask as we visit the country in a couple of weeks’ time. In your evidence you have tended to look at corporate taxation rather than other forms of taxation. Why do you think that is the higher priority? One can speculate that that may be where the capacity to collect tax is greater, but do you think it is right that corporate taxation is the main focus for increasing the revenue base in developing countries where there are significant corporate operations?

Martin Hearson: To clarify it, from the perspective of ActionAid there are a number of different priorities for developing countries of which corporate taxation is one. I think the question for us is: what is the priority for the UK Government? What is the value added for the UK, and what is the priority for you as a Committee looking at what DFID and the UK Government in general can do? In that area we felt it was important to make clear that, while there are many different things that DFID is doing, and can do, to support developing countries across the range of issues that need to be addressed—corporate taxation, individual taxation, administrative development and so on—there are many issues where policies elsewhere in Government, particularly the Treasury, have an impact in the area of corporate taxation. That is why we feel it is important for the Committee to look at that issue.

Savior Mwambwa: The Committee will be interested to know that, for countries like Zambia that are dominated by lots of foreign companies, lots of other non-tax benefits may come from such investment, but tax revenue is the most important one. By the very nature of the mining industry, it is not very integrated in the rest of the local economy. There are very few benefits in terms of employment and very little technology transfer, so for a Government like Zambia’s maximising tax revenue is the surest way to make sure that the benefits of such foreign investment are spread across the rest of the local people in the shortest possible time.

Q3 Chair: When we had a tele-briefing with DFID in Zambia last week they suggested that the situation had turned round in that country in recent years from a point where effectively the Government were subsidising the mining industries to the tune of about 4% of GDP. They are now getting a revenue base out of mining of about the same amount, so that is a turnaround of about 8%, which is obviously in the right direction. First, is that a fair summary of your understanding? Second, what is the potential for them to go further down that route? Is there scope to get more taxes out of the mining sector in Zambia?

Savior Mwambwa: It is true that the new Government have put in place very specific, positive steps to try to redress the situation, not only to increase tax rates but to deal with some of the regulations around the agreements between the mining companies and the Government, but, if you compare it with the potential revenue the Government can raise, there is still a long way to go. A lot of constraints face the country, especially the Government, which have to deal not only with the existing structure rules in Zambia but also the international system around that. There is definitely a lot of political commitment by the new Government to try to turn round the situation.

Chair: To put that in context, this is our first evidence session. We will be visiting Zambia and, as it happens, Malawi, and we will be taking further evidence when
we get back. We are hoping to be better informed to ask questions, particularly of British companies and their accountability, so anything you can say on that front will be helpful to us.

Q4 Jeremy Lefroy: I should declare an interest, in that I lived in Tanzania for 11 years and have been involved in business, corporate taxation and so on. While absolutely recognising the importance of corporate taxation issues, do you agree that personal income taxes, particularly those of the wealthy elite in many of these countries, are also a major issue? I was extremely concerned about the lack of income tax collected from people living in those countries who were extremely wealthy, whether nationals or expatriates. It is absolutely right to focus on corporate taxation issues, but I think we should cast the net a bit wider. Do you agree?

Savior Mwambwa: I cannot speak for Tanzania, but definitely for Zambia. I agree it is very important, but, if you look at the facts, it is quite clear that in Zambia income tax forms the biggest proportion of Government revenue compared with corporate tax. The mining companies in proportionate terms contribute far less to Government revenue. I agree with you, but that is not the case in Zambia. What we are trying to say is that more can be done by the international community—countries like the UK—and our own Government to have a proportionate balance.

Q5 Chair: Is there an issue of administration? Clearly, the people Mr Lefroy is talking about, who would be high earners paying tax—the elite—are one thing, but, if you go down the scale, I would guess that the administration of trying to collect a small amount of tax from relatively low earners could be quite burdensome in a developing country. Is it better to try to get those taxes in the form of VAT or indirect taxation that people pay on their transactions, and concentrate income tax on the higher end of the income scale?

Joseph Stead: First, there are some concerns about trying to go too far down the indirect tax route, because there are issues about how progressive that may be. Certainly, VAT can be very regressive in terms of putting high cost on very low income earners.

To come back to the point about personal income taxes, we accept that it is an area in which action needs to be taken. The way we have structured our submission is that, in addition to looking at corporate income tax, we have stressed the international financial system and the way that the structure of secrecy jurisdictions allows large amounts of capital flight. A lot of that is personal incomes. The fact that we have secrecy jurisdictions that allow that to be hidden from view creates a problem for personal income taxation. We think the UK can bring value to this by taking action to reduce the levels of secrecy globally, and that will provide the information that will allow developing countries to improve their efforts in collecting income tax. You have a situation where Africa is a net creditor to the rest of the world due to the amount of money flowing out from the continent. That is where we see the UK’s role in tackling that.

Martin Heanson: That is absolutely right. Many of the solutions that we advocate in terms of corporate taxation, particularly information exchange agreements, better coverage of those and a more effective mechanism to make that work, would also be a benefit in tackling high earners.

As to your point about going down the income scale, one of the things we are concerned about as NGOs is that there are moves to try to bring the informal sector into the tax system. That is something we encourage, because it means more people will have a stake in the fiscal contract, and ultimately more tax revenue is raised, but it has to be done in a way that is perceived to be fair. As these efforts take place in developing countries, insufficient analysis is being made, as happens here, of the impact on different income groups, for example by gender, of different tax measures. In looking at the question you ask, which is very important, I think more work needs to be done, which could be supported by DFID, to help developing countries do the kind of analysis we do here.

Q6 Pauline Latham: In terms of people working for NGOs in different countries, where do they pay tax? If somebody is working for ActionAid, Save the Children or Oxfam but they are working permanently in Zambia, or as permanently as anybody in any job, where would they pay their tax?

Savior Mwambwa: I worked for a British charity, WaterAid, in Zambia. I think the case may be true of other similar groups. You pay tax to the Zambia Revenue Authority, unless in the beginning when the organisation is setting up you apply for tax exemption, which is given in certain circumstances mostly for humanitarian organisations. I think that those who pay income tax, like my NGO and others, would pay it to the Revenue Authority.

Q7 Pauline Latham: So British people who are sent out there would pay tax in Zambia.

Savior Mwambwa: I do not know about British people.

Q8 Pauline Latham: I am talking about people whose origin is in Britain. Obviously, if you are a Zambian you will pay tax in Zambia, but I am talking about NGOs who send people from Britain to work out there. Where do they pay their taxes?

Martin Heanson: For ActionAid the vast majority of our staff working in a particular country are locals who are employed locally and pay taxes locally.

Q9 Pauline Latham: That is the vast majority. What about the minority?

Martin Heanson: As to that minority, we have some expat staff, and international tax rules define where your tax liability arises. It depends on from where you are earning it. Tax treaties will state the definition whereby your tax liability arises either in, say, Zambia or the UK if you are an expat. It is not up to us; it is defined by international tax rules.
Q10 Pauline Latham: So there are quite a few British NGOs working abroad who pay tax here and not in the country they are working.

Martin Heasron: There is a small minority of NGO staff working in developing countries who may pay tax here.

Q11 Mr Gyimah: Moving to transfer pricing, which features quite prominently in your written submissions, can you briefly outline why you consider this issue to be so crucial?

Savior Mwambwa: Speaking from the Zambian perspective, I could give many concrete examples. Existing rules on transfer pricing make it very difficult for Government authorities in a country like Zambia to prevent the tax avoidance practices that companies undertake. A specific example in Zambia is one of the Glencore subsidiaries—just one company—which is believed to have avoided paying at least $50 million over two or three years, partly because it tried to manipulate the transfer pricing rules. That happened in spite of the existence of such rules in Zambia, but also current international rules like those of the OECD are insufficient to tackle that. It can get complicated for a poor country like Zambia whose authorities are short-staffed to police such rules. I think more can be done to have alternative mechanisms to create a disincentive for companies to do this.

Joseph Stead: The reason we see it as a key issue is that it is a global problem; all countries struggle with this, but it is especially marked in poor developing countries. The estimates of losses are huge. Christian Aid’s research into transfer pricing and false invoicing estimates lost revenue of $160 billion every year. One of the main problems is that at the minute a set of rules devised through the OECD works to some degree, not perfectly, for developed countries, but as it is applied to developing countries it is proving very difficult to get it to work effectively. There is a complex set of guidelines that does not necessarily fit the capacity or nature of the economies in developing countries to work adequately, and developing countries do not have a voice in how the rules are being developed. The OECD guidelines are formed by the developed countries, and that is an arena in which developing countries are not able to contribute. They are not members of the OECD and so it becomes very difficult for progress to be made to get those rules to work for developing countries. I think that is the nub of the concern.

Martin Heasron: You had a written submission from the African Tax Administration Forum, which brings together 35 tax authorities across Africa. It is an impressive organisation that is doing great work to try to build capacity on the continent. I have had the opportunity to talk to them quite a few times. One of the things to which they draw attention is that this is a particular area they will not be able to tackle without a combination of simplified or revised international rules and capacity building. As Joe says, it is a perfect example of an area where the UK, not just as an aid donor but also as a player in the international tax system, has an important role.

Savior Mwambwa: We filed an OECD complaint in 2010 regarding the Glencore case with a Swiss national contact point. They opened a formal inquiry but it could not go further because Glencore refused to co-operate. Given the nature of the way these things are designed—for example, they are voluntary, not binding—they do little or nothing to deter companies from engaging in that. The rules or even the mechanisms to seek recourse could be there, but in reality they are ineffective. There is a need to look at it again critically and reform existing mechanisms.

Q12 Mr Gyimah: Which is more important: strengthening transfer pricing or enforcing existing legislation?

Savior Mwambwa: I think it is both; it is not a question of either/or. You can enforce something only if it is proven to be effective in the first place. I think we have first to look at the design. Is what is in existence appropriate and effective? If not, what sort of reform do we need? Then we can look at the second step of enforcing much more effective rules.

Q13 Jeremy Lefroy: I entirely accept the point about transfer mispricing but would like to give a couple of examples. When I was involved in coffee in Tanzania, as an association we, together with the Tanzanian Government, introduced a scheme whereby coffee exports were measured against market prices, and it could not be exported without meeting those market prices. I thought that was a good scheme, but it was discontinued. I do not know whether it was discontinued because of pressure from the industry—I do not think so—but the Government could have continued with such a scheme but chose not to. That was a classic example of a good mechanism that was available but was not working. In another case I remember looking at some official statistics and seeing an incredible example of what I believed to be the blatant under-pricing of a particular commodity. I raised it with the official body in the country concerned; I wrote to them. Nothing was done about it. Do you not think this is a two-way thing? It is not just about companies that are always desperately trying to get away with things; it is about Governments and trade associations, or whatever, working together to come up with something that is transparent, workable and market-related. It takes both sides to do that, and in some cases there seems to be a lack of willingness on the side of Governments as well as the international business community.

Savior Mwambwa: Absolutely. There are things that are very much in the remit of national Governments, and also issues of political commitment. That is why, for example, we advocate transparency in terms of transactions in which companies engage across borders, or country by country. That would also help to deal with governance issues to do with corruption and the secrecy surrounding that. I agree with you, but there could be a much more effective way of unravelling these kinds of relationships if, for example, we go for the basic principles around transparency, especially for companies that work across borders. If there is a reference price, with internal trading and everything else, it is still very complicated if you do not shine the light of
transparency on what is going on, even for Governments.

**Martin Hearson:** Certainly, the atmosphere in Africa has changed over the last few years. There is a strong willingness among revenue authorities, and in many cases Governments, in African countries to build capacity to deal with transfer pricing. That is why it is one of the main priorities for the African Tax Administration Forum. In many cases they are hamstrung by the fact they are told by donors they must use the existing international standards; there is no room to negotiate or change them.

So, in the kinds of discussions you are talking about, they are often discouraged from going down that route, which is the one Brazil has pursued. Brazil has its own tailored transfer pricing regime, which it has developed in consultation with business, based on market rates, and it is a much simplified approach. But other countries are actively discouraged by donor organisations, and in many cases by the Treasury here, from pursuing the same course.

You are right. That is precisely why the current transfer pricing rules are an obstacle rather than a solution. India has the biggest tax authority in the world. It has never won a single transfer pricing case that has gone to court; it has always lost. That is because the rules make it so hard for a tax authority challenging a multinational company to build a solid case.

**Q14 Mr McCann:** I have two questions for Joseph. First, in your written evidence you set out your objections to the controlled foreign companies rules. Can you explain to us exactly what your objections are to the rules?

**Joseph Stead:** I can. Possibly I should defer to ActionAid because they have done more of the research than I have. In fairness to Martin, I should let ActionAid take credit for some of this.

**Martin Hearson:** It is useful to set it in the context of a report produced last year in the run-up to the G20 summit in Cannes by the IMF, the OECD, the World Bank and the UN. The G20 asked them to come up with some recommendations for things they should do on tax and development. One thing they said was that in certain cases tax policy changes in G20 countries could have spill-over effects on developing countries. As an example, they said that effectively the controlled foreign company rules had the potential negatively to impact on developing countries. They recommended that Governments should conduct a spill-over analysis, which is to understand in as much detail as possible how this might impact developing countries and then think about steps to take to mitigate it either by legislation or capacity-building work. The Treasury refuses to do that, so we still do not have that analysis for the UK despite that recommendation from those key international economic advisers.

Our key concern is what the changes to the existing rules will do. To explain what they do, the CFC rules discourage the shifting of profits from the UK, or any other jurisdiction, into a tax haven because they impose UK tax rates on a tax haven company that is owned by a British company. So, if I have a subsidiary in Jersey and another in Ghana, and try to move my profits from Ghana to Jersey to get the tax liability in Jersey, the UK will impose the UK tax rate on the Jersey company. Therefore, it discourages me from doing that. Under the changes to the rules that will no longer apply unless I am shifting profits from the UK into the tax haven. If I am shifting it from any other country, such as a developing country, that will no longer apply, which means it is much more advantageous for me as a multinational company to shift my profits out of a developing country and into a tax haven. Because developing countries are at a much earlier stage of developing their legislation and administration, they are much less protected from those kinds of activities than developed countries.

**Mr McCann:** That is extremely clear.

**Joseph Stead:** We have asked the Treasury why they are unwilling to do such an impact assessment following the report to which Martin referred. The answer we still get back from the Treasury is that these rules are designed to look solely at the impact on UK tax revenue. That is the concern we have with the Treasury and why we believe they are not thinking about the impact on development of any of their policies. While the Treasury's main focus will always be on the UK, we strongly believe—this is supported by the IMF, the World Bank, the OECD and the UN—that they need to look at the impact that UK policy can have on developing countries. It may not be the primary focus but they need to think what the impact will be, and we just do not see that. That is why we would like a Committee like this to ask those questions of Treasury, because so far we do not feel we have had satisfactory answers from them.

**Q15 Chair:** Is your assessment that the end result is that less tax is being paid overall, or that the tax is being paid but not to the benefit of the developing country in which the operation is taking place?

**Martin Hearson:** In the changes proposed in the budget, less tax would be paid both in developing countries and in the UK, so the changes have an impact both in the UK and developing countries. We think the impact is more significant in developing countries, but it would reduce overall the tax liability of companies.

**Q16 Mr McCann:** I have another question for Christian Aid, which I think you will be able to answer. Christian Aid have estimated the capital flight from developing countries to be $160 billion, but a number of organisations question that figure. How did you arrive at it?

**Joseph Stead:** It is not the capital flight; that is the lost revenue as a result of tax evasion. I can go through that if you want. We did address this before the Committee back in March 2009. I do not know whether you want to go back to that.

**Q17 Mr McCann:** Has it changed, or is it just the same?

**Joseph Stead:** It is the same explanation. I know there has been reference in other submissions to a report published that questioned our analysis on the basis that we had not gone down to a low enough level on
the trade data. We had a discussion with the author of that report. They accepted we had done more than they assumed. We can provide you with further written evidence of exactly why that attack on our report was flawed, and the details of the conversations we had with the author, which said that their criticisms were not valid in the way they claimed.

Q18 Mr McCann: Can we get that information?  
Joseph Stead: We will send that to you in writing.

Savior Mwambwa: Perhaps it is not surprising you do not have one agreed figure. By the very nature of the issues themselves, when investigating tax avoidance there is secrecy, so it is very difficult to get accurate figures. To illustrate it with an example, a few weeks ago the Zambian Minister of Mines announced that the Zambian government audited the gold industry as it was the biggest overseas investor in the Zambian economy and it was resulted that the Zambian government was losing $100 million in tax avoidance. So, whether it is $100 million or $50 million, you can contrast clearly the proportion of forgone income with, for example, DFID’s budget support to the Zambian Government.

Q19 Chair: The implication behind that is that DFID would be better occupied helping the Zambian authorities to collect taxes rather than handing over aid money.

Savior Mwambwa: One of the things is to build capacity, but you will not solve the entirety of the problem by that means. If we are arguing about figures, whether it is 10 million or 20 million, our own Government recognises this as a very big problem and one of the areas they need to deal with to close a major loophole, but they need support. A lot of the problem is not really about the local structure but the way the international network of systems and rules is designed. There is no question about the extent of the loss; it is in huge proportions, whether it is in Zambia or the rest of the developed countries.

Joseph Stead: The estimates come from looking at macro level statistics. We put all that together. It is not just Christian Aid; others have made the same estimate. Transfer mispricing appears to be a huge problem. Companies come back and say there is no evidence at the micro level in individual companies. We would love to be able to provide that evidence, but getting access to the information to do that is very difficult. Because of the way companies report and the information to which we have access, being able to find and then publish transfer pricing problems and things like that is very difficult.

We have been trying to do research into the transfer pricing of cobalt from the DRC to Finland. From the external evidence it appears that cobalt is being sold by GTL, which is the company in charge of selling this cobalt in Congo—it is based in Jersey, so you cannot get access to any of the company accounts—to Finland, where one of the joint venture partners has a huge cobalt smelter. From the external evidence, it looks as though there is a huge problem of underpricing of that cobalt to the tune of about $4 billion over 10 years, but because we do not have access to the accounts and we are unable to gain access to the information, there remain unanswered questions. We cannot get any resolution to take it any further. The companies challenge us and say, “This is not the situation as we understand it. Where are your concrete examples of it?” Because of the way systems and accounting are set up, it is very difficult to get access to that information and provide micro-level examples to support our macro-level figures.

Q20 Jeremy Lefroy: To put a quick definitional question, what would you define as a tax haven? Is the Republic of Ireland a tax haven, charging 10%?  
Savior Mwambwa: From my perspective, it is not so much about the tax rate that exists but the secrecy a jurisdiction affords to the information, basically offering advantageous tax preferences. I think the common characteristic is secrecy, which is also backed by the legal protection of the authorities. One country could have a proportion of it with those characteristics. For example, the City of London is listed as a tax haven, in spite of counter-intuitive factors.

Martin Hearson: I think the definitional point is less relevant than the properties of a particular jurisdiction. Ireland, for example, has a 10% tax rate and no CFC regime. The dismantling of our controlled foreign company regime that we are doing is exactly what Ireland has already done. There are some characteristics that mean it is possible for a company to use that jurisdiction to avoid or evade tax in other countries. The same would apply to the Netherlands, for example. Various characteristics about the way it treats intellectual property, for example, make it very attractive. It does not generally appear on the list of tax havens and it is not particularly secret, but it has tax policies that are problematic. Then you have secrecy jurisdictions. Secrecy is an additional problem to low tax rates.

Q21 Jeremy Lefroy: What I am trying to get at is that pretty much every developed country I can think of could be described as a tax haven in one way or another, or has a very close relationship with one. France has Monaco or Andorra; the UK has the Channel Islands. It is very difficult to find a developed country that does not have one way or another of enabling people substantially to reduce taxes on corporate profits.

Martin Hearson: That is why we would go back to the recommendation made by the IMF, the OECD, the World Bank and the UN last year, which was that G20 countries should assess the impact of their tax regimes. They said that, first, you should do a baseline analysis and look at the entirety of your tax regime and the characteristics of it that may have negative impacts on developing countries before looking at changes to it. I think all countries—Ireland, the Netherlands, the US and UK—should be doing that kind of analysis to understand how their tax regime has a negative impact on developing countries; otherwise, all those countries are supporting capacity-building work in developing countries to help them build tax administration capacity, but it is poor value for them if, on the one hand, they are doing that and,
on the other hand, their tax regimes undermine that effort.

**Q22 Jeremy Lefroy:** You are advocating the automatic exchange of information between tax authorities. What kind of information do you think should be exchanged?

**Martin Hearson:** I will give you an example from our work of the kind of case in which I think it would be useful. We published a report in 2010 on SABMiller, the brewing company, in which we uncovered a number of cases of what appeared to be strong evidence of transfer pricing abuses. There is some debate about whether this was tax avoidance or was closer to tax evasion; that is, whether it was non-arm’s length pricing or just a very clever use of that regime.

The revenue authorities of the African countries involved in that report, including Zambia, met and wanted to be able to discuss that report and consider a joint audit of the company. They were unable to do so because they did not have the legal treaty framework to permit them to discuss the affairs of one taxpayer in another jurisdiction. As part of the research I visited the site in Switzerland, which gave the report some additional colour. When I had a chat with some of their revenue officials, they said that was something they could never do, because in many cases they did not have access to the information they needed. If they were auditing one subsidiary of a multinational, they did not have the full financial information about another subsidiary. Those are two examples.

To me, the more important point is that you need a multilateral treaty framework. Within it you need some information that is exchanged on request and some that is exchanged automatically in order to make best use of that, but the first stage is to get to the point of having a multilateral treaty framework. Africa is going ahead with that; it is developing its own treaty framework. A number of countries in Africa are also joining the global treaty that has recently been created. Africa is moving ahead on this and it needs more support from the UK.

**Joseph Stead:** Looking at UK policy, it seems that we are actively moving away from that. Martin says that what is needed is something that is multilateral and an automatic exchange. When we see what the UK has done in terms of the deal it has signed with Switzerland, that is not an automatic exchange; at best it is on request, a limited number of requests can be made, and it is not multilateral; indeed, it is undermining the efforts that are being made to put multilateral pressure on Switzerland. It seems that the deals done by the UK and Germany may scupper attempts by the EU in its savings directive to get a European deal to force automatic information exchange with Switzerland.

We see calls from other countries for automatic information exchange with Switzerland. America, through its FACTA regulations, is looking at trying to get automatic information exchange through banks; India has made it clear that it sees automatic information exchange with Switzerland as very important, yet the UK is actively undermining this by the deals it is signing with Switzerland. We believe UK policy could be much more proactive in this area and support those multilateral approaches towards automatic information exchange that, as Martin says, Africa desperately needs. At the minute, the economic power of African countries is not enough to bring to bear on Switzerland to get access to information that is needed. If the UK with other economically powerful countries makes it clear to Switzerland that they have to do this, I think we can finally break Swiss banking secrecy.

**Savior Mwambwa:** In the case of Zambia, for example, if we had such a mechanism in place with the automatic exchange of information, probably Glencore would not have engaged in the activities they did in relation to transfer pricing, management services in Mauritius, freight cost in the Netherlands and so on. I think it can also serve as a deterrent to companies that sooner or later the authorities will catch up with them.

**Q23 Pauline Latham:** Following on from automatic exchanges of information, would country-by-country reporting add anything extra?

**Joseph Stead:** Yes, I believe it would. Country-by-country reporting would do several things. It would help to restore trust and understanding of exactly what role multinational corporations are playing in the various societies and countries in which they are operating. There is a clear demand for people to understand exactly what a company is doing in every country where it is operating, so it would help with that. It would also make it much easier for revenue authorities in developing countries to identify where potential abuse of the tax system may be happening and thus be able to identify clearly where to focus their attentions and audit.

It would also help in the long-term process of being able to have a better understanding of exactly how multinationals work, and international taxation operates. I think that to provide more data in an easier and more accessible format would allow a wider range of people to engage and take the debate forward; it would certainly help those in developing countries to formulate stronger policies and positions. If that is combined with efforts that are desperately needed to create greater spaces and opportunities around the world, as the OECD and strengthening the role of the UN in this, developing countries will then have a much more powerful and meaningful say in exactly how we get international tax rules and norms that work for all countries.

**Savior Mwambwa:** I think it promotes the kind of co-operation among countries in the region that we see, for example, with Sadiq Petroleum and Tricontinental Oil. Zambia and the DRC could cooperate more and more if there was country-by-country reporting. They could come up with common regional tax codes or co-operation, which would also help to prevent big companies playing one country off another. In most cases I think competition should not be among countries but among companies, but currently countries compete to have the lowest tax rates because companies are able to use the lack of information in one country to play one country off another. We need to flip that. Companies should be
able to compete and say, “Zambia can offer the highest tax returns from investment compared with this country,” and not the other way round. Therefore, country-by-country reporting would make it easier for Governments in the region to co-operate rather than compete.

**Q24 Pauline Latham:** Do you not think that might impose a financial burden on individual companies, and therefore it would disincentivise their investment in individual countries?

**Savior Mwambwa:** I think the cost of that is marginal compared with the gains that would come. Market information is one of the factors that can lead to efficiency. The problem with the current system is that only a few companies take advantage of that, so it is not a level playing field, but once you have country-by-country reporting it will lead to more transparency and access to information, the gains from which would far outweigh any costs of doing that.

**Q25 Pauline Latham:** You talked about Zambia working with DRC. Is that a reality, because individual countries might not necessarily relate terribly well to each other?

**Savior Mwambwa:** Because of the current system of secrecy, they feel they have to compete with each other, but not once they are sure there is more gain to be had from co-operating. A lot of things are happening. At AU level, a few days ago a high-level panel of experts led by Thabo Mbeki was set up to promote these kinds of issues. We also have the Africa Mining Vision, which has emphasised the need for that kind of co-operation. In Zambia the new President, Michael Sata, won the election on the fight against corruption and the need to get the most from tax revenue from mining. Already you can see these changes happening within African Governments themselves, so there is enough political drive and appetite. That is building, and it needs to be supported.

**Q26 Mr Gyimah:** To go back to the comment you made a few minutes ago about countries not competing on tax rates, I am not sure I understand fully what you mean. Are you saying they should all have the same tax rate?

**Savior Mwambwa:** Not necessarily the tax rate. For example, the structure as it is now is that Glencore can come to Zambia and say, “I want a mining licence, but in order for me to invest in your mining sector you give me X concessions or tax rates. If you don’t, I’ll go to DRC because there I will get the following.” That need not be the case.

**Q27 Mr Gyimah:** Are those concessions corporate tax rates?

**Savior Mwambwa:** It is a range. They might include tax rates but they may include other things like tax breaks or electricity subsidy for example, but as long as it is done in secrecy it is not easy for one country to know what the other country is offering. The Government of Zambia needs to sit in some formal setting with DRC and say, “What are the basics, the minimum and the principles about how we deal with multinational companies?” I am not saying they should have the tax rate, but that they could agree on similar things and have transparency. That would help them increase their bargaining and negotiating power with the companies, because transparency is one of the biggest tools countries can have against multinational companies.

**Q28 Jeremy Lefroy:** Given that the Chinese are by far the biggest buyers of some of these minerals and commodities around the world, are you pressing the same case you make here on the Chinese Government?

**Martin Hearson:** In terms of country-by-country reporting, we are calling for an international financial reporting standard, which would apply across the vast majority of countries in the world.

**Q29 Jeremy Lefroy:** Including China?

**Martin Hearson:** I am not sure on that factual point. I do not want to say one way or the other, but I know that the general move is towards convergence. For example, the US and India are now starting to adopt those standards, but the primary vehicle we have been advocating up to now has been the G20, which incorporates China. It is an interesting discussion, because back in 2009 at the London summit, when the issue of tax havens first came up one of the difficulties was that it was not just the UK that had its associated tax havens. China has Macau and Hong Kong as well. There was quite difficult negotiation there. We think it is very important that on a lot of these issues there is movement at global level, because it is at that level you can deal with the kind of issue you are raising. We as NGOs have difficulty influencing a country like China. That is what we have been calling for.

We have been pushing for country-by-country reporting, because we recognise that there is work to do on cost-benefit analysis and that it is not yet a finished proposal. That work has been taken forward by an OECD task force, which incorporates OECD member states but also developing countries and tax haven countries and a whole variety of stakeholders. That task force was set up by the OECD after pressure was exerted by the previous UK Government. It is a little disappointing that under the current Administration there seems to be much less enthusiasm for that work at an international level on tax justice, which is a shame, because real progress is being made to assess, by country-by-country reporting, the cost and benefits to work out what further research needs to be done.

**Q30 Jeremy Lefroy:** To challenge you on that, I have not come across anything that would indicate that this Government is less keen on that than the previous one. Are you able to give us some evidence of it?

**Martin Hearson:** Sure. This task force was established in 2009 under the auspices of the OECD. It has a number of working groups. One of those working groups looks at country-by-country reporting; another looks at transfer pricing; another looks at information exchange. Each of those working groups has a number of members from OECD
Governments, NGOs, businesses and so on. When the task force was proposed, the Minister at the time, Stephen Timms, spoke up and put some funding in. They pressed the OECD to initiate this. They were very vocal and present at ministerial level at some of the meetings. Since the change of Government, often the one civil servant in DFID who has this brief is either not there or does not speak. I hear from people who are more engaged in the secretariat that, whereas under the previous Government it was felt the UK was the driving force behind the work on tax and development in the OECD, now it is not clear.

Q31 Chair: Which Government Department are we talking about?

Martin Hearson: This is precisely our point. DFID has had this relationship, although in the previous Government it was Stephen Timms, the Treasury Minister. David Gauke, Mr Timms’s replacement, would be in a position to engage much more in the OECD’s work than he has been doing currently.

Q32 Chair: Maybe we should follow that up, Mr Hearson.

Martin Hearson: We think that would be a really positive thing to do.

Q33 Jeremy Lefroy: We should ask David Gauke about it and allow him the right of reply to that charge, which is quite a serious one you are making. Would you acknowledge that, under the current Government—I am not saying the previous Government were not doing it—DFID are placing a great deal of emphasis on local revenue collection through things like the Trade Mark East Africa developments, which have substantially increased revenue collection in Burundi, for instance, and take both local and cross-border revenue collection very seriously?

Martin Hearson: In our preparation for this inquiry, way before we were asked for evidence, we made a submission—we did not use FOI—requesting a summary of all of the work that DFID was doing to support capacity building in developing countries. That was in August, and it took until the deadline you set for submissions for that information to be gathered. We understand that is because up to now there has been no centralised approach to the work that is done on tax and development. There are some very positive and successful isolated examples, but there is not a strategic approach. That is not just across DFID; it needs to be across the whole of Government. HMRC does a whole range of work as well, some DFID-funded and some entirely on its own initiative, to support capacity building. There are examples of things begun under the new Government. One of the really positive ones is the research centre, and in a few minutes you are to hear from Mick Moore, who leads that. That is a really great thing that has been done. But what is missing is a strategic approach that understands where DFID’s resources are best devoted to support the work that the African continent is already doing and is crying out for support, and where the rest of Government needs to look at its own policies.

Joseph Stead: We see some of the great stuff DFID does in this area, but it does not seem as though it adds up to a whole, so it is a matter of seeing that cohesiveness within DFID and, as Martin says, the idea that this project is shared across Government. In his Beyond Aid speech, Andrew Mitchell made it very clear that he saw part of DFID’s role to make the case for development across Government and ensure that other Government Departments saw themselves as having a role in development. We do not see that happening in this area, especially when the Treasury is such a key player. We need to see that. It is vital to make sure the Government deliver on this agenda; that the good stuff they do can be scaled up and communicated; that it fits in with the great efforts made in revenue collection in developing countries; and that a change in UK tax policy, or an approach in international fora, does not undermine the work being done by allowing further tax abuse to happen in another area.

Q34 Hugh Bayley: I would like to begin with a question to Mr Mwambwa. You talked about hundreds of millions of dollars in revenue forgone by the Zambia Revenue Authority. As a committee we are focused on the impact that UK policy can have on poverty reduction, for example as measured by the millennium development goals. Are you able to give us any feel in terms of poverty reduction how much $100 million of aid is capable of buying in Zambia compared with $100 million of additional revenue raised by the Revenue Authority? Of course, aid comes with conditionality; it might be earmarked for, say, schoolteachers’ salaries, whereas general Revenue Authority money is spent in the ways that the Government of Zambia think best.

Savior Mwambwa: As you are aware, apart from the European Union, which is the biggest provider of budget aid to Zambia, DFID itself has been providing aid to Zambia for a couple of years. Recent statistics from the Central Statistics Office in Zambia show that in spite of that poverty levels have not reduced. That is against the backdrop of previous dependency on aid. In this year’s budget at least the proportion of local revenue is about 70%, and it is estimated that 20% is aid money. Over the last five years Zambia has seen a sharp reduction in the amount of aid dependency. Of course, it is good that our country has become less dependent on aid, but what increased tax revenue will do is also strengthen local accountability and the ability of citizens to hold Governments to account. It also helps to deal with corruption. There are qualitative values in increasing tax revenue, aside from the resource utilisation aspects of it. The normal argument would be that maybe the advantage of aid over taxes is that donors have control over how it is used, but in terms of the actual impact that you want to have, it is quite clear that no amount of aid would substitute the country’s own ability to generate local resources because of all the other benefits that come from that.

Q35 Hugh Bayley: Perhaps I may ask one of you to describe the changes that the UN wants to see to the role and remit of the UN tax committee?
Martin Hearson: UN bodies do not always get a good press, and that is often justified, but it is important to say that in this case we are talking not about a big amorphous UN body but about a tightly focused committee of experts that produces tools that are used every day by revenue authorities in developing countries. In particular, its model tax treaty is well respected and is used a lot in negotiations of tax treaties by developing countries. The discussion is about the fact that the predominant set of international standards is still the OECD, which does not and cannot represent the interests of—

Q36 Hugh Bayley: I understood that distinction from your evidence, but what are the changes to the role of the UN tax committee that the UN’s Economic and Social Council is supporting and that you tell us the UK Government are not supporting?

Martin Hearson: The changes are proposed by the G77. The Economic and Social Council did not reach a decision because of opposition, so it is the developing countries that are advocating these changes. The changes were two-fold. The first was to increase the committee’s resourcing, because at the moment it has three staff in total. It is inadequately resourced; it does not have the resources to pay for the travel of members to all the meetings held, which means that developing country participation is reduced. So, the first aim was a considerable increase in resourcing. The second aim was to keep the committee of experts as currently constituted but to create a separate intergovernmental body, the reason being that the experts are represented in a personal capacity. It is interesting to have a body in which developing countries and developed countries are able to discuss international tax issues in an official capacity. That is the key thing that is missing and what is being proposed.

Q37 Hugh Bayley: I would like to draw two parallels. I understand from work I have done in years past on trade the value that UNCTAD has as a kind of forum that empowers developing countries, which the WTO does not do to the same degree. Nevertheless, if you do not reach agreement in the WTO, there is no deal. I think of the UN to some extent as a talk shop and a way of facilitating conversations and perhaps providing services to people from poorer countries, but it does not have the authority to impose decisions. I did work over 10 years to get the Bribery Act on to the British statute book. The OECD anti-bribery convention was a driver; the UN convention was much more decorative; it did not have a bite. Is there not a danger in undermining the OECD? Shouldn’t you be trying to strengthen the UN tax committee so it can provide better advice and services and a voice to developing countries? If you were to undermine the work that the OECD does, surely you would end up reducing the pressure on developed countries to become more transparent and address the very issues that you are raising with the committee.

Joseph Stead: The problem with the analogy of trade is that the WTO does at least have representation by the developing countries, so they have a voice in the WTO as well as in UNCTAD.

Hugh Bayley: That is true. The problem with the OECD is that the developing countries are not there as members to have a legitimate voice in those discussions. The danger is that, if you keep the OECD as the driving force, it will pay attention to the interests of its members, who are the developed countries. Therefore, the developing countries do not get their voices and interests taken into account.

Q38 Hugh Bayley: Aren’t you cutting off your nose to spite your face? The OECD has a strong track record of making countries like Britain get real about things like bribery and anti-corruption and to change its law. The UN just does not have the leverage to make Britain, the United States, France, Germany and Japan change their laws. You might dream up a little utopia—or a big utopia—in the UN, but, surely, you need the OECD to make the rich countries of the world do the sorts of things you are advocating.

Martin Hearson: I make two points. Firstly, by no means are we saying there is not a role for the OECD. The way it works at the moment is that the UN committee takes the standards set by the OECD, adapts them for the needs of developing countries and then produces an equivalent. That works very well because the OECD has a strong role. That is very important to note. I had a second point but I have forgotten it.

Q39 Mr Gyimah: We have received some written evidence that suggests that the introduction of a mandatory beneficial ownership registry would be useful. Would you support that? What do you think the measure would achieve?

Joseph Stead: Essentially, we would support it. What it would achieve is that you would know who owned things. That is a huge problem at the minute. The existence of shell companies makes it very difficult to know who is behind things. There are countless examples where shell companies have been used for corrupt purposes. Politician or elites have been able to buy mineral rights or whatever and keep their involvement hidden, and that is clearly helping corruption. We had an example of the Northern Rock-owned Granite entity. No one knew who owned that. It is a problem in terms of the financial crisis in the UK. Not having clear ways to understand who owns things can create huge problems in accountability.

Chair: You will appreciate that we are in a dynamic situation. You have given us written and oral evidence. If you reflect on anything you have said to us, or anything we have said, that you feel you can add to following this evidence session, please feel free to pass that on to us. It will help us to ask questions if we have that kind of ammunition, some of which you have given us. Please do not regard this as the end of it. If you have anything else that you feel is important or relevant to the inquiry, I hope you will feel able to give it to us. We will be visiting Zambia in particular in a couple of weeks’ time and we will have an opportunity to explore these things in more detail, so it is particularly helpful that you have been
able to be here today. We appreciate the fact that you have taken us through your perspective on that. Perhaps I may say formally thank you very much indeed. Obviously, you are welcome to sit in on the second half of the evidence this morning, if you wish to do so.

Examination of Witnesses

Witnesses: Professor Mick Moore, Professorial Fellow, Institute of Development Studies, Professor Tim Besley, School Professor of Economics and Political Science, London School of Economics, and Dr Jonathan Di John, Senior Lecturer, Department of Development Studies, gave evidence.

Q40 Chair: Good morning and thank you very much for coming in. You have been able to sit in on the first half of the evidence session. I shall ask you to comment on that in a minute. I would appreciate it if for the record you would introduce yourselves.

Dr Di John: My name is Jonathan Di John. I am a senior lecturer in political economic development at the School of Oriental and African Studies.

Professor Besley: My name is Tim Besley, School Professor of Economics and Political Science at the LSE.

Professor Moore: I am Mick Moore. I am an academic researcher on economics and politics. I am the Chief Executive Officer of the International Centre for Tax and Development, which is a research centre funded jointly by DFID and the Government of Norway.

Q41 Chair: You have heard some of the comments and, indeed, accusations made by the previous panel. Do you have any particular comments, either where you take issue with what they have said or you want to reinforce their position, if you feel that they are right? I ask each of you briefly whether you want to comment.

Professor Moore: I have three quick comments. First, Hugh Bayley, you asked whether aid to Zambia would be more poverty reducing than local taxation. There is a very important broader point here. Some recent research suggested that aid is probably the most unstable source of public revenue for developing countries. In a situation where a major source of revenue is unstable, it is almost true by definition that public expenditure will be very inefficient, because you do not know how much money you have. By contrast, taxation is the most stable source of revenue. There is a presumption that tax is better than aid, all else being equal. I think that is a strong presumption. As to my second comment, some of our previous colleagues, in particular Mr Mwambwa, talked about transparency. I think transparency is a key thing running through a wide range of particular points here. Transparency about rules and their application is central to many of the things discussed, like transfer mispricing, tax havens and information exchange, but one issue that was barely mentioned is tax exemptions given by Governments of developing countries. For many developing countries these are very large and often unjustified. Typically, for many African countries, as far as we know, 5% of gross domestic product is given away annually in tax exemptions, and that might be a third, or even more, of actual tax collections. We are talking about a large amount of money. These exemptions are often given on a rather arbitrary basis and are not transparent at all. That is a very important issue to be taken into account here. I am not saying who is responsible for this, but it is a very big issue that should be mentioned.

As to my third point, perhaps my attitude differs a little from that of some of the previous speakers. I ask the Committee not to be sidetracked by the argument about the allegedly regressive nature of value added tax. Apart from the United States, value added tax is almost worldwide now. It is a slightly complicated but very efficient way of raising revenue. Almost all developing countries have adopted it and it is bedding down rather well. It is far from clear that value added tax is a regressive tax. Yes, it falls on consumption, but in many developing countries, as in Britain, a large number of basic goods are zero-rated, so it is not clear that it is actually regressive, and research shows we do not know the answer. But the important thing about its alleged regressive nature is what tax this is actually replacing. In a situation where tax authorities find it very difficult to raise revenue at all, if you have a good instrument that is doing a very good job, I would keep it and concentrate on other things. I would not want to raise that as a problem.

Professor Besley: I begin where Mick ended. I think the tenor of the previous debate was, for natural reasons, a little too focused on some of the multinational taxation issues, which I will come to in a second. It is important to recognise that the long-run project is to build broad-based taxation in the area of VAT and income tax. If we lose sight of that, we are losing sight of the main development problem. Apart from the benefits that Mick outlined, VAT has considerable benefits to encourage administration, because the process of administering VAT involves firms formalising and submitting proper accounts because they get the advantage of deducting the tax on their inputs. There are lots of long-run benefits from eventually introducing a well-administered VAT. The same goes for income taxation. The history of income taxation is that firms are predominantly responsible for complying, not individuals, even though it is an individual tax. The vast majority of tax in the UK is collected through PAYE, and the history of it is that you develop strong systems of firm-based taxation, so again there is a long-run development benefit built into trying to build those broad-based taxes. I have a couple of comments on things that have been raised. There is a very big difference between resource and royalty taxation and corporate taxation in general. If you told me that the plan was to raise the cost of capital to multinationals operating in the developing
world, in general I would say that is a very bad idea. In general, there is overwhelming evidence that the kinds of benefits that foreign direct investment brings to development outweigh the costs in almost all areas. Therefore, discouraging it by trying to increase the cost of capital to operate in the developing world as a general phenomenon would, I think, be a mistaken mandate. Of course, you want them to comply with broad-based rules.

Q42 Chair: A point was made about competition between different countries with tax exemptions, deals and lack of transparency. I just question, therefore, whether in those circumstances if a company declares that its operation in one country is loss-making and finishes up paying no tax but, by other transactions, picks up a profit elsewhere, it is not benefiting the country.

Professor Besley: That is absolutely right. I am not going to push back on that particular point, but China’s use of special development zones with tax exemptions has been a key part of its development strategy. India is now doing it. Of course, it has to be controlled, and it has to be recognised that there are wider issues of exactly the kind you describe, but I do not think there is a general issue here that says there should be a mandate to tax corporations more heavily in the developing world. But I would draw a distinction in the case of royalty taxation, which is a separate issue. The International Growth Centre to which I belong has been doing some work on royalty taxation in Zambia. We have someone working with the Zambian Government on alternative systems of royalty taxation, but that is a separate set of issues where I see a much stronger case for wanting to raise more taxes. We can come back to some of these issues.

Dr Di John: I make just a couple of comments. Firstly, the issue of tax exemptions is quite an important one and it was not emphasised. I also think they are not necessarily always irrational or arbitrary. A lot of it has to do with the types of privileges and subsidies given to powerful interest groups, elites and so on.

Q43 Chair: Which very often include Members of Parliament.

Dr Di John: That is correct. Secondly, aid is much more volatile than tax revenues, although one needs to distinguish between those countries that are very dependent on, say, oil as the dominant form of tax. Oil-dependent economies will have a much more volatile tax base, or historically have done so, than those with a more diversified one.

Thirdly, in the previous session I think there was unquestioned acceptance of the tax gap and how much tax revenues are lost to less developed countries, and OECD countries for that matter, because of tax havens. The Oxford University Centre for Business Taxation has done important work on taxation, arguing that there might be serious overestimates of that gap: first, because there are a lot of tax exemptions from which elites benefit, so all the income tax lost because of a tax haven is not necessarily, or likely to be, taxed in a poor country; and, secondly, there are a lot of tax exemptions and tax holidays given to foreign investors as part of production strategies, so that money going back in will not necessarily be taxed either. There needs to be some more serious work on how big that tax gap is.

Chair: Those are interesting comments.

Q44 Hugh Bayley: To start with Dr Di John, why is the capacity of revenue authorities in countries that are broadly similar economically so different country to country? Why are some revenue authorities much more effective than others in introducing tax systems that work and raising revenue from them?

Dr Di John: That is a very good and complicated question, and it is one of the frontier questions of political economy research. One of the things has to do with the economic structure of a country, so countries that have taxes that are easier to collect, for example on oil and minerals, tend to be higher tax collection countries. Thandika Mkandawire of the LSE has done historical research on why, broadly speaking, southern African countries tend to have a higher tax effort and collection than the rest of sub-Saharan Africa. He found in the work that there was a colonial story to this, which was to do with the fact that in southern African countries—South Africa, Zimbabwe, Zambia, Botswana and so on—there was much earlier formalisation of the labour force than in other sub-Saharan African countries. Because of that there are many more registered workers. He finds that legacy has an important statistical relationship to why southern African countries collect tax.

I think the second reason is really a case-by-case one. The political economy, settlements and elite bargains in countries in terms of how big tax exemptions are tend to differ substantially among countries at similar levels of development.

Thirdly, I would argue that countries that have more well-developed national political parties—this is not always the case—tend to be able to mobilise tax better than those political systems at the same level of development that have more fragmented party structures.

Q45 Hugh Bayley: Professor Besley, what do you see as the relationship between the effectiveness of a tax authority and the prospects for economic growth in the country concerned? Is there a correlation? Which drives which?

Professor Besley: The answer is that neither drives either, but that does not mean it is unimportant. If you look at the history of the way states finance themselves, it is generally a move from narrow bases and forms of finance to broad bases. Broad bases have a huge advantage in fostering incentives for economic growth, because the fruits of that growth generally accrue in the form of public revenues. It is true that countries with broad-based taxation typically will have Governments that have very strong incentives to promote the market economy. Market economies, unlike non-market economies, are relatively easier to tax, so you set up a somewhat virtuous circle between the development of broad-based taxation and economic growth.
Where do you get that broad-based taxation in the first place? That is why I say it does not run in any direction. I think it comes back to the forces Jonathan mentioned. I would add that one very strong statistical correlative effect is a revenue authority’s strong checks and balances on the way Government operates. Typically, parliamentary systems raise quite a lot more revenue than presidential systems, because the latter have many fewer checks and balances on executive power. There is quite a strong correlation between the form of political institutions and the ability to raise taxes. That is a macro political factor when you drill down and look at checks and balances. That is an issue of accountability. Systems that have parliamentary scrutiny typically scrutinise public expenditures more effectively on average—of course, there are different cases—than those that do not.

Q46 Hugh Bayley: I was interested in Dr Di John’s illustration of southern Africa as having a relatively better developed series of tax regimes and authorities than other parts of sub-Saharan Africa. He seemed to be arguing that that was because of earlier development of a formal economy. What is the best way for a developing country to increase participation in the formal and taxable economy?

Dr Di John: Is that a question to me?

Q47 Hugh Bayley: It was addressed to Professor Besley, but whoever wants to answer can do so. Professor Besley: Dr Di John may want to come in. The answer is a strong legal system. Why do people want to operate inside the formal economy? It is because there must be benefits from operating inside the law. In many countries you are concerned about, law is a rather arbitrary system. Therefore, operating inside the conventional legal system is problematic. What do you do? You operate outside in informal networks, and those informal networks are more reliable than operating through the formal legal system. I once did some research—I have not done it recently—on the time it takes to get a court case heard in India. If you have a commercial dispute it takes a phenomenal amount of time, so firms do not want to operate inside such a system. Formalisation and legal development is a very strong one. That is why throughout history the development of the legal system is absolutely central to the development of the tax system, through credit registries and the formalisation of land rights and other property titles. These two things historically have gone hand in hand, and people want to be part of the formal economy because they believe there are distinct advantages from operating inside it.

Dr Di John: I would broadly think of that as the main issue. A few studies have been done to attempt to register informal sector firms. Judith Tendler at MIT has done work on the poorest state, Ceará, in north-east Brazil. She found that firms were in the informal sector partly because they did not trust the legal system and partly because it gave them the competitive advantage of not paying tax. Her argument was that in Ceará in north-east Brazil the state government managed to register lots of informal leather and shoe firms by providing them with a deal. Her argument is that you need to give informal actors incentives to register because they are in the informal sector for a reason. One thing that happened there was that a push to raise tax registration among informal firms was related to a production strategy, and in return for registering, firms got access to micro-credit and distribution and marketing assistance from the state. There was a huge increase in informal firm registration because they perceived a benefit from it. One of the things often missing in a lot of the tax discussions is a debate about how to collect more tax. That is often discussed in isolation from what to do with it and as part of other strategies. I think tax needs to be linked much more to production strategies and also to expenditure issues, because the classic reason people give for not paying tax is that they feel the Government will not spend it in a way that benefits them. There need to be more holistic discussions of how tax is interrelated with issues of production and expenditure, and the case of north-east Brazil is a classic example of how one might think about that.

Professor Moore: Tim is absolutely right. It is the legal system that needs to be changed. Tax administrations are the result of the political system being in place. It has been for a long time trying to do something about extending the net to the informal sector. I think the message is, “Don’t expect a lot of progress very quickly.” Experiments are taking place. The World Bank Foreign Investment Advisory Service has a series of different regimes with which it is experimenting in developing countries. Progress will be slow, one reason for which is that a national tax administration that is focused mainly on taxing the larger corporate sector finds it very hard organisationally to put a lot of energy into taxing small-scale informal enterprises in slums or rural areas. It is true, as many people argue, that if there is to be real progress in taxing the informal sector in developing countries, it will be done by local governments, not national tax administrations.

Q48 Hugh Bayley: In the earlier session, Mr Mwambwa said he would value in-country raised revenue more highly than aid because it would increase accountability locally. You, Professor Moore, said that people in developing countries were reluctant to pay tax because they feared that, to put it bluntly, the tax would not benefit them, or certainly the country. You seem to be saying something rather different—that there is scepticism about how well used tax is and little accountability to the citizenry in developing countries. Are you saying something different from Mr Mwambwa?

Dr Di John: No. First, there is a wide variation in tax collection, so obviously the legitimacy of Governments in the eyes of the citizens varies across countries. To collect tax you need a certain level of quasi-voluntary compliance, as Margaret Levi always argued. If you had to collect it at the barrel of a gun, the transaction cost would be too high. Because there is a big variation across countries, that particular issue differs across countries, but a good baseline assumption to start with is that somehow expenditure
patterns need to be seen as legitimate for tax collection to increase. It is a chicken-and-egg problem, but I do not think there is evidence one way or the other.

**Q49 Hugh Bayley:** Professor Besley, we have become used to seeing relatively high rates of growth in Africa and in other parts of the developing world in the last decade. They are much stronger rates of growth than we have in the OECD world, if you like. Is there a connection between an increased formalisation of the economy and increased growth?

**Professor Besley:** The answer is that it will vary enormously depending on the type of economy. If it is a resource-dependent economy, the growth comes primarily from increases in natural resource prices and you do not have a tax regime that taxes that in any way, the answer is that you will not increase collection. It is interesting that at the moment two countries that are quite concerned about trying to increase tax revenues as a share of GDP are China and India, both of whom have enjoyed considerable growth but have quite big structural issues in the way they levy and collect taxes. So there is no natural reason to believe that tax rates, for example, will grow faster than the rate of GDP or even at the rate of GDP growth, and since the demand for public services tends to grow faster than the rate of growth of GDP, you probably need to raise tax revenues more quickly than the rate of growth of GDP. It is not true that countries that have been successful in economic growth, even though they are thought of as countries that are broadly on good growth paths, are entirely satisfied with the way their tax systems are able to generate returns to Government from that growth.

**Q50 Mr Gyimah:** I want to explore briefly the relationship between the tax base and governance issues. There is a widespread consensus on the notion that countries that have a broad tax base, i.e. a high proportion of the population pay taxes, are likely to be more accountable to their citizens, and vice versa. Bearing that in mind, to what extent does the size of the tax base have implications for the quality of governance from your perspective, starting perhaps with Professor Moore, given the comments he made a few minutes ago about the formal economy and the fact it is more likely that a lot of developing countries rely on a few corporate taxpayers?

**Professor Moore:** I think we all share your intuition that there must be a connection. I have to say that the research evidence on this is a bit patchy. I cannot give you cast-iron evidence, partly because it is a very difficult subject to research for all kinds of reasons. I am sure there is something there but it is very hard to prove. As to the connection between paying taxes and accountability, in part it is a matter of who pays and in part to whom it is paid. If we focus on most countries in sub-Saharan Africa, I think the important constituency for them in paying tax and the relation to Government is the private sector, both corporate and non-corporate, because they are the taxpayers who tend to be organised—chambers of commerce, etc.—and the people who can, if you like, actualise that relationship. That is where I would hope to see progress.

The other point is the local level. Generally speaking, in sub-Saharan Africa taxation at local level is a mess of all kinds, and it is a very unconstructive mess. Taxes are levied in all kinds of arbitrary ways, and it will not change very fast very quickly. International aid has not focused very much on this. The IMF has not focused on this until recently. There is a lot of scope for improving that, particularly through property taxes in medium and larger cities. Over a 20-year perspective I would hope to see quite a lot of improvement there and people paying significant local taxes and, therefore, being more interested in what happens to their money.

**Q51 Mr Gyimah:** Are there any comments to add to that?

**Dr Di John:** I want to add a couple of comments about the relationship between tax and governance. First, it is important to remember that, relative to an OECD country, what we mean by broad-based taxation, even when it exists in a low-income country, is that there are very few individuals or corporate entities paying tax or making up the bulk of tax. In a country like Tanzania, at best there may be 1,000 individuals and corporations that pay 80% of the tax base. The big challenge of governance is that you have a lot of demands for representation with very few people paying taxes. That does not mean the tax burden does not affect everyone—VAT does so—but it is much more skewed, and that is a big challenge.

It is also important to keep in mind what we expect from governance when the average tax take in per capita terms is between $50 and $350 per person per year. We have to think of that versus the position in an OECD country where the figure is between $10,000 and $15,000 per person per year. The implications of that are enormous and are not often discussed. Finally, in terms of local government, the most under-utilised tax, and one that historically was very important in OECD countries, is property and land tax. That is a very under-utilised tax. It was a very big tax in the United States in the 19th century and in Japan in the Meiji restoration. It is a very important tax because it would be the main source of funding for local government, and it is negligible in even middle-income countries, let alone poor ones. Further, to develop property taxes means that you must develop land cadastres. To the extent you do that, it would help to improve the security of property rights. Very few countries have relevant cadastres. I think urban property taxes need to be much higher on the agenda both for their effect on property rights and also the financing of local government.

**Q52 Mr Gyimah:** An interesting point that Professor Moore introduces is: to whom do you pay the taxes? In countries where governance is poor, is it fair to say that an increase in tax revenues may not necessarily help development? Might it not simply enrich corrupt elites, for example?

**Professor Moore:** Yes. We should not expect over the next five years that people paying more tax will have
any visible impact whatever on governance. We are talking of relationships that develop over decades, not years, so what could be naive, but it is the long-term structural changes that are important. A couple of things have been mentioned here. Property taxes are important for reasons other than taxes; there are synergies here between things. Value added tax is important because it helps to develop corporate accounts. It is also a great tax because it gradually brings more small businesses into the tax net, or threatens to do so, and therefore focuses their attention on tax issues. A series of things can be done by way of slow but steady institutional changes that will add up quite positively over a couple of decades, not a couple of years.

Q53 Jeremy Lefroy: Continuing on the subject of the tax base, first I return to VAT. One extremely important caveat is that the VAT system has to work. Therefore, the VAT that is reclaimable by organisations must be capable of being reclaimed, and that is a major problem in many countries. They find it takes several years to get back the VAT, if at all. As to the tax base, I would challenge one point made by Dr Di John, as well as agreeing with something else he said. Particularly in agricultural-based countries, where a large proportion of the population work in that sector, their tax rate is higher than the marginal tax rate of the richest people. Looking at the crop levies imposed, we see that in Ivory Coast in particular it is 40% on cocoa. They are paying a marginal tax rate of probably 80%, given that the income of small farmers—what they receive for their cocoa—includes the price of their labour. Therefore, if a Government takes 30% to 40% as a crop tax, in effect it is an income tax at a huge rate. From the limited work I have done on it, the people on the smallest incomes are paying the highest marginal rate of tax in a country. In most of these countries—I think of Tanzania—the highest rate of income tax is 30%. Particularly when commodity prices are low, you find that the marginal rate of tax for farmers is higher than 30%, taking into account all their taxes. The base is very broad but it does not include the right people. I put to you the question I posed to the previous panel: do you want to look at that, in countries that do collect a lot of income tax, most comes from the PAYE system, so salaried workers contribute the vast majority of personal income tax. In a country like Mozambique, the top 15 corporations pay zero corporate income tax. That is part of a production strategy to attract foreign direct investment, but I agree that personal tax up to 1% or 1% is very low. In countries that collect a lot of income tax you have quite a progressive system, in the sense of personal income tax. It is very regressive in the sense that the middle class tends to pay a lot more personal income tax than the upper class. I think that is a common story, expect for South Africa. Q55 Pauline Latham: To make a comment on that section, when we went to Rwanda we saw a fantastic scheme where they are registering all the land. Until other countries register all the land and have a proper registration of people, there is no way they can have a fair taxation system, because there are so many people who are double-registered or not registered at all; they do not know who owns the land, and they cannot tax people on it. Any developing country must have that system, which is quite sophisticated. It is based on voter registration, but it relates to people who could pay taxes. It is something that needs to be done in all the countries before they can get a proper broad tax base. I want to ask a couple of questions, one a general one and then a question specifically to Dr Di John. Dependency on natural resource taxation often leads to large fluctuations in tax revenues, especially when commodity prices go up and down. How can countries best cope with that? Professor Besley: The answer is that it all depends on governance. There are countries that have devised effective schemes. One interesting case in point is that the Ghanaians are managing their oil revenues through the central bank because it is the one institution that people trust to take a long-term view and not spend too much out of short-term fluctuations. You might pick an institution like the central bank that you feel has enough credibility to deny what you might call quite a successful economic liberalisation. One of the reasons marketing boards were unwound in sub-Saharan Africa was that the effective marginal tax rate on farmers was so high. It might be quite high; it is probably higher than elites pay, but that is partly because of elites avoiding it. In most sub-Saharan African countries that I know—I have studied the countries in eastern Africa—the tax rates on the agricultural sector is one half of every other sector, so that is not a normal case.

Q54 Jeremy Lefroy: Have a look at countries like Ivory Coast at times when commodity prices are low, and look at the marginal tax rates. Dr Di John: I completely agree that the issue of domestic political settlements and what elites are allowed to get away with in terms of paying or not paying taxes is the biggest issue in terms of understanding the political economy of tax. I can refer you to a New York Times documentary last year on Pakistan called Elites Don’t Pay Taxes. That is particularly about how the biggest landowners in the country pay zero income tax. I would point you to that, in countries that do collect a lot of income tax, most comes from the PAYE system, so salaried workers contribute the vast majority of personal income tax. In a country like Mozambique, the top 15 corporations pay zero corporate income tax. That is part of a production strategy to attract foreign direct investment, but I agree that personal tax up to 0.1% or 1% is very low. In countries that collect a lot of income tax you have quite a progressive system, in the sense of personal income tax. It is very regressive in the sense that the middle class tends to pay a lot more personal income tax than the upper class. I think that is a common story, expect for South Africa.
excess spending during boom times, which means you get big fluctuations in revenues.

**Pauline Latham:** Perhaps we should have them here.

**Professor Besley:** That is a particular example, but there are questions about how you design those institutions and give them the incentives to make sure people understand the difference between a permanent and a temporary shock in prices. Even the best analysts will tell you that they cannot say whether the current spike in oil prices is temporary or permanent, so it is a difficult thing to do, but we know what is cautious and incautious behaviour in relation to spending in those fluctuations, so it is down to institution design. In other countries there may be very few credible institutions that can resist the political pressure to spend out of resource revenue that inevitably arises. The answer is that it depends. There are solutions available, but I do not think it is one size fits all in relation to giving it always to this or that particular institution.

**Professor Moore:** I would agree. There are all kinds of funds you can or cannot set up, which have had a rather mixed experience so far. If you want to do it, as a Government you can do so very easily.

**Q56 Pauline Latham:** I have a specific question for Dr Di John. On your work in Africa you have drawn particular attention to the gemstone sector. Will you comment briefly on the particular challenges in the gemstone sector in Zambia?

**Dr Di John:** It was quite a small part of the paper I did on the political economy of tax in Zambia, and it was mostly through interviewing politicians and business people in the sector. It is a sector that is largely unregulated. The estimate of its contribution to exports is $300 million to $400 million a year, and what is reported is about $20 million. Most of it goes to the DRC and tends to be owned by political party leaders and associated business people. Before we talk about the gemstone sector, the argument I was making was that, from the historical perspective, if one thinks that elite bargains are important for creating political stability, as Douglas North and others have argued, economic liberalisation has created an important challenge for how states create privileges or economic rents to elites. Previously you could do it through cheap credit, tariff protection, jobs in state-owned enterprises and so on. Economic liberalisation has taken away a lot of the levers for the creation of economic rents to elites. In a lot of interviews I found that the tax system, or lack of regulation of particular sectors, had been used as a way to create rents. There has been an increase in the tolerance of tax evasion among elites. I was interpreting the gemstone sector as one way that the dominant political party at the time, which was MMD, was distributing rents or privileges to various members. The challenge of maintaining political stability does not go away just because you liberalise, but liberalisation does mean that the old mechanisms of creating rents are not there. In this transitional period to a more market-based and pluralist economy, we are likely to see the tax system as a substantial source of rent creation in its various forms. That is how I view the lack of regulation of the gemstone sector. There are other examples of this in sub-Saharan Africa in places that are otherwise pretty good tax collectors. Zambia is one of the better tax collectors in sub-Saharan Africa; its tax collection is 17% or 18% of GDP, and it collects, relatively, a fair amount of personal and corporate income tax, especially personal income tax. That was my general interpretation of the sector but it was not a main part of the research.

**Q57 Mr McCann:** I move on to harmonisation between donors, in particular how you see DFID’s role. There is a perceived lack of co-ordination between donors in the sector. Professor Moore, you have suggested that DFID should be involved in this area, but not necessarily spend any more money. Is that realistic? Should DFID be focusing on multilateral agencies in order to cut down the number of players in the field, and therefore presumably get a quicker result, or should they also continue with their own individual efforts as an organisation?

**Professor Moore:** I think it makes sense to continue with individual efforts because you get credibility and knowledge from having projects in-country that you do not have if you are not funding any projects. That is fine. I would be very sceptical about scaling up the number of projects and the number of countries because so many other donors seem to be doing that at present. In a sense there are co-ordination problems at two levels. At the big level, especially in international taxation and transfer pricing, you have particularly the OECD and IMF who are not entirely congruent one with the other, which is a problem. If you go down to country aid level, you have an increasing number of bilaterals who were not in this business 10 years ago. Ten or 20 years ago the Germans and DFID were almost the only bilateral donors with significant programmes, working well with the World Bank and the IMF, but now you have a lot of bilaterals who have seen all these discussions on tax in the last few years and have been to these meetings. The Americans are a good example. Suddenly, they want a tax project, so they are going round spreading little bits of money here and there. I think we have so much experience to show that this is not a good idea. Co-ordination, harmonisation and pooled projects for tax activities are really important. Although DFID do not have the same prominence they once had in this field 10 or 20 years ago, they are still quite a big player and have the capacity to help co-ordinate others, partly because they have very good relations with the IMF and the World Bank, so they are really well placed to co-ordinate.

**Q58 Mr McCann:** To be clear, do you think that the bilateral operations are effectively pilots in order that we can see how things best work in-country and we can expand those? How do you then control them if the numbers expand and they are doing damage rather than helping?
**Professor Moore:** Solid evidence that they are doing damage is very hard to gain, but when you see several different aid agencies in the same country all funding a different aspect of the revenue authority, you know there is almost certainly a problem. A lot of that has occurred and often it is an excuse for no reform. Bangladesh has had a lot of that for a long time. I would not say the bilateral projects are just pilots; they give credibility. If a donor like DFID wants to go along and say, “We have a voice on taxation,” the fact that you have a few projects in some countries, you are employing specialists and know something about it adds something to it, but DFID are doing that already.

**Q59 Chair:** Where the Government are engaged in budget support, that is a standard part of the package, very often in co-ordination with other donors. We saw that in Tanzania. It was not entirely transparent; it was more an ability to say, “We have co-ordinated what we have done. Their tax revenue has gone up and their aid dependency has gone down, so we think it is working.” Could it be more scientific than that? But where there is a delivery, we are dealing now increasingly, with fragile post-conflict countries that are corrupt and incompetent, is it possible to construct a tax project that will make a difference in a country like the DRC?

**Professor Moore:** The Adam Smith Institute has been running a tax project in Afghanistan for some years. They claim that it has been rather successful. They have asked us to look at it and we have not yet done it, so I do not know whether it has been successful. South Sudan would be a very good example, where what you have is a revenue system that is a fragment of a lot of bits of things. It is not a revenue system in any significant sense. The idea of employing cadres of people—the stabilisation unit and Adam Smith Institute—to set up a taxation system on the ground seems to me to be quite plausible and sensible, because the technology of raising tax is a pretty transferable one. If you can do it in one country, with some adaptations you can do it in another. It is not like biological research, where agricultural research in one country has to be considerably adapted for another. If there is evidence that these kinds of on-the-ground interventions work—not just funding but sending in people—I would be in favour of them, but so far I do not know of any evidence that they work. You might want to look a little more at the Afghanistan case.

**Q60 Chair:** We will have an opportunity to do an inquiry on that, so we will follow it up.

**Professor Besley:** DFID is pioneering a somewhat different effort in this direction through its funding of the International Growth Centre. At the moment we are engaging with the revenue authority in Pakistan in a rather unique project where, by working with the revenue authority, we are doing an experimental intervention on incentives for tax inspectors to see what impact that has on revenue collection. That simply would not have been feasible Government to Government for lots of reasons, but by working with a DFID-funded centre from the LSE we are able to engage in what I think will be a really interesting research project. We also have some work going on with the Bangladeshi tax authority. I think a certain weight is attached to official development assistance in this area, and one has to consider what can be done directly and what indirectly.

**Q61 Mr McCann:** Professor Moore, you mentioned that new donors had come in and there were different ideas about South Africa and India. Have they brought anything new to the table, because they have emerged as developing countries and are moving forward? What is your take on that?

**Professor Moore:** What they have brought to the table are some of the international taxation issues, of which transfer pricing is an example. They are concerned about this, and clearly they will now just be much bigger players in the field, so there is a sense that, rather than the OECD countries trying to do something for the benefit of the south, as it were, we are much more into a game of mutual advantage. Both sides, north and south—at least the bigger BRIC countries of the south—have a real interest in progress, and the more we can do work on tax, especially in sub-Saharan Africa, it works so much better if you send tax people to talk to tax people. Tax collectors are a fairly isolated breed in sub-Saharan Africa. With some exceptions of people who come in from the private sector recently at very high levels, you are talking mainly of people who have been in that career all their lives. They were probably not even graduates originally, so it is a rather isolated culture and they respond so much better to tax advisers or whatever. The more we can have South Africans, Indians and other people exchanging with sub-Saharan Africa the better.

**Q62 Jeremy Leftey:** You spoke just now about India and South Africa. Clearly, China is a huge influence across the developing world, particularly in sub-Saharan Africa. What influence do you think China has as probably the major purchaser of commodities, agricultural but particularly minerals, in tax collection?

**Professor Moore:** I do not know the answer to that question. I would be surprised if they had any significant impact at present. I have no reason to think that their companies are any more corrupt or susceptible to tax evasion than companies from elsewhere. It is important to bear in mind that in the context of China we are talking about thousands of companies, some state-owned, some private and some quasi-state owned. These are issues to which the Chinese Government are not paying attention, but that is more a guess than anything.

**Dr Di John:** From a different angle, I think the increasing role of China and also India in competing for natural resources could have a positive effect in the sense that, the more people there are bargaining over natural resources, you would think Governments
should gradually be in a better bargaining position to get slightly higher royalty rates from some of the mineral and fuel deals that are done. From the longer-run perspective, I think the increasing presence of China, India, South Africa and Brazil—players that were not in sub-Saharan Africa—should increase bargaining power. Of course, the geological survey capacity of sub-Saharan African countries if woefully low. They do not know what they have in the ground; only multinational corporations do. Maybe the best thing donors can do is improve both their auditing capacity of firms in LDCs and also their geological survey capacity. That would give them an enormous bargaining chip and also enable them to appropriate more of the rents from natural resources than they currently get.

Q63 Chair: Do they underestimate their leverage? If you look at Brazil at the moment, it is expanding its offshore oil and gas industry in a very aggressive fashion. Basically, it requires any foreign agent, firstly, to put 1% of its turnover into research and, secondly, to operate through a 50%-owned Brazilian partner. Are countries in this, cosine gaining a trick here? It may not be what foreign companies like, but they seem to be prepared to do it in Brazil. Why won’t they do it in Africa?

Dr Di John: To start with, in many sectors Brazil is as sophisticated as, or more sophisticated than, South Korea, so we are talking about a country at a completely different level of development, particularly in these particular sectors and heavy industry. A lot of it has to do with very differential capacity and level of skill.

Q64 Chair: Botswana got itself a capacity in the diamond business that has enabled it not just to take a 50% stake but to acquire expertise to add more value in-country. That is a good example. I gather that Namibia is following suit; some of the other countries are not. To take Zambia in particular, shouldn’t there be experts in copper, and are there?

Dr Di John: You would think so, but in the 1960s they exported 600,000 tonnes a year. By the late 1990s that was down to below 250,000 tonnes, so they did not seem too expert at running that industry. Relative to the previous session, one thing to keep in mind about a country like Zambia is that in the 1990s the copper sector represented losses of 10% of GDP per year because of employment padding, mismanagement and so on. They were losing $1 million a day in the copper industry, so, while they gain relatively little from royalties now compared with other mineral and fuel countries, it is certainly a lot better than minus 10% of GDP per year. People forget that historical perspective. I am not so sure they did know as much as you would have thought about the copper industry.

Q65 Jeremy Lefroy: You talk about royalties, which clearly is very important. We are talking here about two separate streams of taxation. There are royalties that can be defined perhaps more by tonnage, but earlier we referred to income tax, which is much more difficult to define. I think that is where the whole business of tax transparency arises. I just put the question again about countries such as China. Do you think that the same problems we are talking about as applying perhaps to western countries in terms of transfer pricing and so on would apply equally to countries such as China or India in their dealings with natural resource exports?

Professor Moore: I am not really expert on this. Dr Di John: Neither am I. Professor Besley: Neither am I.

Chair: Jeremy, you have beaten the panel.

Q66 Hugh Bayley: That gives me much more trust in all the rest of your answers. There are just two snippets I do not quite understand. Professor Moore, you talked about the OECD and the IMF pulling in different directions. Can you describe the issue? Professor Besley, you gave the example of incentivising tax collectors in Bangladesh and then said, as an aside, that it was not something you could do on a Government-to-Government basis. I am being very naïve here. Can you explain why?

Professor Moore: I am probably going to upset someone when this becomes public. It is not so much that they are going in different directions, but you would think that at this moment, and for the last few years, when there has been so much international interest in tax issues, especially international tax issues, the two leading organisations in the world would be making a lot of effort to co-ordinate and co-operate with each other, and frankly they are not. Q67 Hugh Bayley: Give an example so I understand the problem.

Professor Moore: I refer to the OECD’s expert task force on tax and development. I think it is right. I am a member; the IMF is not.

Q68 Hugh Bayley: I see. So, you would like to see more institutional wisdom-sharing and so on.

Professor Moore: Yes, and co-operation. I understand where this comes from, because the OECD has been, if you like, the more activist recently in putting these issues on the agenda, and the IMF, for a range of reasons, has been a little more conservative and has not shifted as much, partly because it has limited resources to put into issues of domestic and international taxation. These are institutional rough edges; there is no reason to think that it is structural and fundamental. I hope it is not.

Professor Besley: To give a brief answer to the question, I think it comes down to what I call policy ownership. There is a world of difference between a Government feeling that it is initiating a policy and feeling that the policy is initiated on its behalf. In the growth centre, not just in tax areas but more generally, the mantra is demand-driven research. We engage with the Government and say, “What are your priorities? Is it to evolve a programme of work that comes from what you perceive the need to be?” That has some issues associated with it. There may be areas where the Government do not want to go that we could perceive to be priorities, but it is a very different model from one where the external donor with the money is essentially trying to set the policy agenda.
We have noticed a big difference in the way we operate, because the initiation of policy agendas is from the Government itself. We then support that; that is where we come in. That just creates a very different climate. I think things are feasible in that mode that would not be feasible were it an external Government coming in to set the agenda.

**Q69 Jeremy Lefroy:** The title of this inquiry is “Tax in Developing Countries: Increasing Resources for Development”. It has always struck me that one way in which resources could be increased, which is not often looked at, is the fact that we have in excess of $350 billion a year in remittances now going into developing countries. Yet I am not sure that in many cases the kind of tax breaks that a western donor would get, in this country through gift aid by making a donation either directly or through a charity, are either taken up or are available to the people who are doing the very same thing by sending remittances, often directly for development work. Will you comment on that and say whether it is perhaps worth exploring? Perhaps you can even put a figure on how much you think could be contributed that is not being contributed.

**Professor Moore:** I have to say that any mention of tax breaks in relation to developing countries is generally a bad idea. There are far too many tax breaks.

**Q70 Jeremy Lefroy:** Any of us who donate to Oxfam, Christian Aid or any of the other organisations that give evidence to us get a tax break; it is called gift aid, because they are organised to do that, quite rightly, and I fully support that. Every year $350 billion-plus goes in remittances from people who are working in developed countries and sending money back to their families for education, which is exactly the same kind of things that Oxfam, Christian Aid and so on are doing, and yet very often there is no mechanism for them to recover the income tax that they have paid in the developed countries. It seems to me this is one way of getting substantially increased resources for development through remittances that is not being taken up at the moment.

**Professor Besley:** Provided it could be policed and there was a proper public benefit test, I can see the merits. The problem is that it could just be a way of cycling money back to the UK through effectively creating a tax haven possibility. Assuming such a scheme could operate on the basis that you want it to operate, which is to create a clearly defined public benefit with the remittance, I would be in favour of it, but I would be somewhat sceptical that it would open up all manner of possible routes for people to avoid UK tax without necessarily generating a public benefit in the country concerned. That would be my only concern.

**Q71 Chair:** It has been the reputation of tax collectors down the ages that they have tended to operate in many countries as a franchise from which they skim a percentage. Is a lot of that still going on?

**Professor Moore:** Yes. If one looks at what the tax process is like, especially in many of the lower income and badly governed sub-Saharan African countries, you have people who, on the one hand, struggle very hard every month or fortnight to meet revenue targets set by the Government. If they cannot meet the revenue targets, they squeeze somebody else to make sure they meet them. It is not a pretty process. On the other hand, they are consistently skimming off a certain proportion of this money for themselves, or someone else higher up the system. If you look at the actual tax collection process, up close it is pretty ugly. The extent of reform of tax administration in sub-Saharan Africa over the last decade or so is quite impressive. A lot of what is happening on the ground is positive, so it is bad but there is a real possibility of it getting better.

**Professor Besley:** The schemes that we are looking at in Pakistan are precisely trying to incentivise, so they are not tax farming, which is at the extreme end, where you get to keep a proportion. Bonus pay has a bad name at the moment, but, frankly, the idea of trying it in environments where people are very poorly incentivised to do a decent job, on a controlled basis with the right safeguards, is something we should be doing.

**Dr Di John:** In broader terms, a much bigger issue, particularly for post-war economies like Afghanistan’s, is the extent to which the state has a monopoly over tax collection. The biggest challenge in a post-war country—is this some research that came out of the Crisis States Research Centre at the LSE—is that the probability of collapse is much greater when you do not have a monopoly over tax collection. That is a much bigger issue and is based on the structure of warlord politics, and so on. That is quite an important issue.

In sub-Saharan Africa another quite important thing is that in places like Mozambique and Tanzania, where you have dominant one-party states, there are competitive elections but the same party is winning. In the case of Mozambique and Tanzania, FRELIMO and CCM respectively collect a fair amount of taxes to finance party activities, so they are skimming off part of a political settlement or deal to finance their election campaigns, to give rents and privileges to party cadres and so on. That is quite an important problem. The Tanzanian state loses a fair amount of revenue and the CCM runs the Government. There is competition between the state and the dominant party that goes on in both countries. To give an example, FRELIMO runs the import and export scanning machines in Mozambique, so they are the customs officials. That is a privately owned FRELIMO company that is outsourced from the state. That is a bigger issue than whether tax inspectors are skimming 1% or 5%.

**Q72 Jeremy Lefroy:** I was going to ask almost precisely that question. What evidence do you have that the tax collection systems in these countries have been used as a revenue-raising operation by the dominant political parties? You have just answered that there is evidence, with which I would agree from my experience. The consequential question is: what problems does that bring for a multi-party democracy
where one party is using its dominance of Government effectively to extort funds for its own political uses?

Dr Di John: It is certainly a big challenge to the opposition, although in Zambia, where I also uncovered evidence of MMD using the tax system to finance its activities, the MMD just lost an election. There is hope, but it does create a big advantage to the incumbent. In times of economic crisis you will see power turnovers. I think that Zambia, despite all its growth, has seen a huge de-urbanisation without much of an increase in the income levels of the rural poor. That has been the main reason why Sata won the election. Therefore, in crises it is not an absolute advantage, but it is certainly a big competitive advantage for dominant one-party states, or dominant party political systems.

Professor Moore: Maybe I am speaking in defence of African tax collectors. The mechanisms used for political funding vary a lot. We know very little about them. Even if the tax system is being used to raise revenue for the party, prime minister or president, it does not necessarily mean that it is the official revenue authority that is doing it. Often it will be done, for example, by Ministries with jurisdiction over forestry or fishing. They will have the right to raise revenue. It never goes to the revenue authority itself; it just goes directly from the Ministry to the politicians. This happens at local level. Customs does tend to be in most countries more corrupt. Often, there is a more institutionalised rake-off from customs than from domestic revenue, so there is quite a lot of variation in the way these systems are used.

Chair: Thank you very much indeed for a fascinating session. If I may say the same to you as I said to the previous panel, if on reflection there is anything you think you could add to our inquiry as it proceeds, we would be very happy to hear from you. Thank you for submitting your evidence and for coming here today. We have learnt quite a lot, and I hope we will learn a lot more by the time we get to the end of this inquiry. Thank you very much for your assistance.
Tuesday 24 April 2012

Members present:
Rt Hon Malcolm Bruce (Chair)
Richard Burden
Richard Harrington
Mr Michael McCann
Pauline Latham
Jeremy Lefroy

Examination of Witnesses

Witnesses: Tim Scott, Global Head of Tax, Glencore International plc, Emmanuel Mutati, Board Chairman, Mopani Copper Mines PLC, Graham Mackay, Chief Executive, SABMiller Plc, and Christopher Lenon, Chairman, Tax and Fiscal Affairs Committee, Business and Advisory Committee to the Organisation for Economic Co-operation and Development, gave evidence

Q73 Chair: Good morning, and thank you very much for coming to assist us with this inquiry into tax in developing countries, particularly in relation to resources and development. Before we start, for the record, will you introduce yourselves?

Tim Scott: My name is Tim Scott. I am the Head of Tax at Glencore International plc.

Emmanuel Mutati: My name is Emmanuel Mutati. I am Chairman of the Board of Mopani Copper Mines in Zambia.

Graham Mackay: I am Graham Mackay. I am Chief Executive of SABMiller.

Christopher Lenon: I am Chris Lenon. I am speaking as the Chair of the Tax Committee of the Business and Industry Advisory Committee to the OECD.

Q74 Chair: Thank you very much. As I think you appreciate, what we are really looking at is the ability of developing countries to develop their tax base from all sources: inward investment and resource development, as well as general economic activity within their countries. Obviously you represent investors within developing countries. As I think you know, we went to Zambia as a case study, but it is important to understand that this is not a focus on Zambia per se. It is a case study, and we are interested in the wider implications elsewhere.

Again, as you know, we visited copper mines, including the Mopani mine in the copper belt of Zambia, and we appreciate the fact that those visits were facilitated—I think that the Committee found them very interesting. Perhaps to get us started, the real issue is the extent to which you can attract investment and also secure sufficient revenues for the country in question. If you are an outside investor, clearly you want to be able to invest and make a profit—that is understood. However, the country that has the resources wants to gain a tax and a revenue flow from that. Do you think that tax policies can and should deliver that kind of balance?

Emmanuel Mutati: I think it is possible that tax policies can deliver an attraction of investment. If we go back a few years, when the copper industry was under the parastatal company, and declined from 700,000 tonnes of finished copper to 230,000 towards 1999, obviously the Government were then receiving much less tax. A decision was then made by the Government to privatise the industry, and the new investors entered into development agreements with the Government, with a tax regime that attracted investment. That was a tax regime agreed between the Government and the new investors, with a stability period of about 15 years. That was the kind of tax regime that brought in investment for Glencore in particular. By mid-2008, we had already invested $1 billion in the property. To date we have invested $2 billion. In Zambia, to last year, there has been a total investment of $5 billion, but along the line—

Q75 Chair: By the copper industry in general?

Emmanuel Mutati: By the copper industry, yes. Employment has grown, for Mopani for instance, from 10,000 at privatisation to 16,300 people. However, along the line, the Government reviewed the tax regime in 2008 and decided to introduce a windfall tax, which was a top-line deduction. That discouraged investment, and then there were not as many people who were interested to come through and invest in Zambia. We believe that if there is a favourable tax regime in the country and stability, which offers confidence to investors, there is a lot of potential in Zambia to invest more. This could then assist the Government to develop the nation and to be less dependent on foreign aid.

Q76 Chair: Perhaps we can hear from SABMiller as well. The sort of tension you experience is that you are seen to be investing and developing, but because you can offset taxes and so forth, not always do the country or the people see the revenue flow. That is really what we are getting to: how do you get the balance right? How do you achieve the right incentive to invest, and then enough visible tax flow for the community to see the benefit?

Graham Mackay: I suppose the first thing I would say is that these are not problems or balances that are unique to the emerging markets.

Chair: No.

Graham Mackay: They occur right here, in America and in the EU. Our perspective is somewhat different from that of the mining sector because we are a consumer company, and the resources that you mentioned earlier are essentially the people of the country to whom we sell consumer goods. What we see is a very unbalanced tax system in many emerging markets, in the sense that we as multinationals are under intense scrutiny all the time, locally as well as internationally or globally, and of course we pay a
very large proportion of all the taxes collected in many of the countries in which we operate. It is very easy and profitable, or seen to be easy and profitable, for the local tax inspectorate to focus on us and to, in effect, camp with us, and to inspect our doings and our books all the time. That is what we are used to. What we see, though, is the need for easier, simpler, more accessible regulation, which encourages local industry, in our industry segments but also in others, to register, come into the formal tax net, and be part of the economy in some sort of formal way. In many of the countries in which we operate, there is little of that, and in fact big, formal companies such as ourselves are the only taxpayers, by and large. We think tax reform, or tax capability, is crucially important for these countries and will make an enormous difference. There has to be the will to institute simple, accessible tax systems that allow businesses to register and be part of the formal economy.

Q77 Chair: I think that that is understood. It is equally understandable. I suppose, that when people in a poor country see what they see as rich businesses, one way or another they tend to see that as the first target. Clearly the objective is to build a tax base across the piece. I don’t know what kind of advice you would give.

Christopher Lenon: My background is in resources as well, with Rio Tinto. It seems to me that the challenge we have is that we live in very volatile times. If you look at commodity prices, be they in mining, food or whatever, they have fluctuated dramatically over the last 10 or 15 years. The challenge is to find the balance between stability for the investor, for the Government and for the country in terms of the income flows they receive, and the volatility that you have, because we are all operating in a global market where prices are set at a global level.

The other point that was made earlier was that we often talk about fairly significant levels of investment. Clearly from the investor’s perspective, one of their concerns is to recover that investment and then to earn income that meets whatever hurdle rate they have in terms of that investment. They will seek stability in order to recover and then receive the return after that. It is finding a balance between that and what the host Government seeks in terms of taxes.

As Graham has said, these are not just issues for developing countries. They are issues for every country. It is trying to find that balance between the stability that both the investor and the Government seek, and the volatility that we live in. The key thing there is that unless countries have sophisticated tax administrations, they will always struggle in this area. That is why we believe that capacity development for tax administrations in developing countries is the absolute first priority in terms of moving to a more stable situation.

Chair: I think the UK Government, through DFID, does put money into capacity building in countries, but I think you are implying that more could be done in that area to assist development.

Q78 Richard Harrington: Gentlemen, thank you very much for joining us today. I would like to say that I visited Africa for the first time in my capacity in this Committee. From a business point of view, I had had no dealings with Africa at all. However, from my perspective, the huge effect that both the SABMiller operation that we saw in Southern Sudan, and the mine we saw in Zambia, had on people’s lives is very much to your credit. In the case of Southern Sudan, there is almost nothing else—no other form of private enterprise at all. We saw salaries in the mine in Zambia that were 10 times that of others that we had seen in the country. A lot of the criticism that we heard beforehand has to be put into perspective with that in mind.

From a tax perspective, however, which is the purpose of this inquiry, rather than the greater social benefits that you may or may not have, the argument seems to be between very simple revenue-based taxes and the more complex type of corporate taxes that we are more used to in more developed countries. The latter would seem to cause most of the controversy from the opponents’ point of view, because of all the transfer pricing, capital allowances, and things that more sophisticated tax environments are used to. I realise that it has a lot to do with the extent, but as a matter of principle, would you agree basically that revenue–based taxation is a lot simpler to deal with, a lot easier to calculate, and a lot more appropriate in the less developed economies? I don’t know if you would like to answer first, Mr Scott.

Tim Scott: I think there is a place for it. The problem with a uniquely revenue-based taxation system is that it is not going to take account of relative levels of profitability of an investment, and therefore the tax take and the return to investors are not correlated.

Q79 Richard Harrington: Is that not really a question of the level at which the taxation is—whether it is 1% or 12%—rather than the actual principle?

Tim Scott: Correct. In principle these kinds of taxes exist, and we see the point in them.

Q80 Richard Harrington: It seems to me that for the Exchequer of these countries, it is much easier to administer a very simple revenue-based thing. From your point of view, provided the percentage is acceptable, it means that there are fewer arguments about your accounts and all the complexities of it, and it really is just a question of extent rather than principle.

Tim Scott: That’s right. I would say, on the other hand, that the more complex, as you say, taxation of profits is not something that we have found ZRA in particular, or tax authorities in other developing or developed countries, to have phenomenal problems with.

Q81 Richard Harrington: We understand from what we were told in Zambia that the current level of the revenue tax that you are facing has gone up dramatically to 6%.

Tim Scott: Yes.
Q82 Richard Harrington: Is this 6% sustainable, from your point of view?
Emmanuel Mutati: It isn’t really. We feel it is on the high side. I think that 3% was more sustainable—where it was before.

Q83 Richard Harrington: People forget that 6% sounds a small amount from the top, but if you take it to the bottom line it is 30% or 40%, I would imagine, on crude figures.
Emmanuel Mutati: Yes.
Tim Scott: Where we stand at the moment, even without paying profits taxes because of capital allowances and recouping past cost, we are looking at an effective tax rate of above 50%.

Q84 Richard Harrington: Which presumably is not sustainable for the future as far as reinvestment and everything is concerned.
Tim Scott: It’s a lot of money, and we pay it, but new investors will look at this and factor it into their investment decisions.

Q85 Richard Harrington: Presumably you make representations about this to the Government of Zambia on a regular basis. Presumably they see the figures as well.
Emmanuel Mutati: They do. We have made representations. In the past it has not been easy. We would like to mention to this meeting that in fact the new Government are much more amenable to discussing these issues. We have already had meetings with the Minister of Finance, and when the Government start their programme for next year’s Budget, they will invite the mining industry to look at the tax issues.

Q86 Chair: Given the reservation that Mr Scott has set out, although you will always argue that it is too high, as long as it is not really too high, isn’t it much better for both parties to have some degree of certainty? You know what you are paying, they know what they are getting, and you don’t have this endless wrangling and changing—bringing in new taxes and altering the taxes. At the end of the day, you may say, “Grin and bear it,” but at least you both know where you are.
Tim Scott: Absolutely. Stability in the level of taxation is more important in some ways than the level of taxation. It is when there is instability and the post-tax returns cannot be calculated that investors cannot make the kind of decisions that they need to make.

Q87 Richard Harrington: I must say that we all commented afterwards how little both your firm and the employees seem to get back for their taxes. Most of the things that people’s taxes pay for in this country you have to provide to your own employees—health, education and the other things. In terms of the infrastructure that you will probably need to get your product to market, it all seems very undeveloped. I can understand that some resentment must build up.
Tim Scott: Resentment is not the right word at all. We are perfectly happy. We invested in Zambia knowing exactly what we were doing, how much it would cost pre-tax, and with our calculations of what our anticipated tax would be. In terms of health with looking after a quarter of a million people per year, or educating 2,000 children, that is a perfectly acceptable cost to us, and not resentment at all. This is a desperately poor country and we are very happy to play our part. That is a question aside from taxation.

Q88 Chair: Mr Mackay, it is a different business, but I wonder whether you want to comment. Obviously you are quite used to having to pay things like customs and excise duties on your products.
Graham Mackay: Yes. In fact, it is not as different as one might suppose, because if you look at all the tax that we pay in Africa, about 84% of is in fact consumption taxes. It is not corporate income tax or tax on profits at all. That is not all that different from the rest of the world. It is not as though there is a special situation that pertains in Africa.
I would make a couple of points on that. First, consumption taxes have their place. They are simple; they have all the merits that you have mentioned. However, they are also, in a consumer industry, really regressive taxes. That gets a lot of commentary here, for instance, but that is a fact. Secondly, because they are simple does not mean that everybody complies with them. In our industry there are local industries that we compete with—and other international industries, obviously, but we do not have to worry about them—and what we compete with in particular is informal alcohol. Somewhere between probably 50% and 70% of all the alcohol consumed on the African continent is informal subsistence alcohol, untaxed, outside the net, and some of it very dangerous. It causes deaths, which are reported in the newspapers from time to time.

Simply raising past a natural limit the level of consumption taxes in our business has a similarly deleterious effect on investment, because we simply cannot make the numbers work. One of the things that Governments routinely do—again, this is not limited to Africa—is to underestimate the elasticity of demand for a product like beer, or any given product. They think, “People will buy it anyway, won’t they?” The answer is, “No, they will not. They will either do without, or buy something else.” The level of consumption taxes in our industry is high, compared with corporate taxes. It has the merit of simplicity, but it is not a panacea for everything. The temptation is perhaps, without wishing to upstage my mining colleagues, to make those even more variable. Excise duties can be varied at the stroke of a pen, and very often are, year by year. The phenomenon of killing the golden goose—finding that actually total excise take has dropped precipitately because essentially you have strangled the industry—has happened many times over the last few years in Africa and in other parts of the world where we operate.

Q89 Mr McCann: Good morning, gentlemen. At our last evidence session, witnesses suggested that Government should endorse country-by-country reporting of financial information, and also an automatic exchange of that information between tax
Tim Scott: The country-by-country reporting of financial information has pros and cons. The pros are the transparency. The cons or the disadvantages would be the cost to business of producing this information in a reliable and, I presume, audited format. The second potential disadvantage is that with this information it is not clear to me that anyone would be any the wiser on the level of taxation paid, or whether the right tax had been paid at all. That is simply because one has to look at financial reports in the context of the tax law, and of tax returns as well, before one has a very clear idea. I am not too sure that this is amazingly useful. The second point, on automatic exchange of information between tax authorities—information which taxpayers had submitted to individual tax authorities—I think is a good idea, and something that we would have no problem with.

Q90 Mr McCann: Could I just press you on your response about the disadvantages? In terms of the cost of preparation, surely the information exists already? In these days, when we are not working with slates and we have the ability to use computers and transfer information electronically, that wouldn’t be such a huge burden.

On the second point, the whole idea is that we ensure that there is no suggestion that companies are trying to tailor their finances in order to avoid paying tax. Therefore, the ability to shine a light on these issues would ensure that campaigns run by organisations like ActionAid would not be able to make the argument that you are not paying your proper taxes.

Tim Scott: No, I hear what you say. They are valid points. It is an ongoing debate on many levels, and that is my view on it. I don’t particularly disagree with you, and we are happy to work with partners, NGOs and Government to take that one forward.

Q91 Mr McCann: Does anybody else have any views on it?

Graham Mackay: I think you could make a cost argument. To say that the information is there as it is is not quite true, because we do not produce statutory accounts country by country all over the world. We run a much more fragmented business than most mining companies. We have small businesses in a lot of countries. I would not suggest that cost per se is an insuperable barrier.

What I think is much more relevant is the question of how enlightened one would be from looking at this. Tax affairs are extremely complicated on an individual country basis, and they are even more complicated on a group basis. To unravel the picture from the enormous minutiae of detail and make a confident assertion about anything, really, on a global basis for a company like ours would be extremely difficult. It is also a question of who you are doing this for. We are completely transparent in our tax affairs. We file tax returns for every Government who have an interest in taxing us, or who are able to tax us. The information is provided to Governments. It is provided to the users of the information. I am not sure what purpose would be served by producing country-by-country accounts.

There is also the point that there is little consensus, if any, on exactly what those accounts should look like and how they should be presented. There is no accounting standard for them. In fact, there does not seem to be an emerging standard, either. My own view, and our view, is that we want to back off from the question and say, “What is the problem we are trying to solve, and is there another way of solving the problem?” That comes back to the debate about tax capacity in local countries.

On the question of sharing information between tax authorities, as long as taxpayer confidentiality is respected—that is confidentiality with respect to the outside world—we have no problem at all.

Christopher Lenon: In my previous role as Head of Tax at Rio, I led its development of country-by-country reporting. In its submission you have had this document. This costs a reasonable amount of money to produce. You cannot just go to accounting systems to retrieve the information, because SAP, which most of us use as our accounting system, is not set up in that way. There is additional work involved in getting to that. It is useful in showing how much tax companies pay, but as has been said, it does not tell you whether it is the right amount of tax. It can provide data that allow you to question whether, perhaps, too little tax is being paid, or why it is that a small amount of tax is being paid. The fundamental issue is that international tax, particularly in terms of income taxation, is fundamentally very complicated, and it is really only companies and properly resourced tax administrations who will be able to work out whether the right amount of tax is paid. Even if you put enormous amounts of data into the public arena, you still would not be able to work out whether the right amount of tax had been paid.

Country-by-country, which I think is a good thing, we have supported on a voluntary basis. All it does is to show you how much tax has been paid. You can then look at the accounts and get some idea of whether that is within a range, but because tax depends on a series of fairly complicated calculations, like capital allowances and so on, you will not be able, year by year, to say, “That is right; that is wrong.” And so on. It will give you a broad indication, but it will not tell you if the answer is right. The only way that you will do that is through a thorough examination of all the data provided to tax authorities.

To give you some idea, the returns that Rio produces in the US are that thick in terms of data. That is what is required under US law. You need that level of detail to work out the tax for those companies.

Q92 Mr McCann: One final point, Chair. Can I summarise your position by saying this: that you feel that no matter what you would do in relation to how much information you collated and how thick the books are in terms of the information publicly available, there would still be those and their communities who would level the accusation at you that you are not paying enough?
Good morning.

Q93 Jeremy Lefroy: Good morning. I have a couple of points, both of which are raised by things that Mr Mackay has said. First, there is the question of the informal sector that does not pay tax, which you referred to, and which I would imagine occurs in pretty much every industry. Would you not then see perhaps an opportunity within reporting to say, “This is the size of the informal sector. This is the amount of tax forgone by Government because of the existence of the informal sector. These are the health effects,” and so on. This would put the positive case alongside what you are already doing. That is one question—or proposal. The other side is that I am slightly mystified by the statement that individual countries are not producing statutory accounts. Presumably in every country in which you all operate your limited companies or PLCs, there is a legal requirement to file certain accounts. If that is not the case, should not we also, in addition to providing support to tax authorities, be saying to companies—such as yours, Mr Mutati—10 fastest growing economies in the world are in sub-Saharan Africa—“Let’s bring company law up to date.” The UK provides an excellent example of company law, as I believe does South Africa. Let’s bring that up to date. Let’s use the most modern forms. If SAP is not providing the kind of software that enables this kind of thing to be done, I am sure it could, if it was encouraged to do so. We also have things called international accounting standards. I am sure that you all report to those when it comes to the London Stock Exchange. Surely we should be encouraging all countries to move in this direction as they seek to encourage outside investment, which in turn will be far more confident in investing in countries that adopt these kinds of standards?

Emmanuel Mutati: May I pick up on that, on the issue of submission of statutory accounts? It is a legal requirement in Zambia for companies to submit their annual audited accounts to the Securities and Exchange Commission, and we have indicated that at item 5.1 in our document. At the same time, the accounts are lodged with the companies registry, and the public can access the accounts for the fee of $4. They are available. As we all know, there has been the EITI, which has been implemented in Zambia for the last two years. We have done two years—2008 and 2009—and we are now in the process of publishing what the mining industry pays to the Government, and what the Government receive from the mining industry. In 2008, the first year, there were some problems—about a 30% discrepancy; 2009 was much better, with an overall discrepancy of 1.5%. We are moving in the right direction.

Christopher Lenon: On the statutory accounts, the OECD has a taskforce on tax and development, on which I sit, and it has just done a project on statutory accounts. The conclusion from that is that there are a large number of countries where there is no requirement to file statutory accounts. A prime example would be the US, where there is no need. However, the pattern is varied around the world. The dilemma you have is that if you require countries to introduce statutory accounts, you clearly require that for all businesses that are limited liability. There is a cost to that. What information will you get from those statutory accounts? The dilemma is that the information you get from accounts, rather like voluntary country-by-country reporting, will give you some idea of roughly where you are, but it will not get you all the way to, “Is this the right answer or not?” because of the adjustments that are made between accounts and the final tax calculation. It appears to be a way forward, but I am not sure, based on the report that has been produced, whether it takes you any further forward. It does not get you all the way: it gets you some of the way, and there is a cost to imposing it.

Q94 Jeremy Lefroy: May I just come back on that? I may be wrong on this—as a chartered accountant, I may well be wrong—but it is my belief that one of the reasons why London and the UK are trusted, particularly as a centre for probably the world’s largest financial services industry, is our high standards of reporting. Therefore, shouldn’t we as a country be encouraging this in every country in which our UK-based multinationals—and indeed others—operate? I do not hear from UK-based companies that their shareholders and analysts have a huge problem with the kind of information that is provided. They are able to look at the tax note and say, “Yes, that makes sense,” or, “That doesn’t make sense.” I am not talking about small or medium businesses. We in Britain have exemptions for those anyway, so we recognise the burden of bureaucracy and the burden of reporting. However, shouldn’t we be encouraging other countries to move in the direction in which we have been moving since the Companies Acts of 1948 and 1986? We have had this progression and believe it is the right course to follow. Shouldn’t we be encouraging other countries to do that?

Christopher Lenon: It is the balance between the transparency and probity that you gain, and the cost that you impose—that is the dilemma. What do you actually gain from making that imposition that you cannot gain from having a better resourced tax authority working out the right tax? They are the trade-offs that you have to look at.

Q95 Jeremy Lefroy: I am not sure that I see it as an either/or. We are not saying that we can get there tomorrow, but I see it as a both/and. As I say, six of the top 10 fastest growing economies in the world are in sub-Saharan Africa, and of course, looking further beyond, there is tremendous progress all around the world. We would be encouraging the local accountancy firms and local people to say, “This is an area in which we need to invest.” As we all know, one of the great problems that those of us, including me, who have worked for many years in developing countries have is finding sufficiently qualified finance professionals not just in the accountancy firms, but in business. We often have to bring expatriates in, because we don’t find enough
there. Surely this would be one way of promoting a higher-powered accountancy profession in all the countries in which we operate, which is to all our advantage.

Graham Mackay: I am not a tax expert, but all I would plead in this particular line of argument is that if that is the course that Her Majesty’s Government would pursue, it should be via the sovereign states—

Mr McCann: Of course.

Graham Mackay: —and not by using UK registered companies as a stick to beat them with. This proposition would work only if it were adhered to completely on a local basis, not if the sole UK multinational in town were the only one that produced statutory accounts. That would not get you anywhere. Can I just pick up two other points from this particular part of the debate? One is the suggestion that of course we should make these facts known to the local Governments, and persuade them to extend registration and formalise the local industry—of course we do that. We do it constantly in many countries, in fact with a great deal of success from time to time. It is not always successful, but it is a long debate, and unfortunately continuity within Governments and civil services cannot be assured, so you win one year and then you do a bit of backsliding the next.

The problem with doing that in public is that it embarrasses the Government, because you are laying on the table your private negotiations with the Government, or private discussion with the Government. We are not pleading for anything special for our company. We are simply trying to get them to create a level playing field in that country, but it is quite a politicised process. We cannot make it public, and I think it would be counter-productive if we did.

The other point that I would make is that the phrase “the right amount of tax” has been used several times. We pay the right amount of tax. We pay exactly what “the right amount of tax” has been used several times. We pay exactly what we owe, legally, to every jurisdiction we operate in. We pay the right amount of tax. We pay exactly what we owe, legally, to every jurisdiction we operate in. The other point that I would make is that the phrase “the right amount of tax” has been used several times. We pay exactly what we owe, legally, to every jurisdiction we operate in.

As far as that is concerned, that is right. If you want to judge what is the morally right amount of tax, or the right amount of tax for development or for the long term of the country, you cannot do that from one year’s accounts—first, because they are far too complex; and, secondly, because they do not give you a pattern. You cannot form a view as to where all this stuff came from and where it is going to.

Investment allowances are a very good case in point. The fact that you happen to have investment allowances in the country, which drives you into a tax loss position for a couple of years—is that bad? It happens here; it happens in the whole world. Africa should be allowed to do that, too. In essence, we don’t think that there is any way to get at this problem through simply enforcing some level of global transparency. We don’t think that that will work. We think that the suggestion of raising tax capacities and capabilities of a country is the way forward, plus all the work that is being done by the OECD and so on. This transparency drive to achieve a right outcome is, we believe, doomed, quite frankly.

Q96 Pauline Latham: Before I start, may I just draw attention to the Register of Members’ Interests in respect of SABMiller?

May I change the subject slightly on to transfer pricing laws? Do you all think that the current transfer pricing laws are appropriate, and do you think they are effectively enforced? Rio Tinto argues in its written evidence, which was referred to earlier, that companies should be required to provide information on related-party transactions on their annual tax returns. Would you all support that?

Tim Scott: Yes.

Q97 Pauline Latham: Is that yes to everything?

Tim Scott: Yes.

Pauline Latham: That is very clear, thank you. Does anybody else have any views?

Chair: Has anybody got a comment?

Pauline Latham: Does nobody else have any feelings about the transfer pricing laws and whether they are appropriate?

Q98 Chair: The point is that people who have given evidence—or complained about this—say that transfer pricing is a way of moving resources to the lowest tax denominator, I suppose. What we are saying is: to what extent do you feel that that can happen, or does the enforcement actually cover it?

Tim Scott: Can I add a bit more, in that case? Transfer pricing is a neutral term. A transferred price is what occurs when one member of a group sells or transacts with another member of the group. The concern of many people, including ourselves, is to make sure that the transaction is fair, that the price is the right price, and that it is ostensibly the price that would have occurred had the two parties not been related to each other.

When people talk about transfer pricing as some sort of dark art, I think it is slightly misconceived. What they should be talking about is “transfer mispricing” or the abuse of transfer pricing. Transfer pricing is not an avoidance technique at all. Generally around the world, including in the countries in which we operate, including Zambia, there are laws under tax legislation that enforce this principle of arm’s length, correct transfer pricing.

Q99 Chair: Do you refute the allegation that companies—I am not saying your company—use transfer pricing to transfer assets from a high-tax regime to a low-tax regime? In other words, people will say, “It is amazing how much copper is transacted in the states of Jersey or the Cayman Islands, which do not produce any of these things.” That is the charge that is being levelled. In simple terms, do you believe that that fundamentally does not happen, or that the system can expose it, and that the allegations are therefore somewhat misplaced? Is that what you would say?

Tim Scott: I can only really speak for Glencore, obviously, because I see only what happens within the Glencore context. That is, of course, the case. Transfer pricing is ostensibly arm’s length—it is demonstrably, transparently arm’s length—and we would be willing to speak to tax authorities about this, as we do, all
the time. More broadly, the question is whether other people abuse it. I somehow would doubt it, because I think that most tax authorities, including the Zambian ones, are perfectly capable of looking at a transaction. They have the right—and they do—to audit the books and raise these questions. On a consistent level, so that there were macro-economic effects of this practice, I don’t think that is likely.

Q100 Mr McCann: Can I put a direct question to Mr Mackay? You said in response to an earlier question, “We pay the right amount of tax.” The direct allegation against companies like yours is that you manipulate your figures so that you can minimise the amount of money that you pay tax on. Therefore, I will put the direct point to you: has your company in any circumstances inflated figures, inflated transaction costs, or inflated service costs within your company in order to avoid or minimise tax that is paid?

Graham Mackay: Absolutely not. We operate within the OECD guidelines, so greater minds than mine have certainly concentrated longer than I have on these matters. The OECD guidelines are, we believe, fair. They have had a lot of thought put into them. The arm’s length pricing principle is a fundamental cornerstone of that. In fact, I should point out too that, in our particular industry, what could be called transfer pricing, which is essentially costs of services that cross borders, is very small, because our businesses produce, market and buy locally. It is not as though we are shipping a vast amount of commodities, or buying, processing and shipping them, as many companies do. We do not do that. Our production is all local.

In the case of Africa, for instance, we do have group buying, which is run for the Africa region out of a professionally established hub. The operating bosses of the business are at liberty to choose whether to buy locally or to buy from the hub. They are not incentivised on any profits made outside their own market at all. When they choose to buy from the central procurement agency, it is because it is a better deal for them. In fact, to come back to my initial point, the value of that stuff that goes on, compared with the size of the business as a whole, is minimal—it is very, very small indeed. I absolutely deny that allegation.

Q101 Richard Burden: I think I understand what you are saying: that you operate within the rules and that they are transparent. However, I am still not sure that you have answered the question: do any of your companies use transfer pricing to minimise or reduce tax liabilities? Even if it is transparent, do you do that?

Graham Mackay: We do not make charges or set up company structures for the purpose of minimising tax. That is not the purpose of doing so. We set up company structures to provide expertise and services to operating companies, which they would not be able to afford, or practically obtain, by any other means.

I should also point out that that is the way in which all multinational companies operate. It is simply not practical to imagine that one can buy a business, or start a business, in Ghana, Uganda or Zambia, or anywhere like that, and run it using local resources and expertise to modern standards, and bring it up to speed with the way we do that. It requires specialised knowledge and specialised skills. You cannot disperse those knowledge and skills because they are not available on that sort of scale, and it would be wildly inefficient to do so. It has to be centralised and specialised somewhere. If it is specialised somewhere outside Ghana, say, it is irrelevant to Ghana where it is specialised in. The fact is that the Ghanaian business pays and buys a service, and buys it at good value, according to the arm’s length pricing treaties. That is it.

Q102 Richard Burden: Would that be the case—

Tim Scott: For Glencore? Yes. Our business, in fact, is slightly simpler than Graham’s. What we do is that Glencore buys metal from Mopani, and buys it at the correct LME price.

Q103 Richard Burden: And, from the OECD’s point of view, no problem.

Christopher Lenon: The issue is that we live in a world where there are significant intangible assets. If you look at most companies, and you look at their tangible assets and their market capitalisation, there is a significant gap. That gap is their intangible assets: their intellectual property, their brand, their benefits of operating as a group, and their knowhow. All that has to be charged for under the principles, because the principles say that if you provide a service, you should charge an arm’s length price. The principle is that most of that knowhow is located in OECD countries. In fact, the UK Government’s policy is to encourage that, and to encourage high-value manufacturing and intellectual property. Under the principles, it is therefore correct to charge for those benefits. Valuing those benefits is sometimes very difficult, and the OECD has a project at the moment on intangibles, but what companies seek to do is to operate within the principles. There will always be exceptions. I cannot say that every company that is a member of the Big Four will prepare their returns based on the arm’s length principles, and they will provide the information. However, the vast majority of companies using the Big Four will provide their returns based on the arm’s length principles, and they will provide the information. Therefore, I absolutely deny that allegation.

Q104 Richard Burden: If you were advising civil society, would you say, “You are barking up the wrong tree here; there is not an issue,” or, “There is an issue, but you are going about it in the wrong way?” If it is the latter, what is the right way they should go about it?

Christopher Lenon: The way you will see developing countries raise more tax is if they have more high-value activities occurring in—

Richard Burden: Yes, that is—
Christopher Lenon: No, hold on. Tax follows what actually happens in terms of your business model. Unless you have high-value activities occurring in your country, the likelihood is that you will be taxing lower-margin activities. If you are taxing lower-margin activities, you will raise less tax, so tax policy needs to follow on from economic policy, and economic policy should be seeking to encourage more higher-value activity to occur. That is facilitated by having an investment regime that is transparent, stable and based on the rule of law, and a tax system that follows on from that, which again is transparent, stable and well administered. My conclusion would be that you can tax only the activities that occur in your country. We have a world in which most of the higher-value activities occur in OECD countries.

Q105 Richard Burden: I absolutely understand. I tried to interrupt you before because I absolutely understand what you are saying about the kind of economic activity you want to incentivise in developing countries to maximise the tax benefits to local people, but that was not my question. My question was: in relation to transfer pricing, or mispricing, is there an issue that civil society needs to be getting at, and they are getting at it in the wrong way; or is there not an issue from the OECD’s point of view?

Christopher Lenon: My view is that they are probably getting at it in the wrong way, and the focus should be, as was said right at the beginning, on exchange of information to deal with tax avoidance and evasion in developing countries. This is a very important area that needs to be worked on. It is probably going too slowly in terms of developing that network. That is an important area. Capacity building, which has been referred to on a number of occasions, is equally a very important area. Unless you have tax administrations that can devise tax policy, administer that tax policy, and collect the taxes that that tax policy intended to be collected, you will not have a fully functioning tax administration. Those are the two areas that are key to improving tax in developing countries.

Q106 Mr McCann: Can I just ask a follow-up question to that, Mr Lenon? Do you believe that companies are taking advantage of the lack of capacity?

Christopher Lenon: Having dealt with tax in developing countries since the late 1980s, I think there is a misunderstanding. I would rather deal with a well-resourced, well-functioning tax administration than one that is completely arbitrary—and I have dealt with both. The trouble with arbitrary ones is that they can make mistakes both in your favour and significantly against you. I would think that most business would see capacity building as the important area that we should focus on.

Q107 Mr McCann: But is it capacity building only up to a certain point that allows them to behave in a way that gives them more profit, and are they taking advantage of that? I am not asking the question of whether you would want to deal with someone who is unprofessional or who is professional. I am asking: is there capacity up to a certain point, and are companies enjoying an additional benefit because that is not moved to an optimum level?

Christopher Lenon: I think we should aspire to capacity building where tax authorities in the developing countries are of the same standard and quality as they are in OECD countries.

Q108 Jeremy Lefroy: I should also draw attention to my entry in the Register of Interests, similarly to Mrs Latham, about a visit that we paid to Nile Breweries last year, which was extremely instructive, and showed the involvement of the brewery with smallholder farmers, which I think we appreciated, as well as in the local health system.

May I ask a follow-up question on the previous one? Rio Tinto has argued in its evidence that companies should be required to provide information on related-party transactions as part of their annual tax returns. I wondered whether you would all agree with that?

Tim Scott: No problem. Absolutely right.

Q109 Jeremy Lefroy: So that is something that we should recommend.

Tim Scott: Yes. Yes.

Christopher Lenon: If you look at the US, Canada or Australia, there is a requirement in all those tax returns to provide a full schedule of your transfer pricing transactions. I think what Rio is proposing is that some form of standardised schedule should be adopted as best practice so that the information is available but, because it is standardised, it is much easier for businesses to set up their systems to provide that information in a consistent way.

Q110 Jeremy Lefroy: Thank you very much. I would like to move on to a question about minimising tax liabilities. Would it be safe to assume that all the companies represented here would use legal means that are available to them to minimise their tax liabilities?

Tim Scott: No, I don’t think that is a fair way of putting it. We obviously do not pay more tax than we have to under law, but we do not pay these so-called clever lawyers and accountants to find loopholes through the law that, although they legally work, result in us paying less tax than we should be paying. There is a moral element to this as well, which we are aware of. We pay what is the right amount of tax—the tax that the Government would be expecting to receive—according to the spirit of the law, and not necessarily the letter that we have managed to find a way around.

Graham Mackay: Yes, I agree with that completely. You do not pay more tax than you have to, but there is such a thing as aggressive tax planning and non-aggressive tax planning. We are not aggressive tax planners. We do not do things purely for tax reasons, and we certainly do not set up company structures such as we are talking about here for tax reasons. They are for sound commercial reasons. Tax is a huge cost. It costs us more than anything else, including raw materials. It is obviously something that
you pay a lot of attention to, and that you minimise within certain parameters, but those parameters are clearly understood.

Q111 Jeremy Lefroy: Clearly, one of the major ways in which tax liabilities are minimised is through capital investment, because with capital allowances of often 100%, that reduces tax paid. Do you think there is sufficient understanding of the fact that the reduction in the tax liabilities, or at least the deferral of tax liabilities, is a consequence of the investment that everybody is seeking?

Graham Mackay: As a matter of fact, for our corporate income tax in our African subsidiaries, our effective rate is higher than the statutory rate, as a result of running out of capital allowances. So they are perfectly legitimate, and the net result is that they do run out. They encourage investment. The regimes differ dramatically from country to country, as I am sure you know—not just within Africa, but in the rest of the world as well. It is a matter of record that our own corporate tax rate is in the upper quartile of the FTSE 100. It is not aggressively managed at all.

Christopher Lenon: In terms of capital allowances and any form of tax incentive, what tax administrations need to do is to ensure that they are doing the right cost-benefit analysis of the tax forgone. That would apply to any Government, be it OECD or developing country. Obviously, it is true that in situations where there is significant investment, it is likely to wipe out the corporate tax liability for a period of time. However, people don’t invest to get capital allowances; they invest to make money. The tax follows the investment, but the key is that Governments have the capability to make the right policy choices in terms of the tax incentives that they provide in their codes. That, again, comes back to capacity.

Q112 Richard Burden: My question is specifically to SABMiller. You will know that we have had written evidence from ActionAid in which it refers to a report that it has written that mentions your company specifically. I don’t intend to go through the allegations in that report, other than to say that my understanding is that it is not accusing SABMiller of tax evasion—in other words anything illegal—but I guess it does draw a similar distinction to the one that you drew about issues of morality. It talks about some actions and policies that SAB pursues as being, I think, ethically questionable. You have referred to there perhaps being a problem in some companies with aggressive tax planning. I guess you were getting at the same sort of territory there. Specifically on what ActionAid said about SABMiller, could you give SABMiller’s position on those allegations?

Graham Mackay: We think—actually we don’t just think; we state—that ActionAid’s allegations and inferences are squarely wrong. It accuses us of transferring profits out of Africa into tax havens, in essence, in legal but morally dubious ways. That is not what we do. We have a number of service providing centres, which charge at arm’s length rates for the services they provide. Any effect on our overall tax rate of any of these activities is absolutely de minimis; it is not even a rounding error. We derive no tax benefits from any of those activities whatsoever. They are simply commercially efficient service charging mechanisms—that is that.

Q113 Mr McCann: Did ActionAid contact SABMiller directly before the campaign started to allow you to answer any of those allegations?

Graham Mackay: It did, and it ignored our replies.

Q114 Mr McCann: How detailed was the reply that you sent in relation to the individual allegations that it made?

Graham Mackay: We gave detailed written replies.

Q115 Mr McCann: So, in terms of the points that were made about intra-company transactions, royalty payments for the use of trademarks, management and service fees, procurement payments and interest on loans from sister companies, which is estimated at a value of £100 million—I must get my currency right—you answered every one of those detailed points before the campaign started?

Graham Mackay: Yes. We met it on three separate occasions to discuss its allegations in detail, and wrote it a letter.

Q116 Pauline Latham: This is to Glencore. Obviously, most people in the room will be aware of the leaked report and the allegations made in the Grant Thornton report. Will you set out Glencore’s position on those?

Emmanuel Mutati: Yes, please. The advisors to the Zambia Revenue Authority, together with the Revenue Authority, carried out an audit at Mopani. They had indicated to Mopani that a draft report would be discussed with Mopani before closing it out. Unfortunately the report leaked in the paper. The Zambia Revenue Authority described that as a “confidential, preliminary and incomplete draft” of the report, as we have indicated in our paper in item 5.3. We have been in discussion with the Zambia Revenue Authority, and we are about to close the issues that we have at hand with the Zambia Revenue Authority.

Q117 Pauline Latham: The Centre for Trade Policy and Development, which is a Zambian organisation, told the Committee that it had filed a complaint with a Swiss national contact point regarding the case, but Glencore had refused to co-operate. Is that true?

Tim Scott: No, that is completely untrue. In fact it did—a Swiss Economic Ministry agency called SECO. We went to speak to SECO for some time and went through these allegations specifically with it. SECO is completely content with our answers. We have no case to answer as far as it is concerned. What SECO then did was to ask whether we would speak directly with the NGO, with SECO acting as a mediator. We said, “Yes, we would be perfectly happy.” As far as I understand, that process is ongoing, I would add that anyone can come to Glencore and talk to us.
Q118 Pauline Latham: What do you think the motivation is behind all these accusations against the companies that you represent here?

Tim Scott: I do not want to speculate about people’s motivations, because I completely respect concerns about desperately poor countries and the living standards of people in them. We are trying to do our bit to build the economies of those countries. I have no argument with people’s motivations. The situation that we have got into at the moment is primarily, or indeed uniquely, because of the leaking of this draft, incomplete report to the press. This in no way was a final conclusion on any aspect of our business in Zambia, but it has been taken as such, and people think there is a case to answer, which obviously there is at this point. We have answered it to you in our written submission, and we are speaking directly, of course, to the Zambia Revenue Authority. Any NGO that wants to speak to us as well is perfectly welcome.

Q119 Mr McCann: I fully take on board the points you make about it being a draft report that was leaked, and the various issues in it. One of the things that had been raised was that the single draft audit that was, I thought, progressively leaked at every stage. I wondered what the interactions had been between the company and the auditors. Were there discussions between them as the report was being put together, and an ability for misunderstandings to be resolved? What was the agreement on the draft report? Was that to be shared with both sides—an opportunity to, again, sort out any misunderstandings before a final report would be concluded?

Emmanuel Mutati: The audit was undertaken by the Zambia Revenue Authority, and they were the ones present on site. We were not aware of who the advisors were who were working with the Zambia Revenue Authority. We co-operated as much as we could. In fact, initially the proposal was that they would do the audit offsite—in the capital city, 400 km away—and we suggested that they come on site and do the audit, because we have the resources on site, and that would assist them in their audit. They agreed to come on site. We provided all the information and answers they wanted. In fact, it is on record that the Zambia Revenue Authority wrote to Mopani to commend it for the co-operation with the audit. We were surprised to hear comments that we were not co-operating; it is on record that we co-operated fully with the authorities.

Mr McCann: Thank you.

Tim Scott: I will add, if I can, that I don’t believe we ever saw a draft of this report by Grant Thornton, or had any ability to respond to it before it was leaked to the press. That is correct, yes?

Emmanuel Mutati: Yes.

Jeremy Lefroy: I realise we are running out of time. I wanted to ask a rather technical question about hedging, but maybe we do not have time for that.

Q120 Chair: There is just one final question, and I hope you appreciate that these are allegations that have been made, and it is a really good opportunity to have them answered and addressed. The final one, relating to local taxes for the Mopani mine, is that those of us who visited the mine also afterwards met the mayor and some of the local council, and they stated that they were angry, but also disappointed that in their view, Mopani should have been paying to the local authority ZMK9.4 billion per year, whereas Mopani the mine said that ZMK2.4 billion was all that they were prepared to pay. I gather there is a court action ongoing about it. As you will appreciate, we got a very bald statement: “They owe us ZMK9.4 billion; they haven’t paid it. What’s going on?” I wondered if you could tell us precisely what the basis of the dispute is.

Emmanuel Mutati: As we have stated in our document, we pay our dues in line with the Act—in line with the law. The Mulufira Council, we believe, has acted outside the law, in the sense that it has included two plants—specifically the smelter and the refinery—in the evaluation, which the Act does not provide for. Those are classified under the Factory Act. They are not supposed to be included, and that is where the dispute is. We have met with them once, and we are due to meet them in the next week or so to resolve the issue. We believe that we will resolve this. We have asked theMulufira Council to come to Kitwe, and we have resolved that. We believe that they will now see our side of the story, and we will be resolving the issue in the next week or so.

Q121 Chair: You would accept that it is not a particularly happy situation for a major employer such as yourself that is operating in a community to be in dispute for whatever reason with that local community. The mayor was a reasonable man, I thought. He simply defended the line. The district commissioner, who was also at the meeting, said that the company was engaging, and when there were accusations, he said, “It is not true that they are not talking to us.” He did acknowledge that. Nevertheless, it seemed to me that this had created an atmosphere in the community, and that it was in neither side’s interest to see it prolonged.

Emmanuel Mutati: Yes. Indeed. This is somewhat unfortunate. As I said, we act under the law, and if the council includes assets that are not covered by the applicable law, we have to discuss with them and say, “We can pay according to what the Act says.” Unless the Act is amended, we cannot do otherwise, and this is what we have stated. We said that once we agree what is supposed to be paid under the Act, we will pay, including the outstanding due to date. We have continued to pay them, but on the old rates. We are saying, “Once we resolve, we will pay you whatever the balance ought to be.”

Q122 Chair: Yes, because you provide hospital facilities and school facilities, albeit at a fee, within the community. There is no connection between that degree of goodwill and, if you like, corporate social responsibility, and this very specific dispute about the revenue you pay to the local authority?

Emmanuel Mutati: We do assist them a lot. In fact, there was recently an outbreak of typhoid in a council area, and we were the major player in that regard. We provided a new pump, a new generator, medicines, access to a laboratory and access to hospitals. We
support them in many ways that I think they may have disclosed to yourselves.

**Q123 Jeremy Lefroy:** This is just a general question, and refers to a comment of Mr McKay’s at the beginning, which is the perception and perhaps the reality that large companies are targeted by revenue authorities because they are seen as effectively milk cows for tax revenue. Certainly, with my experience in one or two countries, I would concur with this. One thing I have often advocated, but which perhaps not surprisingly has not been taken up, is the disclosure of the total amounts paid by all major businesses within a country, whether multinational or nationally owned. Would you see that as a step forward? It might identify not only the amounts that were being paid, but also the amounts that were not being paid by some fairly major businesses, which are perhaps not multinational, which is a perception that I have often had.

**Tim Scott:** I do not think that that necessarily will assist in any debate. To take ourselves, for example, we are in a start-up phase where a massive, $2 billion-worth of capital expenditure means that capital allowances are essentially deferring our cash payments of income tax well into the future.

**Q124 Jeremy Lefroy:** May I interrupt you? You have already declared, understandably, the amount of taxes that you are paying. We saw advertisements in a Zambian magazine when we were there. You should have nothing to fear from this.

**Tim Scott:** No, but people will compare these two reported profit figures and ask what the difference is.

**Q125 Jeremy Lefroy:** I am talking about total taxes—not just profit taxes, but the total tax.

**Tim Scott:** The total tax? Correct.

**Chair:** I think we saw First Quantum, wasn’t it, with an advert in one of the in-flight magazines we saw in Zambia, saying, “This is our turnover, this is the tax we have paid, this is the number of people we employ, this is the PAYE, and other social benefits we pay.” To be honest, it made a very positive story. I take your point that if you have $2 billion-worth of investment, your profits contribution may not look so good, but even so, if you state all of that, and show what the offsets are, doesn’t it actually help?

**Q126 Jeremy Lefroy:** The reason I ask this is that a company I was involved in was awarded a certificate for being the second largest taxpayer in a particular region, which we were very proud to be. The fact was that we were very surprised to hear that we were the second biggest taxpayer, given that we felt we were a fairly small company. Were more information of that sort put into the public domain, it might encourage people to find out who was not paying their taxes. I am sure that none of those represented here would be at all afraid of that.

**Graham McKay:** I am not sure it would have much effect, to be perfectly honest. These things are broadly known. We recently received a “Taxpayer of the Year” award in Mozambique. It’s the same sort of thing. We pay far more tax than anyone else.

**Q127 Jeremy Lefroy:** Is that implying that the tax authorities are, should we say, not looking sufficiently hard at many major businesses within their jurisdiction?

**Graham McKay:** It is politically more difficult, and it is much more work.

**Q128 Mr McCann:** Can I just follow up on the question you asked, Chair, of Mr Mutati? Just to be clear, there is no connection between the local tax dispute and any of the additional services that the company provides to the local community.

**Emmanuel Mutati:** No, there is no connection.

**Graham Mackay:** Chair, could I just record a correction for the record? I stated earlier that we had met ActionAid three times. In fact, I have just been told that the situation is that we met it once, and we answered three sets of questions formally.

**Chair:** Thank you for putting that correction on the record. Can I say to all four of you: thank you very much for coming along and giving us evidence? Obviously, we have had a lot of written evidence from you and your critics, but an oral hearing like this gives us an opportunity to press those points, and you—I hope you agree—the opportunity to explain your perspective. The Committee is looking for evidence. We are not interested in allegations that aren’t substantiated. We want to make sure that we get the facts. The ultimate objective—I think this is your point, Mr Lenon—is to see a situation where developing countries genuinely develop, and where in the process of developing their capacity to raise revenue from all sources improves to the point where they become less dependent on aid and more able to fund their own services. That is what we as a Committee are interested in. Obviously, major investors like yourselves have a significant contribution, but as you have all said, you are not the only players, and you shouldn’t be treated as the only players. There are others as well. Thank you very much indeed. We really appreciate the fact that you have come and given us evidence.
Examination of Witnesses

Witnesses: Eddie Rich, Deputy Head and Regional Director (Southern and Eastern Africa and the Middle East), Extractive Industries Transparency Initiative, Dr Odd-Hege Fjeldstad, Research Director, International Centre for Tax and Development, and John Christiensen, Director, Tax Justice Network, gave evidence.

Q129 Chair: Thank you, gentlemen. I think I can just say good morning. Thank you for coming in to give evidence. I think you have heard the evidence we have just had, but again, for the record, I wondered if you could introduce yourselves, perhaps starting with you, Mr Rich.

Eddie Rich: Thank you, good morning. My name is Eddie Rich. I am the Deputy Head of the EITI International Secretariat, and I also have regional responsibility for various countries, including Zambia.

John Christiensen: Good morning. My name is John Christiensen. I am the Director of the Tax Justice Network’s International Secretariat. I am a member of the OECD’s Taskforce on Tax and Development, and a member of the Global Taskforce on Financial Integrity.

Dr Fjeldstad: Good morning. My name is Odd Fjeldstad. I am Research Director of the International Centre for Tax and Development.

Q130 Chair: Thank you very much indeed. You have obviously seen the written evidence and heard the exchanges we have just had with representatives of the business community. Perhaps first of all I might just ask you whether there are any particular comments you would make on the basis of what you have heard. Are there any particular things that strike you, perhaps starting with you, Mr Rich?

Eddie Rich: I pass that on to colleagues.

Chair: You defer to Mr Christiensen.

John Christiensen: I am happy to make a couple of comments. First, I welcome the broadly positive response to the issue of information exchange. I did not hear any negative reactions to that and certainly the Tax Justice Network’s point of view is that improved information exchange is a crucial part of deepening transparency.

Secondly, on the issue of country-by-country reporting, I think that the talk about cost to companies is very often overstated. The figures that have been put to the OECD’s Task Force on Tax and Development relating to the additional cost of the accounting provision and of the audits that go with it were frankly very modest indeed. It is not that huge a cost. I would make the point that when they talk about the use of SAP for accounting systems, if these accounting systems were modified to accommodate country-by-country reporting, it would significantly reduce the costs, so I don’t think that cost is really that large a barrier to implementation of country-by-country reporting.

I would say, however, from my point of view, that while voluntary approaches are always good news in some areas, in areas where there are clearly some companies that want to abide by good practice on tax, and some companies that do not, a voluntary approach is not adequate. A mandatory approach, or rather an international accounting standard adopted globally, is the appropriate approach to country-by-country reporting. It is, after all, the bad players who we are trying to tackle, not the good payers. For that reason, good practice needs to be encouraged, and not undermined by making this a voluntary approach.

Finally, I would like to comment about the arm’s length principle that was referred to. Most of the experts within my network would say that the arm’s length principle is deficient in many, many key areas. Its application particularly to intangibles, as Chris Lenon acknowledged, has always been a problem, and is an increasing problem. The arm’s length principle, which is the principle at the heart of the OECD guidelines on transfer pricing, is one approach amongst others. In the long term we need to think about very different ways of taxing multinational companies.

Q131 Chair: Just on that point, I thought Mr Lenon explained it really quite well. They are intangibles; therefore they are difficult to quantify. What kind of international standard could you apply? These things are highly subjective.

John Christiensen: Absolutely.

Chair: They can obviously be abused, but at the same time, people say, “This intellectual property, this technique, or this process is hugely valuable, and we are pricing it at that real value.”

John Christiensen: That is quite correct and I obviously have experience within the industry of trying to apply the arm’s length principle to intangibles: management services, copyrights, licences and so on. From an economist’s point of view it is immensely difficult. It is highly problematic and therefore open to abuse. In the long run, my own view is that we should be moving towards taxing companies globally on a unitary basis, using a formula of reapportionment as the basis for taxation, which is the general trend that the European Union is trying to push through its own initiative.

Q132 Chair: Dr Fjeldstad?

Dr Fjeldstad: There was a question related to whether companies took advantage of lack of capacity in the Government or tax administration in poor countries, and the impression I got from the companies here was that, no, they stick to the law. I found that response a bit vague, because we know that tax planning takes place everywhere—in the UK, in Norway, where I am from, and so on. Of course, if companies have the opportunity to take advantage of weak tax legislation and administration, we would expect that they use it. We see a number of examples of that. For instance, if you look into the tourism sector and hotels, etc., every five or six years they change names to another company, because of the five-year tax holiday. This is an exploitation of the system.

That is one thing. Another thing that was referred to, and with which I agree to some extent, is that there is a need to build tax administrative capacity. However, the major constraint in countries such as Zambia, Tanzania, Mozambique and other countries in Africa is weak tax legislation. Tax policy is the major constraint, which is reflected in these extensive tax
exemption/tax incentive regimes, which imply huge losses of revenue. In Tanzania, for instance, one estimate suggests that the total tax exemptions represent 6% of GDP. That is a huge revenue loss.

Q133 Chair: That is helpful. Perhaps I will come back to you, Mr Rich, on this issue. The EITI was set up initially by the UK, but it is now genuinely international. Its aspirations obviously are something that we would all support. What do you think are its real benefits? To what extent can it deliver what it says on the tin—transparency?

Eddie Rich: I think EITI probably needs to be placed in the context of the wider development debate at the moment about what replaces the Millennium Development Goals. Hillary Clinton, speaking at the Open Government Summit last week in Brasilia, talked about it, characterising the development debate as having moved on from north and south, to open and closed countries. EITI is really one of many mechanisms out there that are being developed to help Governments, companies and civil societies, and to help the debate to move towards more open processes. In terms of answering the question, “What benefits does it have?” we need to understand the context in which each country will come to sign up to and implement it. There will be different reasons in different countries, because their reasons for wanting an open process will be different. The EITI itself, as you say, Chair, was established by the British Government in an announcement at Johannesburg in 2002. At that point it was just an initiative, and then it went through many, many internal discussions with people coming to the table, and developed into a standard. I don’t think that development of an international standard occurred until 2006, when there was established a board and a secretariat as well. Since then, 35 countries are implementing the process. That is 900 million people now with access—in many cases for the first time—to reports with reliable figures of how much money is coming into that sector. This year there will be around 50 of those reports from around the world. It has evolved very fast. There is a lot of information on the table. What does that amount to? That is the issue that we need to move on to. We have been challenged to do that, to some extent. We had an evaluation last year that said, “EITI has been very successful in developing a process and in spreading information, but it doesn’t answer some key questions. It answers how much money is coming into the sector in these countries, but it doesn’t ask how much money should be coming in, whether the right amounts are being paid, how the money is being spent, and so on.” These are the challenges for the future. At the moment there is an ongoing strategic process to look at how the EITI can perhaps develop from being a standard to being a process that allows each country to develop the framework in their own useful way. I would identify quite a few areas, though, where from country to country you see strong, anecdotal and in some cases quantitative information on the benefits: an improved investment climate, increased tax revenue, better tax collection systems, greater stability and trust between the various actors around the table—we heard the discussions from Zambia—and civil society voice and protection. However, those are very variable across the 35 implementing countries. In some cases we can see that really making a societal change and improvement in Government policy; in some cases, frankly, the process has to be more rigorous to expect to see some of those enhancements.

Q134 Mr McCann: There have been some suggestions that EITI could be improved and strengthened, and for example that participating countries should be required to compare their tax receipts with GDP figures, or with profit figures for the extractive industries, and the question of whether participating countries should be required to compare tax receipts from the extractives sector with the quantity of resources extracted. Perhaps I will put it to the Tax Justice Network first: do you think these are good ways of strengthening EITI, or are there other ideas or views that could help us in this area?

John Christiensen: I should preface by saying that my own involvement with EITI and Publish What You Pay generally has been around the issue of country-by-country reporting. Certainly, I think that greater transparency over not only what the tax receipts are, but what contractual deals are being done behind the scenes, and above all a clearer understanding of the costs of tax exemptions—what are the tax expenditures involved in these deals?—needs to be developed. This point was made by one of the previous panelists: building capacity to undertake cost-benefit analysis on tax exemptions and tax expenditures generally would be a very, very important way forward. I would like to see more emphasis on that area as well. I have just heard quite a stunning figure: 6% of Tanzania’s GDP is absorbed in tax exemptions. That is an extraordinary figure. I don’t know whether there is sufficient capacity at a political level to understand the implications of granting these kinds of exemptions. As far as I am concerned, the Tax Justice Network’s engagement with EITI has largely been through developing country-by-country reporting as an appropriate standard for disclosure.

Dr Fjeldstad: Certainly transparency is important, and EITI has initiated a very important process, but also, as Eddie Rich here says, what EITI reports is what is coming in, or what the Government have received. The challenge is, of course, what should have come in. One key area to strengthen the revenue side from extractive industries is to build up more physical measurement systems, where Government can hire people to measure physically what the resource base is, the purity of resources and how much resource has been extracted from individual mines. This physical measurement system was a key component when Norway developed its petroleum tax regime. This is also something that Tanzania has now developed in the mining sector: Tanzania Minerals Audit Agency. It is quite unique. They have people—geologists, accountants, etc.—in all the mines. They started this process a few years back. Now they are developing capacity. That is essential if you want to move towards a regime that says not only how much
is reported or received, but how much should have been received.

Q135 Pauline Latham: Could you tell me exactly how much EITI receives from DFID?
Eddie Rich: I don’t have the exact figures, but it is receiving in the order of $250,000 per year.

Q136 Pauline Latham: Can you tell me why you think the UK has so far been reluctant to implement the EITI, considering it brought the idea to fruition in the first place?
Eddie Rich: That’s a very good question. I am not sure I can. To some extent, the question that we have heard back is that they say to us, “We need to be convinced that it is of domestic value.” I was interested to hear what the CBI said to you last week when it was talking about the EITI. It said, “Any way in which the EITI could be extended would be very beneficial. (In that regard, we would note that the United States has just agreed to join the EITI, and we believe that EU Member States could also set a positive example by signing up.)” If the CBI is supporting implementation in this country, I think there is a strong domestic reason. I also think that it echoes very strongly what President Obama said when launching the EITI process in the US. He is ensuring “that taxpayers receive every dollar they are due from the extraction of natural resources.” Now the size of the sector is not maybe so large in the UK. It may be dwindling to a large extent, but those arguments seem to me to be very powerful here, just as they are in Norway, just as they are in any of the other 35 countries. It is a good example of where, as I was saying at the beginning, we are moving with these development processes from this north and south to open and closed countries. There is no longer a clear distinction that can be written between domestic policy, and foreign and development policy. There needs to be a signal related to multinational companies, certainly including specialised expertise into the more complex tax issues related to multinational companies, certainly including extractive industries, to build specialised tax audit capacity within the revenue authorities. This is not only with extractive industries, however, but also the financial sectors, complex sectors, the tourism sector, telecoms, and so on. There is demand for this. I think the UK is looking a little left behind now on this. Australia is piloting the process. Last week, Colombia and Ukraine committed to implement it, and people are asking us—in Uganda, in South Africa, in Brazil—“Where is the UK on this?” It becomes difficult for us to make the case that these other countries should be doing it when the first question they have back is, “You started it; where is your implementation?”

Q138 Chair: It is strange that the United States is considering signing up and the UK, as yet, does not. You mention Norway. Every time you look at the list, you immediately think, “Where is Uganda?” for example—they have just discovered oil. If we are not setting an example as developed countries, it looks like a thing that was set up for poor countries with resources, rather than a more aspirational standard that says, “What we are trying to do is set up global standards of transparency to which rich and poor countries should all sign up.”

Eddie Rich: I think the UK is looking a little left behind now on this. Australia is piloting the process. Last week, Colombia and Ukraine committed to implement it, and people are asking us—in Uganda, in South Africa, in Brazil—“Where is the UK on this?” It is becoming difficult for us to make the case that these other countries should be doing it when the first question they have back is, “You started it; where is your implementation?”

Q139 Jeremy Lefroy: When we visited Burundi last year, we discovered that the UK, through DFID, was assisting Burundi—the Office des Recettes— with technical advice and immediately they had seen a substantial increase of 25%, I think, in tax collection. Clearly that was extremely beneficial to the Burundian Government and showed the advantage that such advice can bring. Perhaps I could ask Dr Fjeldstad first: could you perhaps give us a summary of how you see that technical assistance to revenue authorities can benefit those countries? You have already referred to weak tax legislation, but are there other ways in which assistance to revenue authorities can help those countries?

Dr Fjeldstad: I will start by saying that several bilateral and multilateral agencies have already contributed substantial support to build capacity in revenue authorities in a number of countries. DFID has certainly been very instrumental in a number of countries, including Uganda, Zambia and Tanzania. They are also involved in the common basket in Mozambique, etc. That has been very important to build up the basics—the essentials of running a revenue authority. I could also add the Rwanda Revenue Authority. In some of those countries—I will say most of the countries I mentioned—the revenue authorities are probably among the best functioning public institutions in the country, relatively speaking. That does not mean that there is no need for further development.

What is now required is, first, to build more specialised expertise into the more complex tax issues related to multinational companies, certainly including extractive industries, to build specialised tax audit capacity within the revenue authorities. This is not only with extractive industries, however, but also the financial sectors, complex sectors, the tourism sector, telecoms, and so on. There is demand for this. I returned just a few days back from Zambia after having had intense workshops with the Zambian, Tanzanian, Mozambican and South African revenue services, and this is a demand that is cross-cutting. Secondly, there is a need to build research and policy analysis capacity within the revenue authorities. Most
have research and policy departments. They are very good at collecting data, but very weak at analysing and using the data. Finance ministries have, to some extent, been left out of the equation. There has been a lot of focus on building administrative capacity in the revenue authorities, which is very good—there is more need, as I mentioned. However, tax legislation and tax policy are a major challenge, and the policy analysis divisions of the finance ministries really need to be lifted up.

Q140 Jeremy Lefroy: Perhaps you could comment specifically on the case of Zambia, since we are looking at that. Is there anything, apart from those general points, that you would like to raise specifically with regard to Zambia?

Dr Fjeldstad: When it comes to extractive industries, certainly. The mining sector is potentially a major revenue source in the country. It is not one yet. There is a challenge with access to information from mining companies. That is a cross-cutting issue that I have discussed both with the Ministry of Finance in Zambia and the Zambia Revenue Authority. They have problems gaining access to information from the mining companies. A problem with the legislation in Zambia is that third party information cannot be used, by law. It is not like in our countries, or at least in Norway, where the revenue authorities can go to the banks and get information on individual clients and companies, etc. That is not allowed by the banking sector or financial sector in a country like Zambia. The same is the case in Tanzania and Mozambique, and many other countries. Access to third party information is a major problem. This can be done through legislation.

Q141 Chair: Mr Christiensen, you were nodding. You wanted to comment?

John Christiensen: Yes, if I may. I strongly support building up a commitment to technical capacity building, but I think it needs to go beyond the tax revenue authorities. One of the things that strikes me, when I have travelled in many countries through electoral cycles, is how little public discussion happens around the issue of tax. Coming from a country like Britain, where tax feeds a huge amount of discussion come election time, and right the way through, it seems to be pretty well absent in many cases.

This is because there is a lack of civil society engagement on this. One of Tax Justice Network’s commitments is not just to working with the tax authorities on technical capacity building, although I think that is an important part, but to building public awareness around tax. When you look at tax compliance and the tax culture in many countries, it is very weak, and in some cases this is a heritage of the history of tax and the way it was imposed in earlier periods. There remains quite a strong resistance, and a feeling that, “We pay the taxes and it disappears, and we don’t get anything back from it.” This needs also to be put into a state building prism, where building democracy also involves building public awareness around taxes and getting the appropriate mix of tax policies. That is not just a technical issue for the tax authorities.

If you look, for example, in Britain, where you have organisations like the institute of fiscal affairs, they are very important in terms of critiquing tax policies and developing new ideas. Very often institutions like that are absent from the civil society dialogue, and that is another area where we need to build, expanding a tax policy dialogue and providing independent research. I am also very much in favour of creating an organisation called “Tax Inspectors Sans Frontières”. The idea behind this would be to take some of the superb technical expertise that is available to tackle transfer pricing abuse, for example, and to provide capacity for tax authorities in Zambia and elsewhere with that long-term support. When you investigate a transfer pricing abuse case, it is not a case of flying someone in for three months. You have to put people in there who might well spend five years working on that case and taking it all the way through the judiciary. There is a very strong case for having that kind of long-term commitment to building capacity in that area.

The final thing I keep on flagging up is that in many developing countries—and elsewhere; let’s not just focus on developing countries—there is a lack of what I would regard as the base information that is needed to tax effectively. This particularly applies to property taxation. Travelling through Latin America and talking to the tax policy people there, they all say, “Our cadastres are wildly out of date, and the end result is we cannot tax property.” This is not accidental. I regard property taxation as an important part of any tax mix, but there is a case for building up the cadastres, modernising them and bringing them up to spec so that you can actually implement a modern tax system.

Q142 Jeremy Lefroy: A quick follow-up question. My perception is that local businessmen and women who, let’s say, are perhaps not so keen on paying tax and do not necessarily get caught in the tax net are often quite generous—they make large donations in civil society. It goes back to what Dr Fjeldstad was saying. One of the problems in a lot of tax legislation is that there is no provision for any—so this is perhaps particularly relevant in this country at this time—tax deductions for charitable giving. In effect, the expectations on giving large donations, whether it is for a local hospital or some other local charitable purpose, are there in a society, but there is no incentive whatsoever for that to be part of their normal declaration of income and getting some kind of tax benefit for that. I wondered whether you felt that if the two could be brought together—if tax regimes in those countries were to be more friendly towards charitable giving, which is a major part of people’s lives there—it would have an effect on tax compliance, because people would say, “By giving this money, I am allowed to offset against tax, therefore it is not such a problem that I am paying tax, or I am declaring my income for tax.”

Dr Fjeldstad: In principle, I agree with you. We have those mechanisms in our society. In practice, I would be a bit cautious about introducing such a system,
because it will complicate the work of the tax administration, and it can also be abused. There were many good intentions behind the giving of exemptions to specific sectors. For instance, religious organisations are very often exempted. Donors are also exempted in many countries for projects where they import goods, etc, but we see there is a lot of abuse. These projects or procurement, equipment, etc, are not used for the purposes they are exempted for. I think here one must be a bit cautious about developing exceptions in the tax regime, which can be abused. The main challenge in a country like Zambia, for instance, is to have a tax system that is transparent, predictable, and has as few exemptions as possible for taxpayers. That would also reduce the compliance costs for taxpayers. It will also reduce the administrative costs for tax administration.

Q143 Pauline Latham: When we were in Zambia, we were told about an extra import duty that applies only to informal traders, the aim being to incentivise them to join the formal economy. Do you think that that sort of model has potential, and should it be scaled up?

Dr Fjeldstad: I think that is a tax that discourages the development of the small trader. It is called the advanced income tax. It is a tax that is perceived to be unfair by the small traders. It also confuses them, when it comes to why they have to pay this in advance, and it squeezes the market. This is a tax that I think really needs to be reconsidered. There is also turnover tax of 3% on businesses in Zambia. A 3% turnover tax is quite high if you are operating on the margin. It can be substantial, and it can be a tax that makes the company, entrepreneur or business person decide, “We have to just move our business. We will not survive otherwise.”

What is the alternative here? There is a discussion, which is not formal but internal to the Zambia Revenue Authority for the time being, but also in dialogue with small business associations, about whether the turnover tax could be turned into a single business permit or licence, which would be the single type of tax they pay, to one office. It would be the responsibility of the municipal or local government to collect.

Q144 Pauline Latham: Do they feel that might be more acceptable to them?

Dr Fjeldstad: Yes. The ZRA research department is in the process of setting up a study on that, based on a baseline that was supported by the German GIZ draft paper from last October or November.

Q145 Pauline Latham: Do you think the tax authorities would be happy with that as well?

Dr Fjeldstad: That is interesting. For the time being it is in the research department at the ZRA, and there are people there who think that this turnover tax is very discouraging for developing the small scale. It is a disincentive. However, they have not decided on what is possible and whether to abolish the turnover and give the single business permit licence to the municipalities. There will be pros and cons here, but a number of people also in the small business sector, whom I interviewed in October and November last year, see this as a much more viable option for them than the current regime.

Q146 Mr McCann: This is a question for Dr Fjeldstad and Mr Christiensen. In our last session, we asked whether revenue-based taxes might be preferable to profit-based taxes, on the basis that revenue figures are more difficult to manipulate than profit figures. What would your view be on that? In terms of revenue-based taxation, are mineral royalties preferable to windfall taxes? What is your view on that?

Dr Fjeldstad: I need a clarification, if I may. What do you mean by revenue-based tax?

Q147 Chair: Obviously royalties is one.

Dr Fjeldstad: Oh, royalties.

Chair: And, I suppose, a turnover tax is as well.

Dr Fjeldstad: Yes. In most mineral-rich countries, royalties are part of the tax regime. In Zambia it has been increased to 6% recovered, which is high—maybe too high. This is a royalty that mining companies have to pay independent of what they have earned, so it is quite high. The normal rate is 3% to 4%, and maybe up to 5%. Royalties, however, are in place in most countries. It is not an either/or between royalties and corporate income taxes. Corporate income tax or profit tax is something that should be in place when they start earning money. The windfall tax has been a big issue, particularly in Zambia; it was introduced in 2008, and abolished a year later. That does not mean that the windfall tax necessarily is a bad tax, but it might have been the case that it was poorly implemented. One problem in Zambia was that the windfall tax was not deductible from the profit tax. It was not deducted as a cost for the companies. Together with the resource tax, the windfall tax plus corporate tax and resource tax meant that the marginal effective tax rate was more than 100% for some companies, so of course it led to an outcry from them. However, if properly designed and implemented, a windfall tax can work, but it must be based on a system where we have very high prices on metals. It is not something that can start when the price of the minerals are at average levels. It must be when we have very, very high prices. Don’t ask me what that would be with respect to copper, but there is historical data that we can look at.

John Christiensen: I concur with what Dr Fjeldstad has said about windfall tax. I think it is a matter of design and timing. If the design is right and the timing is right, these are perfectly appropriate in certain circumstances. Generally I think that turnover taxes can dampen growth and be harmful. I prefer to see profit-based taxes, because I grew up thinking that “turnover is vanity and profit is sanity”, and we must encourage enterprise. Certainly when I hear figures of 3% on turnover, I find that quite a surprisingly high tax rate, which I think would dampen activity, or push activity into the informal sector, which is harmful. Generally speaking, I think a profit-based approach—
Q148 Mr McCann: Profit-based taxes, therefore, with safeguards in place to ensure that there is no manipulation of the figures.

John Christiensen: Absolutely. This is the big problem that we have is that the current regime for taxing multinational companies, I would argue, is not fit for purpose. The current guidelines certainly need to be radically changed, in my opinion, particularly around the taxation of intangibles. This is, in my view, one of the key fault lines in the globalised economy.

Q149 Chair: In the context of Zambia, my understanding is that there is a windfall tax. We have had the same issue in the UK sector in the North sea with oil and gas. The companies protest, because it is a very blunt instrument. It doesn’t take account of the variable costs. If you look at the price and say, “Oh, you are $106 for oil,” and whatever it is for copper, but you might happen to have a very difficult mine or particularly difficult oil field. If that is not taken into account, it is a very blunt instrument. It has the exact effect of saying to investors, “I will avoid a country that is likely to do that to me, if there are others where I find a more stable regime.” It is risky, isn’t it?

Dr Fjeldstad: It is risky.

Q150 Chair: For countries to use windfall tax, it creates a very uncertain atmosphere.

Dr Fjeldstad: Yes. It is risky, so it should be used very cautiously and only when prices are very, very high. That was not the case in Zambia, and they also had a resource tax. The implementation was a major problem and led to outcry.

Q151 Richard Burden: I love the idea of “Tax Experts Sans Frontières”. That might well find a place. I suppose my question is mainly to you, Mr Christiensen. Throughout all the evidence that you have given, in written form and so on, the question of automatic exchange of information took centre stage. Some of the evidence we have had, certainly in the previous evidence session, has suggested that if you have the right degree of transparency and you build up the right capacity in developing countries, you might not need automatic exchange of information in the way that you suggest. What would be your response to that?

John Christiensen: I am intrigued by that. Certainly the demands for automatic information exchange, as the global standard for information exchange, has increased significantly over the last few years. We now have very major countries like India saying that they see automatic information exchange as the appropriate global standard to aspire to. From an operational point of view, I think the automatic information exchange process has attributes that place it significantly ahead of the alternative, with the major alternative being the “on request” model for information exchange, which I describe in my submission.

From a policymaking point of view, I have always felt it is far better to deter rather than detect crime. The advantage of automatic information exchange is, as everyone agrees, that it deters tax evasion, because there is a clear knowledge that your information will automatically be exchanged between tax authorities from one country to the other. In that case only the really hard-line nutcases are likely to go ahead on the assumption that the tax authority in the country of residence will not have access to that information. In that respect I think automatic information exchange is clearly head and shoulders above the alternative model.

Q152 Richard Burden: A last question from me. Again, with the previous panel, there was quite a lot of discussion around transfer pricing. I think in all of your evidence you have suggested that there needs to be a little more probing on things like how you account for and translate issues of intangibles and so on. The impression that was given by the previous panel—admittedly, the companies there could only speak for themselves—was that they would clearly say that they do not evade tax, but they were also very clear that as far as tax avoidance and their companies were concerned, they did not aggressively tax plan. I don’t expect you to comment on individual companies, but would that be your view? Would that be the general picture you would have of the approach of large multinationals in the developing world, or would you say that aggressive tax planning is perhaps rather more of an issue than we heard from the last panel?

John Christiensen: Yes. If we interpret “aggressive tax planning” as being to put a transaction into any part of the process that is primarily driven by seeking a tax advantage, my view is that the vast majority of multinational companies are engaged in aggressive tax planning. They are using tax haven jurisdictions—substituting tax haven jurisdictions extensively, primarily for that purpose. This is the norm rather than an exception. I have experience from both sides of the fence, having been an advisor to Government on these issues, and also having worked in the private sector on precisely this. My experience is that this is the norm rather than the exception.
Q153 Richard Burden: I will break my own rules, because having said that was my last question, I have one further one around the evidence on that. I suppose this may come back to questions of transparency. It seems that these discussions get into questions of, on the one hand, allegations that perhaps may go over the top, or may be not easily substantiable, versus a view that because the allegations are not substantiable, there is not as much of a problem as is being said. How do we break that logjam?

John Christiensen: This is a systemic issue. I find that while case studies are fascinating and always help to spicce up stories, we need to recognise that the current global system is not fit for purpose. Pointing fingers at a bunch of companies and saying, “You are badmash characters,” does not necessarily help. What we need to do is to have a global debate about what is the appropriate way of taxing multinational companies, and what is the appropriate level of transparency around the taxation of multinational companies. My view is that the current system is not fit for purpose. We should be moving, as I said earlier, towards a very different regime for taxing multinational companies.

First of all, the arm’s length principle, which lies at the heart of the OECD’s guidelines, is intellectually flawed, and there is no way of overcoming those intellectual flaws from an economist’s point of view. Secondly, the issue of intangibles is becoming increasingly the area around which there is contention. There is no way through that particular thicket, and therefore moving towards a system of taxing multinational companies that looks more at the issues of economic substance—in other words, where they are making their profits, rather than what legal structures they are putting into place to shift their profits from one subsidiary to another—is the logical way forward.

Q154 Chair: This leads to a final question to all of you on the role of donors in co-ordinating these kinds of measures. We see division of labour: for example, Norway is often brought in to advise on oil and gas taxation in countries that have discovered oil, because the donor community has said, “That is the way we do it.” Taking up precisely that point, what are donors doing, and what should donors be doing to co-ordinate more effectively, establishing practices and transparency systems that will enable this to happen? On your last point, Mr Christiensen, I suppose if you are sitting in Zambia and you are dealing with a copper company, you will say, “This company is basically trading in copper. Why on Earth should I be providing tax breaks for some intellectual property stuff, which after all only exists for them to get the maximum amount of profit from the copper that lies under the soil of, for example, Zambia?

John Christiensen: Would you like me to come back on that?

Q155 Chair: This is a last comment, really, on the role of the donors and trying to raise the game on this.

John Christiensen: I would like to make a point about that. It has been very heartening to see the extent to which donor countries have looked to build tax capacity and the tax system generally as a logical step to moving beyond aid and into what in the jargon is called “domestic resource mobilisation” as a long-term sustainable thing. I have spent most of my career hoping to see this step, and it is very laudable. I think there is a danger that we all tend to move in tandem on this, and there are so many angles one could come at. I would like to see DFID, which I still see as one of the leading lights in this area, to take on some of the harder targets, including building public compliance, and to see tax as a way of strengthening democracy and state building. That is quite a soft thing to achieve—to build public awareness around these things and to build dialogue around what the appropriate tax mix is for a particular country. My argument with the IMF, for example, for the past 20 years, is that it has tended to take a one-size-fits-all approach to tax policy, which is not appropriate. Where we can add value is by helping to build the institutional capacity, not only within the state, but also more broadly within civil society—such as involving university departments, research institutes, think tanks and sponsoring PhDs—with the long term goal of trying to build a clearer awareness of how the tax might help a particular country to move towards greater self-reliance.

Q156 Chair: Dr Fjeldstad?

Dr Fjeldstad: There has been a lot of focus on extractive industries during this discussion, and that also reflects the discussion we experienced in Zambia, for instance. There is a lot of focus on extractive industries, which is natural. Civil society in Zambia also has done a tremendous job there of shedding light on that issue. It is a big political issue. The danger is that one ignores the development of the broader tax system. We know from our own countries that revenues from natural resources and the extractive industry will never be able to finance all their development initiatives—infrastructure, public services, etc. In Norway, oil revenues may be 44% of the total revenues. If the country wants to develop and to have a sustainable, reliable revenue source, one has to develop the ordinary tax system, corporate income taxes, personal taxes and so on. One of the challenges now in a country like Zambia, and also many other developing countries, is to move the debate a bit further—not forgetting the extractive industry, but taking a broader perspective to issues of taxation. That will then lay the foundation for building a broader citizen engagement around taxation. Taxation, we know, is essential for state building. Taxes create citizens.

Q157 Chair: We did have that discussion with the Ministry of Finance in Zambia. The final one to you, Mr Rich.

Eddie Rich: Thank you. Building on that, and building on the Zambia example, and Uganda, Tanzania and Mozambique, all around that east Africa region, where there are such large discoveries of oil and gas resources at the moment, we probably have
one more electoral cycle in which development assistance and aid will be the largest inflow into the economy. After that it becomes these forms of tax, which may not be broad-based at first. This will lead to a very fraught discussion, as we can already see reflected in the discussion going on in each of the countries.

One of the strengths of the EITI is helping that discussion to be had in-country. I would say it is an advantage over some of these mandatory disclosure reporting requirements and so on. It is not an either/or; we see them as complementary, but we need to have Governments, companies and civil society sitting around the table together in countries. What can DFID and other donors do to support that? We have already heard a lot about capacity building on cadastres, and building up civil society, on improving the diversity of the tax base. We have heard about research and development in the sector. I would also encourage DFID to do more of what it is doing in supporting technical assistance of the EITI processes in the countries that are implementing it.

Lastly, I would also say that there is an opportunity for DFID to lift this debate a little bit higher in the public consciousness, and to bring the international debate much more on to the UN table. Is there an opportunity for a UN panel of experts to look at tax and development, particularly the challenges raised by increasing extractive revenue resources in developing countries and others, and to have that discussion across all development partners, not just DFID?

**Chair:** Thank you all very much. It has been extremely helpful. Two things emerge. One is that, having spawned EITI, the UK had better decide what it wants to do with it. We accept entirely that while our focus is on the extractive industries, that is not the title of our inquiry—it is the whole issue of expanding the whole tax base. Of course the industries themselves say, “We don’t just pay corporation tax, but we employ people who pay high salaries and should pay PAYE and so on.” It has really been very helpful to us, and we thank you very much for your written submissions and for coming to give us evidence. Thank you.
Tuesday 15 May 2012

Members present:
Hugh Bayley
Richard Burden
Mr Sam Gyimah
Jeremy Lefroy
Mr Michael McCann

In the absence of the Chair, Richard Burden was called to the Chair.

Examination of Witnesses


Q158 Chair: Good morning.
Mr O’Brien: Good morning, Chairman.

Chair: It is nice to see you, Minister. First of all, apologies from Malcolm Bruce, the Chair of the Committee, who has to be elsewhere today. He asked us to pass on his apologies, and there is certainly no discourtesy intended. I am very pleased to be able to welcome you. This is our third and final evidence session on the taxation inquiry. We have been looking at taxation in developing countries very broadly: corporate and personal taxation, direct and indirect taxation, and investigating what DFID itself can do to try to strengthen revenue collection.

In our first session we heard from several leading academics and a number of NGOs. In our second session, we heard from organisations including Glencore, SABMiller and the Extractive Industries Transparency Initiative. We have also been involved in a case study of Zambia as part of the inquiry; the Committee visited Zambia in March and held a number of meetings over there with Government Ministers, the Revenue Authority, leading corporations and so on. Later this morning we will be hearing from the Exchequer Secretary to the Treasury and from HMRC, and we will have a number of specific points we will want to raise with them. There may also be some issues that we raise with you that we will want to raise with them as well.

Clearly hearing from DFID and you, Minister, will be a vital part of this inquiry. I think we have just over an hour with you, and we certainly look forward to hearing your views on all the main issues and maybe challenging you on one or two points, but we certainly do look forward to what you have to say. Without further ado, for the record, could you introduce your team, and then we can move on to the questions?

Mr O’Brien: Thank you very much indeed, Chairman, and thank you for passing on the apologies of the Chairman of the Committee. I am Stephen O’Brien, Parliamentary Under-Secretary of State at the Department for International Development, and I am accompanied this morning by three officials from that Department: Stephen Sharpley, Simon Whitfield and Justine De Davila. I will ask them, if I may, just to quickly introduce themselves with their job titles and the particular areas in which they specialise.

Stephen Sharpley: I am Stephen Sharpley. I am a senior governance adviser in the policy division in DFID, and I work on public financial management.

Simon Whitfield: I am Simon Whitfield. I am a policy adviser in the policy division in DFID, and I cover largely the international aspects of tax work in DFID.

Justine de Davila: I am Justine de Davila, and I am a governance adviser working on extractive industries in the growth team in the policy division in DFID.

Q159 Chair: Thank you very much indeed. Taxation has been the centre of this inquiry and has been occupying us. How important would you say taxation is as a driver of development?

Mr O’Brien: We are very persuaded, and indeed I think all the evidence shows—I dare say this is completely in accordance with where the Committee’s thinking is—that tax is of course very important. This is patently because it means that countries can generate their own revenues and therefore provide the services to their own citizens, and what is taken into an Exchequer through transparent, democratic, accountable governmental systems then means that there is a compact with their peoples. It is tax that gives them the means to deliver those.

We are very clear that it therefore helps to enhance that relationship between the citizens and a Government. It makes citizens, and certainly states, more effective. So far as DFID is concerned, we are very clear that the challenges on taxation are very much along the lines that I detect have been identified by the Committee. I have been able to read a little bit about the fact-finding mission you went on to Zambia in terms of the issues of informality, tax base erosion, how you work with partner countries, particularly where we have bilateral programmes, and indeed how we within Her Majesty’s Government work across Government, and not least with Her Majesty’s Treasury and HMRC, and a lot of the emerging drivers for challenge and change, in terms of information exchange on tax, looking at how technical assistance generates added benefit to partner countries, and where we can place our effort in terms of quality research and evidence, not least to incentivise other country Governments that this is an area worth putting a lot of effort into and, indeed, wanting to seek to attract those partnership approaches where we believe there is a track record—no doubt we will come on to that—of adding value in certain countries where we have had that partnership.

Q160 Chair: Thank you very much. I guess to some extent it is “How long is a piece of string?”, but would
you say there is any ballpark figure in terms of percentage of GDP that developing countries should be aiming for in terms of collecting that amount in tax receipts?

Mr O'Brien: I do not have that in my mind, and I have not been advised that that is a driver for us. There would be a grave danger in approaching this on a one-size-fits-all-countries basis. As we well know from well-developed Northern Hemisphere countries, the tax bases and so forth are extremely different. It does depend—and no doubt we will come on to this—whether or not you are so-called “resource-rich”. It has a different profile. One of the areas that I would say highlights the difference is if you look at the common problems. They are the narrow tax base, with a large informal sector, no property taxes very often—and lots of issues over property ownership, let alone the taxes—over-reliance on natural resources in those areas where they have them, under-taxed elites—and we know about the issues in Pakistan, for instance, on that in particular. There is low compliance and widespread failure to pay taxes, which is certainly not unique to developing countries, as we well know. The lack of capacity in the tax authority and corruption. A lot of this requires political will, and then we can come on to what will be the good laws and good regulations, how you achieve leadership, the staff quality, the IT systems. The broad number that has been bandied about is about 19%—I suspect the Committee has had that—which is for the implementation of the MDGs. That is an UNDP-derived figure, but within DFID, if you are asking whether we have a specific target on tax, I think that would be too blunt an approach. We are trying to be, as best we can, optimal per country, depending on what part of the process and journey that country is on.

Chair: Thank you. You mentioned technical assistance as being one of the key areas here. That is something we have been looking into, and I think Michael McCann will ask you one or two things in relation to that.

Mr McCann: Good morning everyone. Nice to see you all.

Mr O'Brien: Good morning.

Q161 Mr McCann: Minister, DFID has been rightly praised for the quality of its technical assistance in the tax field, yet it appears that this work is being scaled down by the Department. Can you explain why that is?

Mr O'Brien: I am not sure I recognise that it has been scaled down. I know that if you go back 10 or even 15 years, there has been a variation in how much overseas assistance has focused on tax. There was an initial rate of activity, particularly when, if you like, one of the more obvious things to do was to help set up revenue authorities—although there have been some more recent examples of that—and then there has been a slight diminution. On the latest figures I have seen, our effort is about £25 million per annum dedicated to particular tax projects. Certainly between 2006/07 and 2010/11, we have spent as a Department about £97 million on helping to improve revenue collection, so that is about £20 million per annum. There are three good examples of that; Rwanda, Sierra Leone and Burundi are the areas where significant effort has been made on that. On the technical assistance, there is a large series of programmes, particularly where HMRC is engaged, and we are working with them and doing our very best to ensure that that is well co-ordinated. We, the Treasury and HMRC are working closely on the international tax change, and particularly on capacity building. It is often quite difficult to disaggregate from a broader set of programmes, but I think you will be aware of the country-level work, and examples such as Ethiopia, where we are working with them through the recently established Investment Climate Facility to utilise UK specialist expertise, much more easily termed iFUSE, to mobilise Whitehall expertise to support the work on the investment climate reform.

Q162 Mr McCann: The reason I asked the question is that the International Centre for Tax and Development, which provided both written and oral evidence to the Committee, said in its written evidence that DFID’s work in this field “has declined appreciably since the 1990s,” and it also highlighted the lack of co-ordination between donors in the taxation field. Is that something that you would dispute? I am assuming you would, given your previous answer.

Mr O’Brien: I do somewhat. I do not recognise it. I am very happy to ask Stephen Sharples to elucidate a little further, but I think that the very same organisation has also most recently said that the effort and indeed expenditure has picked up recently. I think there has been a change.

Q163 Mr McCann: Can I buttress another question on to the back of that one then, before Stephen comes in? Would it be the case that, given the renewed focus on private sector development, there would be another look at this issue to determine whether or not additional assistance has to be supplied to support tax revenues in developing countries, with the private sector angle being taken into consideration as well?

Mr O’Brien: I personally think that is a very fair point. If we take for example Sierra Leone, where the iFUSE fund has been twice in recent times, quite clearly they are at a point where they have a number of private sector explorers, followed by potential exploiters, of natural resources. The big challenge there is to ensure that both the laws and the regulations, as well as the potential fiscal arrangements, within Sierra Leone are ready and in place so that, as these private sector operators are taking their risk, and deciding what is possible and to address the markets that they think can be addressed with that natural resource—which, after all, is a one-off asset for that country—they can get that balance of a fair yield to be received by the Exchequer. They have had a series of reviews of those arrangements, and the tax within that, and the fiscal yield within that, has been part of the thinking through, both of what is an appropriate level of royalty, how it is measured, and where it sits within the framework and architecture of laws and regulations, and which will also give what the private sector needs, as you well
understand, which is clarity, stability, and as much certainty as possible of the arrangements into which they will be placing their commercial risk, let alone geological. That is a good example where, if you like, tax technical assistance is supplied as part of our effort to work as a partner with the Sierra Leone Government, to help them put a renewed, reinvigorated, better architecture in place for those activities, to then be in a much better place in terms of fairness for the yield that should be secured off those, which would then be received into what we hope would be a very accountable, political and democratic set of decisions.

Q164 Mr McCann: Stephen, do you want to answer that point?

Stephen Sharples: Maybe I could explain. It is very difficult to monitor the level of spending on tax, because it is quite difficult to define what exactly tax is. In the exercise we carried out for the submission to the Committee, we went into quite some depth to get that information. Earlier on, in 2004/05 to 2008/09, another five-year period, we did an internal exercise reviewing governance programmes. We looked at tax then, and we came up with the figure of £71 million over that five-year period. That would imply it went up a bit from 2004/05 to 2008/09. Earlier on another exercise was carried out to look at the level of spending in this area, and that came up with £159 million, though I am not sure whether it was over a five or a six-year period. That would imply it has come down a bit since then. According to those figures, it was higher in 2001 to 2006; it then went down a bit and now it has come up a bit. However, it is very difficult to make comparisons, because exactly how rigorous we were at that time in identifying these projects, and how we apportioned what related to tax and what did not, I do not know, but those are the figures I have from previous exercises.

Q165 Mr McCann: I am grateful for that, thank you. In terms of the other written evidence that has been supplied by the Department, it also highlighted the technical assistance offered by HMRC. Let us see how generous HMRC is: did it provide this expertise for free, or did it bill DFID for it?

Mr O'Brien: I think there is—may I dare to use the term?—an internal transfer price. Maybe Simon has a better technical answer for you.

Simon Whitfield: The answer is that it depends. In some circumstances, for example in Ethiopia, where HMRC is a major provider of technical assistance, DFID funds, and ultimately it funds HMRC. In terms of one-off, small technical assistance projects—HMRC will correct me later if I am saying the wrong thing—it would fund that out of its own funds.

Q166 Mr McCann: Is that then listed as Official Development Assistance?

Mr O'Brien: I would imagine it is, isn’t it?

Simon Whitfield: I am not sure.

Mr O'Brien: We can find that out.

Q167 Mr McCann: You can find that out and come back to us?

Mr O'Brien: As long as it is in support of a development objective and is supporting countries that are of course the ones in which we operate, which are poor, then by definition one would expect it to count.

Q168 Mr McCann: If I take that answer in the round, would it be the case that the Department uses the expertise needed for the particular circumstances it faces, and thereafter will find out whether that is officially listed as ODA?

Mr O'Brien: I am absolutely sure that the way we approach the design of programmes—and I think this has always been the case within DFID—is to seek to establish where we can best meet the need in a partnership arrangement with our bilateral partners in particular, but also to work sometimes through the IMF or the World Bank, through the multilateral organisations, so that we might be able to support those programmes. The main thing is to tailor the programmes to the country need. By definition it will therefore be exceptional if there is a question mark over whether or not that qualifies for ODA, but I think you are right to raise the question and we would have to give you a specific, well-researched answer, rather than a generality.

Q169 Mr McCann: If we get some written information back, if there are any issues then we can come back and seek some clarification.

Mr O'Brien: I am happy with that. I suspect it would need to be quite specific, what you are driving at, because the answer is probably very specific in terms of particular programmes and assistance offered by HMRC. In principle, I would have thought as long as it is supporting the purposes of development that will be of service to alleviating poverty and in a country generally defined as poor, we would start from the presumption that it is likely to qualify.

Q170 Mr McCann: The final question from me then is that the CBI has told us that it has made a number of offers to co-operate with HMRC in the field of transfer pricing, and in particular to explain the multinational perspective on that particular matter. Is that something you would encourage HMRC to do?

Mr O'Brien: Clearly you will have the Treasury Minister in front of you shortly, and that is primarily a question for that Minister, on the basis that HMRC is accountable to the Treasury. I do not know if you want to address this at a later part of the meeting, Chairman, but on things like transfer pricing, which in itself encompasses a whole load of very different variables and quite a challenge when it comes to definitions and the disclosure of information, particularly as it relates to an understanding within the business world and international businesses, yes, all the expertise and the experience that can be brought to bear to assist is something that we would welcome. I do not know if you want to add something, Simon.

Q171 Chair: On the transfer pricing, we will probably come back to that later.

Mr O'Brien: I thought you might be coming back to transfer pricing later.
Chair: It might be better to do that, perhaps, in the round-up.

Mr O’Brien: But on the specific point, therefore, did you have anything you wanted to add?

Simon Whitfield: Yes. On the specific point, I cannot remember which companies, but I know there has been an offer, which has been accepted in some cases, of companies explaining their business models to developing country tax authorities, because that is essential to understanding how transfer pricing transactions will work. It is not giving specific advice about transfer pricing; it is saying, “This is how we do business, and if you understand this you will understand better how we do things.” I think that has already happened, and that offer is certainly on the table. It was discussed at the Task Force on Tax and Development last week, and I think developing countries are genuinely interested in that.

Mr McCann: Thank you very much.

Q172 Jeremy Lefroy: Taxation is becoming an area of development that is quite fashionable, and understandably it is something that people want to concentrate efforts on, since it is a key to long-term development. Do you think there is a risk of lack of co-ordination among various donors in individual countries?

Mr O’Brien: I am aware that some would say that there is a lack of co-ordination. Let us start from the presumption that donor co-ordination is really important. In each country in which DFID is a partner, we make a huge effort to work and liaise very closely with others. You may or may not have had evidence already that we support the African Tax Administrator Forum, ATAF, which helps with co-ordination, and we are also involved in the Global Forum platform for co-ordinating technical assistance. I know HMRC is working with the World Customs Organisation. Some country-level support involves engagement with civil society. If you want, I can give you some examples, but in particular the DFID-funded International Centre for Tax and Development does involve civil society partners. Donor co-ordination is absolutely vital; I recognise that in some countries it has been called into question, and no doubt there can always be a better co-ordination.

However, as part of our own effort we are trying very hard not to duplicate other donors’ work, which is one of the great challenges. In some places we are best placed to lead on support, for instance, to the revenue authority. In Afghanistan and Sierra Leone, that would be us, but in others it will be the other donors who lead, such as the Norwegians in Zambia, which I think is the country you know best from this perspective. As ever, we want to do what we think will carry the most impact, be most effective, and certainly carry the most value for money. When you look at some of the efforts that have been applied by us in our working in Rwanda and Burundi on the development of their revenue authorities, the value-for-money figures are extraordinarily encouraging.

Q173 Jeremy Lefroy: Could you give us some examples of that?
There are a number of CSOs and NGOs who have stated what they believe to be appropriate, but I think it is a fair and remaining question: where and how do you tax?

You will know better, maybe, than I do, but when I last visited Zambia I was quite encouraged by the fact that, following a review of the mining contracts, they have now moved to a 6% royalty fee, but have chosen therefore not to repeat the windfall approach. If you like, that was the internal trade-off. It was entirely their decision, and entirely therefore something that we would support. It is not a matter for us to seek to interfere in that political decision. However, 6% is at the higher end of the best practice international norm. The question then is information, transparency, and on what the 6% is measured. Is that fair, is that right, is that provable? Similar conversations have been had in Sierra Leone.

You can see how the research leads directly into where you can help suggest an appropriate approach, but also where there are genuine challenges, where there may be some perceptions that it would be jolly easy to tax activity, because you can measure turnover. We know from a lot of practice, however—certainly from my own experience in industrial business—that the difficulty about taxing activity is that very often you can deter the incentives for investment in that activity in the first place, because a tax starts before you have generated any return for the shareholders, whose money it is, not yours, and you have placed it on risk. Therefore the advantage of profit is that it is measured by time, and it is effectively a measure of cost versus a surplus, and then you can tax surplus.

You can see how the research side is very important to understand those issues between what is fair yield, what is measurable, what can be accountable and, above all, what is likely to help encourage, rather than deter, investors to go chasing those commercial opportunities. That, as we all know, is often quite a fine balance and a fine judgment, and your experience in Zambia, from what I understand, was an interesting case study—to go for 6% but not go for more windfall. Would each member of the Committee have made the same decision as the Zambian Government made at the time? They are quite finely judged issues, because you are trying to predict an uncertain future. I have just had a note passed to me, which also reminds me that the International Growth Centre, which has been going a little bit longer and, as you know, is located at the London School of Economics and is funded by us, is providing demand-led policy and advice, particularly on taxation issues. Again, you met that in Zambia. The IGC’s analysis has demonstrated the disincentives to formalisation, for instance, of the larger informal sector firms, which you can see from things like the lack of infrastructure and banking services. That does ultimately deny Governments tax revenues, but the question is at what point you have formalised the informal sector, which I know has been another area of your concern as a Committee. How much does that then disincentivise?

**Chair:** Thank you. I think Hugh was going to pursue some of the issues of revenue-based taxation, but also other areas as well.

**Q175 Hugh Bayley:** I think, Minister, you have largely set out your stall on that. One of the questions I was going to ask was whether you would favour royalties over windfall taxes, and I think you have told us, “That is for the Government in the country concerned to address.” Could I ask you a slightly broader question: what do you think are the relative benefits of profit-based taxation versus revenue-based taxation, and would you apply a different norm to different sectors of the economy?

**Mr O’Brien:** We could get into a very long tax and philosophical argument here—or a discussion, probably not an argument even. I think the last phrase of your question, in a sense, answers the essence of it, if I may put it that way. It is incredibly difficult to find generic, general answers for this. Each country will have a different set of assets and opportunities, a different stage of its economy, a different access to risk finance, and a different governance context into which businesses, both internal and regional as well as foreign direct investment, can have confidence and place their bets, if you like. I think the merit of profit-based taxation is, as I was seeking to hint at a moment ago, that by that being a measure over a period of time that can take into account your genuine costs versus those revenues that have exceeded your costs, it becomes something capable of being given an equitable application between return to shareholders, return to the nation in which you are operating, and return, if you like, where there is an international dimension—to the country in which you are registered and from which you started your risk journey as a commercial operator, and from which you may well draw quite a lot of your employees and technical experts, who are part of the added value of being able to extract the product in the first place. My own personal experience was not so much in extractive industries; it was in construction materials, which therefore dealt with natural materials, but once they had been extracted. Therefore the biggest challenge I remember was that my products were too heavy to go very far. We were not an export business but, by goodness, we did export technology, knowhow, and we were in partnerships and joint ventures. Therefore you have a different set-up, because a lot of that will be under royalty arrangements. There will be different approaches, depending on the particular profile of the country and the particular businesses.

**Q176 Hugh Bayley:** Given your background, can I ask a particular question about bulk products? It struck me from my exposure to these arguments in Zambia that copper exports go out by road, in trucks. So long as you do not have corrupt customs officials, you can work out a price per tonne and charge a tariff on export, and it is pretty difficult to evade—more difficult, I would suggest, certainly than profit-based tax. If you look at the diamond trade, for instance, that would be wholly inappropriate, because you need to attack the problem on the company’s balance sheet, not the customs part. Do you think, with bulk products across borders, like refined copper, just imposing a tax or tariff of so much per tonne is a sensible, simple but safe way for a developing country to raise revenue?
Mr O’Brien: I am certainly not averse to keeping it simple, but I think there is a danger in doing something that is not co-ordinated with the way in which any particular commodity—and I think when you talk bulk, commodities are at the base of this—

Hugh Bayley: Yes.

Mr O’Brien: You have to look at the context of its world market. If one is applying a price per tonne, for instance, on copper per truckload going out of Zambia, but that is not the way that the commoditised copper is going out of other countries to reach the primary purchasers of that for onward refining, such as the Chinese and Asian markets, it could put Zambia at a serious cost disadvantage at the point of freight-on-board price at the port. That is a question, therefore, for the world context.

In principle I think it is part of the first answer. It is tailoring whatever is appropriate. If one was to be out of step with the way world commodity pricing takes place, all of which we know carries its own frightening risks in terms of volatility, very often—as we know from agricultural produce—the cash crop effect of when prices suddenly go down leaves no leverage on the part of the producer to be able to put a floor on that. Those are more economic movements than tax movements, and we need to be very careful not to allow pricing and volumes to be driven by the fiscal arrangements in order to capture the tax. Rather, it has to relate to what is likely to be most competitive in a marketplace, and the tax should then yield off the top of that.

Q177 Hugh Bayley: Thank you. One other question at this point relates to capital flight, and the comments on the very final page of your evidence. Frequently when I talk to Aficans, they complain that London is at the bottom of the list. They talk about the Abacha millions being banked in London, and so on. I know there has been some progress: you say that a total of £170 million of assets have been “restrained, recovered or returned” in your evidence. Could you give us a sense of what DFID can do to help bring those figures up?

Mr O’Brien: Indeed.

Q178 Hugh Bayley:—the former Delta State Governor in Nigeria. It would be interesting to know what period of time this figure covers, what proportion has been a) restrained, b) recovered and c) returned, and which are the principal cases, whether there is a trend of increasing accountability for people who are money laundering or banking with the proceeds of corruption in the West, and whether you have a general further policy statement to make. I am interested to know how big an issue your Department thinks this is, and also how you co-operate with the Treasury, which is a reporting point, I guess, for many of these transgressions.

Mr O’Brien: The short answer to your very important question is that, as far as both Her Majesty’s Government and particularly our Department are concerned, we do not want in any sense for London, let alone anywhere else, to be a hiding place for money laundering, for ill-gotten gains, or for those things that have effectively been a fraud or theft from the public purse. It is absolutely vital, therefore, that we look at cases like the James Ibori case, and recognise that is not only a case that clearly requires all of the enormous amount of work and preparation that goes into securing such a result but, in the best possible legal jurisprudential world, ispour decourager les autres—in other words, to deter others. Of course the primary issue is to tackle the phenomenon of diversion of monies at source, because of course the more successful we are in London and elsewhere in making sure that this is not in any sense a route or a haven for such monies, we do not want them simply to be diverted elsewhere. The question is for them not to be diverted full stop. Therefore it is also working at source. I did say, I think, in my very original response to the general question put by the Chairman, that you really cannot understimate the importance of political will from the very top of each country in this. That is why it is so important as a Department of State, as DFID, that when we have those discussions we are there as a Department of State, on behalf of Her Majesty’s Government, having that kind of discussion to establish the political will that helps us to tackle it at source.

I have just been given quite a long list of all the cross-Whitehall working going on here, which is Her Majesty’s Treasury, us, SOCA, Home Office, Met Police, CPS, City Police, all working—

Q179 Hugh Bayley: Could possibly your official, rather than detain us now, give us—?

Mr O’Brien: That looks to me as though you will get a decent response. I do certainly say that we will respond to you in the detail you ask for. Hugh Bayley: Thank you.

Q180 Mr Gyimah: Minister, changing tack slightly to the informal sector, one of the features of a lot of the countries in which DFID operates is that the informal sector is very large and growing. Could you give us a sense of what DFID can do to help bring informal traders into the tax base?

Mr O’Brien: It is certainly an absolutely key question, and you are absolutely right in saying that it is a major challenge for many poor countries. Extending taxation to the informal economy is clearly important. We touched earlier on the fact that there can be a downside to it, but I think the principle is clear, as with any developed economy: make sure that the information is available, that economic activity is therefore accountable, and that therefore the points at which taxation can be chosen within a country’s decision-making can be selected.

We are funding work that should help by increasing the understanding of these issues involved. I have mentioned both the early-stage stuff that we are doing with the International Centre for Tax and Development, but also the International Growth Centre. We have a major new research programme—again, I am sure my officials can give you the details of this if required—with the Centre for Economic
Policy Research, and we are funding what is now the World Bank’s Investment Climate Advisory Service, which used to be known as the Foreign Investment Advisory Service.

The other thing to bear in mind is that informal businesses are not always small, let alone poor, and when we formalise it, it is not just the technical problem that is a challenge but it is also a question of part of the broad good governance within a country. I gave you the example of how the Burundian Office des Recettes has moved, but that started from a position of being the most corrupt in that part of the subcontinent. Certainly when I was there a few weeks ago I saw a really impressive change, a really impressive performance, with great leadership and the huge experience that has been brought to it by some international advisors who have been doing the same thing in Rwanda, so really able to transfer best practice. How do you really get at making sure these things no longer have incentives to be corrupt but actually the incentive to pay? It is part of the political will, again, that sets a context. In Rwanda, they now have a celebration of taxpaying in the country, which I think, if I may say so, is something we could learn from. It is quite a dramatic shift around of the sense of equity that comes as a result of that, within the country.

Q181 Mr Gyimah: What steps do you think developing country Governments can take to tackle this problem themselves, though?

Mr O’Brien: Probably the easiest thing is to refer to an example of a country that is a bit further along the track on this score: Sri Lanka. It is not a country with which I am particularly familiar myself, and it is one where we do not have a bilateral programme today. There we can certainly see that, although there was a big effort within the country as well as with international donors and partners, in this space doing the same thing in Rwanda, so really able to transfer benefits from formalising. They needed a significant cash incentive to register. So despite the benefits of formalising, there was a deep reluctance. A lot of this is to do with the culture of business. I do not know whether any of the officials have any better experience they can point to, but I know for instance in Liberia, where we have had a small bilateral programme, there was particularly focused in this area, that the disincentive for the informal activity to become formal is that those who are operating in the informal business space like access to the traditional courts, rather than going down the formal court process. Effectively, they want to hold on to their community alternative dispute resolution procedures, if I can put it into our jargon, rather than what is then part of the formal process of resolution of tax disputes. It is possibly a little unexpected.

Stephen Sharpley: I think the key to it all is understanding why businesses will not move into the formal sector, then trying to address whatever those things are. Those issues may not be what we immediately might think. That is why research is important. It will vary from country to country, but trying to understand what the issues are—it may be that speed is very important to them, that kind of thing—will be key to it. In a much more general way, the more that businesses feel their tax money will be well used, the more likely they are to be inclined to pay, and therefore improving public financial management more generally has something to contribute as well.

Q182 Mr Gyimah: One thing you have not touched on, obviously, is local property taxation, although you did refer to it in your introductory remarks. Do you think there should be a greater focus on local property taxation, and do you think this could improve the level of formality, for example, through the preparation of land registries?

Mr O’Brien: This is a very interesting question, because it touches on a broader issue about the tailored approach per country that we were discussing a moment ago. I look across all the countries in sub-Saharan Africa in which I have been travelling, and understanding the programmes in detail, and trying to see where we can have most impact. The question of land and land title, who has the leasehold rights, who has the occupation rights, who has the ability to be licensed—whether it is because, in Sierra Leone, as part of the paramount chief deciding that you can have the use of that bit of land for so long—the question of taxation of property at that point does not arise in terms of the person using the land. It is part of the power structure in many parts of Sierra Leone that that land is for the paramount chief effectively to dispense according to the way they are brokering their community politics. It does not even touch the sides of the way the national economy is structured. In a sense, it would be too early to even think in terms of property tax. Tanzania, as we know, has had a particular view about not having the ability to have title to land. It is effectively a broad leasehold arrangement, so where does taxation apply? Is it on the use of land, effectively rent, or is it on the ownership? Does it happen on transfer, where a lot of transfers do not happen because there is a lack of clarity in the process of land registration?

One of the most interesting things, I think, the Committee has seen has been in Rwanda, where there is a land tenure regularisation project, supported by DFID, which has been through aerial mapping. It is a really powerful physical programme in terms of productivity on the land as a result of knowing, “That is the bit of land I own, and therefore I will make sure it produces even more. Therefore I demand access to a market, and I demand participation in the economy so I can do more than subsistence farming and end up running a small business.” Therefore that is the question relevant to what you are driving for: how do you capture that form of activity? Does it go informal and you cannot get at it, or is it at that point that you encourage even basic skills such as bookkeeping, so that you can have an account that can then look at the informal business that has emerged from that process. Land-based entitlement rights do apply in the extractive industries, in terms of the land upon which extractive industries are based. That is for the larger businesses, rather than the informal sector, which I felt you were driving at. I do not know whether you want to say anything about the larger, particularly foreign-owned, businesses and land rights?
Q183 Chair: We will come on to the extractive industries a little later.
Mr O’Brien: Shall we leave that until then?
Q184 Mr Gyimah: Specifically on property taxation and bringing that into the formal sector, what is DFID doing in this area?
Mr O’Brien: I will ask Simon to answer that one.
Simon Whitfield: Thank you. Certainly it is an area of interest, particularly in the agricultural sector as well. I think FIAS, which was mentioned earlier, has been doing some work on this. The particular point about land registries and so forth is a wide issue. One of the UK Government Departments that has signed up to iUSE, the technical assistance facility that DFID is funding, is the Land Registry, so that is a very direct way that expert support can be provided to developing countries that are tackling these issues.
Q185 Hugh Bayley: I do not want to deter you from the work you are doing on land registries; I think it is very important. However, I think you let the paramount chiefs off a bit too lightly. We were able to do a Domesday Book, which did not tax the peasantry but did tax the barons, who presumably had ways of collecting tithes from the people to whom they allocated tracts of land. Can’t we learn from our own history and find ways of operating systems without the huge Western bureaucracy of a legal land registry for every square metre of land?
Mr O’Brien: I hope I did not give you the wrong impression, Mr Bayley, because I was seeking to answer the difficulty of property taxation in relation to the informal sector, and of course the informal sector is largely not the landowners or the paramount chiefs but those who are active on the land.
I think you make a very important point. The question for us is not whether we can do it, but what the local government chooses to do, and what we can do in supplying technical assistance, if it is part of a relationship we have with them, to support them, if they make a decision that is where they wish to apply their effort to try to widen their tax base. I would personally strongly encourage the focus on property taxation, because, by and large, one of the very few things that is very difficult to shift is the land your country is based on and defined by. Once it is parcelled up into ownerships, by and large—I rather agree with you, and no doubt the Treasury Minister will have more to say about this—taxation works best when it is fixed on something you cannot hide.
Q186 Hugh Bayley: I will just make a passing comment, in part from our clerks. One of the things that bedevils African politics, in my view, is the lack of accountability of governors to those governed. One of the reasons for that is that so little taxation is raised from the people. As soon as you start taxing the people, people demand controls over the Government—Magna Carta and Runnymede and all of that. Is that not one of the benefits that comes from the introduction of systems of local taxation?
Mr O’Brien: Yes, and I think possibly, without wanting to widen the debate too far away from the central thrust of the inquiry, the experience in Nigeria most recently on the fuel subsidy shows the popular issues coupled to, effectively, what was there a reverse taxation. I think it is a very interesting case in point as to how you can couple a wider popular series of issues of equity with the demand for services through their taxed assets and income, and at the same time make sure that the country is able to maintain both its competitiveness and peace and security.
Q187 Hugh Bayley: A point well made. I must move to my allocated questions, or the Chairman will get grumpy. On the question of exchanges of information between tax authorities, the default position is that information is exchanged when one tax authority in one country asks for it from the tax authorities of another country. Would it not be better to have an international system where tax information is exchanged automatically, because it would do more to deter tax evasion?
Mr O’Brien: I hope you are aware that DFID supports automatic exchange of information in principle. Clearly, as you have just outlined, it has an important role to play, where reporting and the administrative burdens are not prohibitive. The G20 finance ministers, in February this year, called for an interim report and update by the OECD on necessary steps to improve comprehensive information exchange, including automatic exchange of information. Now we already have automatic exchange within the EU for tax information on bank interest under the Savings Directive. The Multilateral Convention for Mutual Assistance provides a treaty basis for automatic exchange if signatory countries agree bilaterally. I think by the nature of my answer I have defined where the challenge lies. It is getting it to a sufficiency of agreement amongst the nations.
Q188 Hugh Bayley: First of all, does the Treasury fully, actively and enthusiastically share the policy you have outlined? Secondly, what would you think is a realistic timetable for achieving a universal automatic exchange? If it is good enough for the EU, surely it should be good enough for our relations with other countries?
Mr O’Brien: I have every reason to believe that I and my Treasury colleagues are absolutely batting from the same position. As for a timetable and the state of play, I think that the Minister who succeeds me on this stand will be best placed to answer that, in all fairness.
Q189 Hugh Bayley: Many organisations that advocate automatic information exchange also press for tighter transfer pricing legislation. When you think that 60% of world trade is trade between different branches of multinational companies, one can see the reason for that. One of the suggestions would be some kind of formulary apportionment whereby companies’ taxable profits would be allocated in proportion to, say, the total payroll, total value of property owned or total sales in each country, to prevent the extreme transfer mispricing that we sometimes hear about.
Mr O’Brien: If I can take the general point first, before I come on to the secondary point, we are certainly helping developing countries where we have partnerships with transfer pricing, both bilaterally and
Indeed multilaterally, through international organisations. The HMRC, very much part of working with DFID through the Treasury, has supported, as I mentioned earlier, the African Tax Administrator Forum on transfer pricing, which is a very important initiative and a demonstration of political will, which again is vital. HMRC has provided assistance directly to a number of countries on this: Uganda, Nigeria and South Africa are examples. The OECD, through the Task Force on Tax and Development, which again we are funding, is providing assistance on transfer pricing to Ghana, Kenya, Rwanda and Vietnam. In Ghana and Kenya, this is dovetailed with assistance on exchange of information. We are supporting the development of large taxpayer units in some countries, one of which is Bangladesh, on transfer pricing.

It is clearly an important issue for developing country tax authorities, but it has to be in the context of their overall tax, and indeed public financial management reforms, programmes. For some, it is not the No. 1 priority. It cannot be, because other things, in a sequenced way, have to come first. For others, it has reached that point. Again, it is part of this tailored approach, an extract of being extremely disciplined that we do not apply a general rule. Part of the problem, to some degree, with the campaign for the formulary is that it is in danger of trying to apply a generic, general approach to something that necessarily has to be tailored according to each. At the moment I am personally not persuaded by the formulary approach, on the basis that I think it does not yet demonstrate that it would generate either significantly more, or indeed any more, tax revenues, but in particular it could add enormous administrative burdens, which one would certainly have to take into account. I think you would be the very first to understand the definitional challenges that a lot of these would pose, because the danger of formulary arguments is that not only does it potentially carry a high degree of arbitrariness, but also, if you do not get the definitions right, applied to each and every circumstance, it ends up as a continuing argument that is in danger of not being resolved. Any financial argument tends to mean postponement of cash receipts, which is not ultimately in the interests of the Exchequer. I think those are the challenges that lie behind it. I do not for a moment deny that there is a pretty active series of campaigns on this, and I know that lies behind the question, because you have obviously received representations from some who are developing a lot of thinking on this.

Chair: Thank you very much. If we can now move back to extractive industries again, I think Sam was going to ask about the EITI.

Q190 Mr Gyimah: Thank you, Mr Chair. Why has the UK Government not signed up to the EITI?

Mr O’Brien: Let us be absolutely clear: we are very strong supporters of the EITI. It is something the UK has not implemented, quite simply because the EITI is designed for, and has been focused on, resource-rich countries. We are not, by those definitions, resource-rich. We are conscious of the movement globally, not least from the US, which is the context for this, and I think that the EITI is a very important initiative. It is something that is now being looked at with a great deal of positivity in many countries. So as far as the UK is concerned, the current big effort that the Chancellor of the Exchequer has been leading on is to try to get to a point where EU Member States move equally—because I think this is not something that would be in the UK’s interests to move on unilaterally—whether it is along the Dodd-Frank type approach that the US has led on, or on a different basis. At the moment, we are not in a position where there is agreement among Member States, and we are doing our very best to support the Treasury in making those arguments to get to a common position.

Q191 Mr Gyimah: Can I press you on that for a second? The UK Government founded the EITI. In your own words, we are strong supporters of it. We are encouraging developing Governments to sign up to it and participate. Don’t you think we should be leading by example?

Mr O’Brien: I think if we were resource-rich, that would be a pretty cogent challenge. It is important to recognise the distinction between resource-rich countries, particularly the dependence of not just the current but, as was pointed out very much earlier in the discussion, the potential proportion of GDP of countries in, not least, sub-Saharan Africa if there are appropriate protections, safeguards, transparencies and accountabilities that will enable those countries to get the yield.

It is very interesting to take an example like Ghana, with the recent landing of oil. The right question—often not the one that is asked, but the right question—is how to get to a common position.

Q192 Mr Gyimah: And how do you get to a common position?

Mr O’Brien: Well, the US has led on, or on a different approach that the US has led on, or on a different basis. As far as the UK is concerned, the current big effort that the Chancellor of the Exchequer has been leading on is to try to get to a point where EU Member States move equally—because I think this is not something that would be in the UK’s interests to move on unilaterally—whether it is along the Dodd-Frank type approach that the US has led on, or on a different basis.

Chair: Thank you.
Q192 Mr Gyimah: One final question from me: do you think the EITI has weaknesses, and if so, how can those areas be strengthened? I do not know whether Justine or the Minister would like to take that.

Mr O’Brien: That is an interesting question. I think it is the best that has gained traction at the moment, but I am absolutely sure that it will have scope for improvement. Justine, do you want to add where the perceived weaknesses are coming through?

Justine de Davila: There was an independent evaluation of the EITI last year, which you may be aware of, which found that it had built a very important international brand, that the multi-stakeholder platform of EITI was very important, and that it had improved transparency. Some results of EITI, for example, are that it has built trust and dialogue between different stakeholders who may not perhaps have come together to discuss extractives in the past. It has improved financial reporting. It has empowered civil society to hold Governments to account, and it has improved the operating environment for private investors.

Having said all that, I think there is a recognition within the EITI itself that it has to build on the existing platform and respond to the findings of the evaluation. For that reason, the Chair and the Board have set up a Strategy Working Group, which is looking at the future of the EITI and how it can build on the strengths of the existing standard going forward.

Q193 Chair: Time and perhaps the join between the remit of our Committee and the remit of other Committees may raise some interesting questions about the relationship between energy policy in the UK and the EITI, but I do not think I will go there right now.

Mr O’Brien: I am much relieved you do not want to go there.

Chair: Can we move on? We would like to ask some questions, if we may, about CDC and some issues relating to that.

Mr O’Brien: Yes.

Q194 Jeremy Lefroy: With CDC to start with, in our report last year we recommended that, when investing in tax havens, CDC should follow best practice guidelines. I would like to know how far along the road to that we are.

Mr O’Brien: I think that you will have seen that the revamping of CDC has now taken hold and is well rooted. We have a dynamic new Chief Executive, who is very clear about the new arrangements, which help the judgments that it will have to make as to where it invests. I am certainly persuaded that it is well tuned to the best practice of ensuring that, where it is an originating or sole investor, and that is therefore within CDC’s discretion, it should not use offshore financial centres. Of course, to some degree discretion has to be applied where it is not the originator or sole investor. That I think is one of the main issues that have arisen in the past in relation to this quite tricky area. It is clear that CDC in its new form will not make new investments in or through harmful tax regimes, or regimes that do not comply with the international tax transparency and exchange of information standards.

Q195 Jeremy Lefroy: Given that CDC is supposed to be making more direct investments, presumably that will also mean that those investments will not be made through intermediaries in tax havens.

Mr O’Brien: That is precisely the point, because it will then have the power and discretion to apply that as a policy. It has been articulated in the new way forward that that is what it wishes to do. It is well defined by the OECD and Global Forum on Transparency and Exchange of Information for Tax Purposes.

Q196 Jeremy Lefroy: We also recommended that tax payments made by CDC’s fund managers and investee companies should be published annually on a country-by-country basis. Are you aware whether that is happening, or about to happen?

Mr O’Brien: It sits within the context of the country-by-country reporting debate that has been going on. Maybe you want to deal with the question of country-by-country reporting slightly separately, but I think it goes to some degree to the same answer as I gave to Mr Gyimah on that. To the extent that we can move as EU Member States together, that is the right approach. Certainly Her Majesty’s Government, led by the Treasury, is very much focused on doing what we can to get that movement together. No doubt you will have the opportunity to ask my fellow Minister shortly. However, we have to be very careful not to do anything that would put the UK’s competitiveness at risk on this. CDC is now redesigned and revamped, with a clear mandate to follow best practice and be world class in patient capital investment and in recognising that it has to be done on this more equitable basis; where it has the discretion as an originator and sole investor, it is able to do so.

Q197 Jeremy Lefroy: Since it is a topical subject, and the Secretary of State issued a statement recently about it, I would like to go back to Actis. He has announced the sale of the remaining 40% owned by the Department. I would just like to go back and confirm that in fact the UK taxpayer, or DFID, has received nothing from Actis since it was effectively partially privatised back in 2003/04, despite owning 40% of it. Is that the case?

Mr O’Brien: That is my understanding.

Q198 Jeremy Lefroy: That is certainly what the Secretary of State told us last week.

Mr O’Brien: Yes. That is what has been put out, and that is my understanding. I have not personally checked that myself, but certainly that has been the advice. I do not know whether any of my officials who are accompanying me have any contrary information. I think that is our well-understood position, as indeed has been published by the Secretary of State, as a result of which, therefore, we have the new arrangements. That is notwithstanding the fact that, as the Government were a member of that company in the past—I use the word “member” in its technical sense—and whilst they remain a
member, the new arrangements have therefore given the Government rights to receive not only a value for the sale of 40% but also the carried interest on future profits.

**Q199 Jeremy Lefroy:** Yes, and I think we welcome the negotiations that the Secretary of State has carried out, which will be more beneficial for the UK taxpayer than the previous arrangements. I have in front of me the Actis accounts for 2007, for instance, in which the total administration costs, which are basically all wages and salaries, short and long-term incentive scheme payments, social security costs and pension costs, came to nearly $125 million for an organisation that employed 187 people. By my very rough calculation, that is something like $600,000 per person. This is 2007, as I say: you could take other years as well, most of which are slightly less than that, but I am taking 2007. This is an organisation in which the UK Government had a 40% ownership and yet was paying an average— I stress, an average—of $600,000 in that year to each of its 187 staff. That excludes any profit share going to members. At the same time, the corporation tax paid in that year on a profit on ordinary activities of $10 million was less than $1 million, i.e. less than 10%.

Of course there will be reasons for that, but it strikes me that we have a situation in which we clearly and understandably want developing countries to improve their tax revenues. We wanted this in 2007, and for long periods before that. Yet at the same time we were a shareholder in an organisation that was paying very little in the way of corporation tax in the UK and was paying astronomical returns both to employees and to members. One cannot talk about risk, because the amount of risk capital is very little—in fact, DFID invested almost the majority of the small amount of risk capital in that business. I would just like your comments on that before I move on to something else.

**Mr O’Brien:** What you have in front of you, I do not have in front of me, and I certainly take your report of that. I know that sitting behind me is the lawyer who has been advising the Department on the Actis arrangements. The best way I can answer this is to try to keep it simple and not too legalistic, although I am tempted to delve back into my past as a solicitor. We have to be very careful about the use of the word “member” or “shareholder”.

In this case, whatever arrangements were entered into when Actis was effectively floated out and sold, it was effectively into a partnership, and as with all partnerships, the question as to where you affix the drawings within the partnership before it yields any surplus or profit is a question of how the arrangements were set up. What is absolutely clear is that under the new deal there is an opportunity for that to have to report and be accountable to members, or in our case a shareholder, before, effectively, the Executive of the partnership has been able to take out the revenues, which, as you reported from the 2007 accounts, is broadly what has happened, leaving none for the contributing members.

**Jeremy Lefroy:** I absolutely understand that.

**Mr O’Brien:** That is effectively what has changed. It is a question of choice, of course, as a corporate judgment, but as a matter of law, had there been an ability to enforce something different without going through a new negotiation to a new arrangement, I am absolutely sure that the Government would have done that. I think there was a difficulty in being able to get to the position we now are in, had there not been effectively new negotiation to reach these new arrangements.

**Q200 Jeremy Lefroy:** I fully accept that, but do you not agree with me that it is quite a difficult position for a Government—we are talking about the last Government, but also to some extent this Government, because they have also been a shareholder since 2010—when we are trying to encourage other Governments to up their tax take and enforce proper taxation of income, and at the same time we have an investment in a company that basically was trading on the back of UK taxpayers’ money. The entire investment portfolio initially came from CDC, which was built up through the UK taxpayer, if I am right.

Therefore, this is a real lesson for the future: we have to be incredibly careful about the ways in which these deals are formulated. This applies to CDC, but also to anything else that we might undertake. Otherwise it looks as though we are being slightly hypocritical.

**Mr O’Brien:** It is more than “looks like”; I think it was. I think it was scandalous, and that is why it had to be addressed, and has been addressed. You are quite right: lessons had to be learned. The Secretary of State has made a number of statements on this, and there have been some issues. I think it has been identified that now we are in a better position than we were, but the main thing is that as an example to those whom we are seeking to partner with in order to help them have a better approach to revenue collection, this is a slightly different situation, because it is not revenue collection; it is effectively a shareholder interest, an investor interest, by Government, which is unusual in itself.

**Q201 Jeremy Lefroy:** I know we are short of time, but there is just one final thing on this. You may have noticed that post-purchase, when the DFID shareholding in Actis was bought out, there were reports in the press that the partners were constructing a rather elaborate arrangement whereby the taxation was effectively done substantially at capital gains tax rates in the UK, as opposed to income tax rates, even though effectively the money is coming through as management fees and is therefore income. Would it not therefore be advisable for the Government to look at that quite closely, because surely, particularly with things like the recent anti-avoidance declaration by the legislation brought in by the Chancellor, we would not want to be seen to be encouraging a situation in which the sale by the Government of their remaining 40% resulted in more anti-avoidance schemes being used?

**Mr O’Brien:** Let me take this opportunity first of all to absolutely place it on the record that no Minister, member of DFID or member of the Government has any interest in Actis in the future, and in this particular set of transactions. So far as the arrangements
between, as you put it, the partners and any tax now and in the future are concerned, that has to be a matter between them and HMRC. I do not think I am in any position to comment on that, but I take your point.

Chair: This may be raised later.

Q202 Mr McCann: One question, Chair; I appreciate that time is short. The Secretary of State has described the Actis deal as “scandalous”, and you have just used similar terms. Can we get copies of the paperwork of the advice given to Ministers at the time the Actis deal was carried out, please?

Mr O’Brien: I think the normal principle would apply: that advice to Ministers is not something that is disclosable. Moreover, I am absolutely sure that, unless I have completely misunderstood the briefings I received from the then Government, the current Government would not be able to command a response that would give you those papers from the previous Government. I will have to look into it.

Q203 Mr McCann: If you could look into it, because in a situation where taxpayers’ money has potentially been wasted, or worse, and where decisions were questioned at that time. I think it is important, for the sake of fairness and transparency, that we understand the advice given to Ministers that led them to make the decision to enter into the deal. If you could take it away, I would be most grateful.

Mr O’Brien: I will certainly take it away. I will certainly look into it. However, I hope you understand my response: I would expect first principles normally to apply on that, although I will certainly take your point seriously and see what we can do, if anything.

Q204 Chair: Thank you very much. One last question, because we know the Treasury Minister has been very patiently waiting for his session. Very brief, but now we come to the technical issue: Do the tax affairs of expats in developing countries are sometimes a little bit unclear. During our first evidence session, I think, we were told by ActionAid that expat staff working permanently in a developing country may pay income tax in the country of origin rather than in the developing country, but that that would be defined by intergovernmental tax rules. They have since come back to us and said that, other than in Cambodia, all their expat staff are registered taxpayers in the countries in which they are working. There are specific things, apparently, in Cambodia that change that. However, we are not quite sure what the position is in relation to other NGOs and indeed other organisations.

As far as the Government are concerned, would you feel that British citizens, if they are residing permanently in a developing country, should pay their tax there rather than in the UK, and that that would be the case whether they were NGOs, multinationals or whatever? Or do you have no position on that?

Mr O’Brien: I think I have to declare an interest, insofar as my father was a District Officer in the Southern Province of Tanganyika in the 1950s. Because that was a protectorate and not a colony, when it became independent it meant that the pension scheme for those who none the less were British Government officials was taken over by what became, after the Tanganyikan Government, the Tanzanian Government in 1964, which was subsequently declared bankrupt. Now in his 80th year, my father receives 67% of the British state pension, because his early years were declared null and void, and the British Government have never stepped up to fill that. There is a big risk for expatriates: in my father’s case it was permanent, certainly for a number of years, as he worked abroad both for the Government of the time and also then the private sector. That was the risk. It depends what you call “permanent”. I declare that as an interest, because it has affected a member of my family.

If you are asking in terms of DFID, the expatriates in our country offices are clearly there with a very important role to play: to bring both management and technical expertise to support the programmes and results that we are determined to deliver by the use of UK taxpayers’ money in securing development objectives for the poorest. They will revolve for anything between six months to three or four years, and come back. That is not regarded as permanent, and they pay UK tax when they are there, as you know.

However, the locally hired staff in those country offices pay local tax, and I can certainly confirm, as a matter of the contracts of employment for locally hired staff, that it is a disciplinary offence not to pay their tax in-country, by whatever methodology tax is collected. There are opportunities and options to choose how you pay it, whether it is through PAYE or other self-declared means. That helps answer the question about expatriates. So far as DFID is concerned, that is why we have that arrangement: it is a mobile transferable work force, if you like, bringing technical and management capacity and expertise to bear on tailored programmes. On the locally hired staff, we have a very clear position.

The other aspect to it is not to do with contracts of employment but to do with the current exemption for other self-declared means. That helps answer the question about expatriates. So far as DFID is concerned, that is why we have that arrangement: it is a mobile transferable work force, if you like, bringing technical and management capacity and expertise to bear on tailored programmes. On the locally hired staff, we have a very clear position.

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Q205 Chair: Thank you very much for that. We have overrun a little bit, so apologies for that, but you have answered our questions very fully. There are a number of issues that we have raised with you, and if you could come back to us on them we would be extremely grateful.

Mr O’Brien: I will certainly undertake to do my very best to give you those.
Chair: Thank you very much indeed.
Mr O’Brien: Thank you.

Examination of Witnesses

Witnesses: David Gauke, Exchequer Secretary, HM Treasury, Steven Effingham, Deputy Director, International Tax Team, HM Treasury, Peter Steeds, Deputy Director, Head of Transfer Pricing, Business International, and Alison Shallard Brown, Head of International Relations, HM Revenue & Customs, gave evidence.

Q206 Chair: It is a great pleasure to have you before us, Treasury Secretary. We do not do opening statements, but would you like to introduce yourself and your team, please?
David Gauke: Yes. Thank you very much, Mr Bayley. It is a great pleasure to be here. If I may, perhaps I will ask the officials to introduce themselves. Steve, do you want to start that?
Steven Effingham: My name is Steven Effingham. I am the Deputy Director of the International Tax Team in the Treasury.
Peter Steeds: I am Peter Steeds. I am a Deputy Director in Business International in HMRC, responsible for transfer pricing. I am also the Vice-Chair of CATA, the Commonwealth Association of Tax Administrators.
Alison Shallard Brown: Good afternoon. I am Alison Shallard Brown. I am Head of the International Relations team at HM Revenue and Customs, and we are responsible for co-ordinating the Department’s capacity building and technical assistance work.

Q207 Chair: Thank you. Let me begin by asking you about the change to the Controlled Foreign Company rules, about which you, Minister, will be aware that many development commentators and NGOs express concern. It has been suggested to us that the change could cost developing countries up to £4 billion per year. Do you accept this estimate?
David Gauke: No, we do not. The first point to make is that it is inherently very difficult to make any assessment of this, because one has to have a full understanding of the interactions between multinational companies located in developing countries and those developing countries and their tax systems, which is a very complex matter. It is not something that, frankly, either HM Treasury nor HM Revenue and Customs is well placed to make an assessment on.
As far as the £4 billion number is concerned, that is based, as I understand it, on an extrapolation of about 10 companies’ financial data. It also makes an assumption that companies would pay the full statutory rate within a developing country, whereas in reality that does not tend to be the case, because there are tax holidays, tax breaks, or what have you. That number we do not find terribly convincing—far from it—but it is quite difficult to make any kind of assessment without having a full understanding of what happens in developing countries as opposed to what happens here.
The other point I should make in this context is that the CFC rules were never designed to protect other countries’ tax revenues. The purpose has always been to protect UK tax revenues. There may well be a case that an ancillary impact of that has been a knock-on effect for developing countries, but I do not think that is a sustainable way in which developing countries can protect their revenue. A much better way is building up their capacity and their capability. The CFC regime is badly in need of reform, and has never been designed with the purpose of protecting other countries’ tax revenues.

Q208 Chair: But we talk, do we not, about the need for joined-up Government—for Treasury policies to fit with, and pull in the same direction as, DFID policies, and indeed policies of other Departments? Surely the impact of a change in the taxation regime in the UK or for the UK on developing countries is something of importance to the Treasury when you are designing a policy. You do not accept the £4 billion figure. You will doubtless have had conversations with DFID about the impact. What is your best estimate? If you are unable to give a figure, would you be prepared to commission some work, some analysis of your own, to produce an estimate of the likely cost?
David Gauke: We cannot give a number, and we do not believe that we could reach a number on this, for the very reason I gave a moment or so ago. It is very dependent on the relationship between a multinational company and a developing country. It is dependent on the tax regime not here in the UK, for which rightly we have to make assessments all the time, but the tax regimes in other countries—both their tax law and their tax administration, and the relationship with multinational companies. We are simply not in a position to produce robust numbers on that, and it is therefore not something that we have done, nor can credibly do.

Q209 Mr McCann: Good afternoon, everyone. Minister, the OECD’s Task Force on Tax and Development was initiated by the UK Government back in 2009. In one of our previous evidence sessions, ActionAid was particularly critical that the current Government was a less active participant in the taskforce than your predecessor. How do you react to that criticism? Do you think it is fair?
David Gauke: I do not think it is fair. From my own personal position, I make no apology that the main focus of my job, while it is a wide-ranging brief, has always been ensuring that the UK has as competitive a tax system as possible. However, if you look at what we have done as a Government over the last two years, in terms of progressing the work on extractives at an EU level and reaching tax information exchange
agreements with developing countries and double taxation agreements with some developing countries, we have made a lot of progress. I think there is a degree to which, from the position of some of the NGOs, a lot of progress was made on particular items that they are very supportive of. For example, the idea of country-by-country reporting moved up the agenda very rapidly. Where we are on that particular issue now is looking at whether country-by-country reporting does what it is supposed to do. Is it effective? Is it getting the balance right in terms of burdens on businesses and in terms of providing people with useful information on how multinationals pay their tax?

That is something the OECD is looking at. We are very supportive of the OECD in performing that task. We want to see what the OECD comes back with and what their assessment is as to whether, for example, country-by-country reporting is useful and in what way it can best be done. In that sense there is a degree to which, a few years ago, ideas were being floated. There is now a rigorous testing of whether those ideas are as effective as people would like, and to some extent I am sure NGOs would like to be moving faster in this area. From the Government’s point of view, I think we should look at the evidence first.

Q210 Mr McCann: Can I just ask a practical question about the Task Force? How often does it meet, and have you attended meetings of that particular group?

David Gauke: I think Steve probably knows a little bit more about that.

Steven Effingham: I am not sure of exactly the number of times the Task Force has met, but attendance tends to be covered by officials from DFID. Officials from my team have attended. The discussions were in the period of the former Government, but the proper launch came later. To explain the Treasury’s role, the Task Force is looking at the evidence on things like country-by-country reporting, whether the system works, whether it is feasible and whether it does what many of its supporters hope it does. The Treasury’s input to that debate is reasonably limited. The input is really about what the costs are, which is information you would get from industry, and what the benefits are, which you would get on the NGO side from people like ActionAid, who are supporters and who have done a lot of work on what the outcome of country-by-country reporting would be. On the Government side, the expertise on benefits as well as on costs is really from DFID, and from that reason the lead on representing the UK Government at the Task Force falls to DFID, though as I say members of my team have accompanied DFID on occasion to see how the work is going, and to get a feel for how the work of the Committee is done.

Q211 Mr McCann: Chair, can I ask if we can get a copy of the data on when the meetings took place? I am anxious to compare the allegations that are made sometimes against Government with the actuality of what has happened. Can you get that information?

Chair: Thank you, Minister.

Q212 Jeremy Lefroy: I refer to my entry in the Register of Interests. We want to come on now to the recent UK-Swiss Confederation Taxation Co-operation Agreement, under which the UK will only be allowed to request tax information from the Swiss revenue authority if it has plausible grounds for doing so. We are not quite sure what “plausible grounds” means, and given that there are increasing demands for a more automatic exchange of information, do you think we should have more clarity on that?

David Gauke: The first point to make on this is that this is a big step forward, because previously the opportunity of getting any information from Switzerland was very limited indeed, if not non-existent. This is actually progress in terms of getting more information from the Swiss. I think we can provide a note to elaborate on “plausible grounds”, but essentially it is about having some evidence: not fishing expeditions but specific evidence relating to particular taxpayers.

The point I would make on this is that there was no prospect that we could see that the Swiss were going to agree to automatic exchange of information. There is no indication whatever that they would be prepared to enter into such an arrangement. The Swiss banking secrecy laws have been in place for some years and there is considerable support within Switzerland for them. Indeed, if there is a controversial change of law in Switzerland, there is always a strong possibility of a referendum as well. We did not see a realistic prospect that we would move towards automatic exchange of information with Switzerland.

However, the Swiss deal, in terms of the ability to get some information out of Switzerland, the fact that there will be a levy charged on those funds for the past and indeed ongoing collection of sums relating to matters in the future, more or less in line with our rates of income tax, is a big step forward. It is noticeable that there are a number of other countries: obviously Germany have been going along a similar track as us, but the likes of Austria, Italy and Greece are also looking to explore this. It is a big step forward in closing down one potential route through which tax evaders were able to hide their money. That opportunity is now being lost to them, and I think that is a big step forward for us.

Q213 Jeremy Lefroy: Can I just move on to transfer pricing legislation? Do you see a need for tighter transfer pricing legislation, given that apparently something like 60% of world trade is intra-company? There is a suggestion around for some form of apportionment, whereby companies’ taxable profits would be allocated based on the proportion of total property, payroll or sales in each country. I can see some flaws with that in the sense that pay rates and so on are far higher in countries that maybe have lower tax rates, so that would perhaps defeat the point. Do you think there are moves that could be taken towards some tighter transfer pricing legislation?
**David Gauke:** Clearly transfer pricing is important, and has a very important role to play in ensuring that the right amount of tax is paid in the right jurisdiction. The UK does a lot in providing support to other jurisdictions in terms of that. I will ask Peter in a minute to say a word or two about what we are doing in that field. You are right to identify some flaws in the idea that apportionment could be done on some kind of formula. Inherently the correct and fair amount has to depend on the nature of the transaction. It has to be much more specific. If you had a formulaic apportionment regime, it would be a very blunt instrument indeed, so I think there are some concerns about it. However, you are right to raise the issue of transfer pricing. Capacity building is really important for us from the point of view of the Treasury and HMRC in terms of assisting the Government’s objectives to help developing countries, and transfer pricing is one of the areas where we should focus. Peter, perhaps you would like to say a word or two on that?

**Peter Steeds:** Thank you, Minister. Picking up on the formulary apportionment issue, it is a method that is convenient and that does not have support from OECD countries. Whilst it potentially has the attraction of simplicity, what it will fail to do is attribute profits to the key intangibles that are highly valuable to multinational businesses, both in terms of patents and marketing intangibles such as trademarks. It would also tend to attract profits to large markets, where you have most of the turnover of multinational businesses. That will give a completely different result from trying to apply the arm’s length principle, which looks to replicate what the economic position would be if the multinational enterprise were trading as a series of independent entities. It would be very much a substitute for the arm’s length principle, which is the international standard. What we are trying to do is to work both with developing countries and through the OECD and other international forums, firstly to get some clarity on what the arm’s length standard is, but also to enable developing countries to implement the arm’s length standard and to apply it effectively. Perhaps I could say a few things about some of the work HMRC has been doing to achieve that. We are very active in delivering training programmes, partly through the OECD and partly through other forums, and we have contributed to around 30 training programmes over the last two or three years. We also have secondments: a senior transfer pricing official, who has also worked with ATAF, has been seconded to SARS, the South African Revenue Service, for two years. One of ATAF’s main interests is around transfer pricing, and the individual seconded from HMRC was instrumental in developing their policies around transfer pricing, which is now spreading among ATAF members.

The other really important area is the training that we deliver through CATA, the Commonwealth Association of Tax Administrators. There is an international transactions course starting this week in Malaysia: we have presenters there next week and the week after, delivering training on treaties and transfer pricing. For the first time, for the transfer pricing week, the co-presenter is a Kenyan presenter. I think it speaks volumes for how some developing countries have increased their transfer pricing skills that Kenya, which is a very good example of a country that has made a lot of progress, is now able to provide a presenter to train other tax officials from developing countries. Perhaps my colleague might say something about CATA courses.

**Alison Shallard Brown:** Yes. HMRC has been involved for about 20 years in supporting the Commonwealth Association of Tax Administrators, and every summer we host two six-week programmes in the UK. One is for senior officials from Commonwealth countries, which looks at developing their leadership skills and at a wide range of issues around good tax administration. The majority of participants are from sub-Saharan African countries. We also run the Commonwealth tax inspectors course, which is a technical programme welcoming compliance officers and technicians. Again, the majority of participants are from developing countries. That is something that the Department invests heavily in every year, with around 500 days of staff time going into that programme. It gets very good feedback from delegates, and I think it is a major contributor in terms of developing those individuals and the input that they are then able to take back to their home Administrations.

**Q214 Mr McCann:** Minister, we spoke to Stephen O’Brien about the technical assistance relationship between HMRC and DFID. I wondered what, in your view, were the particular aspects of technical assistance that HMRC is best placed to take the lead on in relation to overseas work. If DFID asked you to do more work, does HMRC have the capacity to upscale its technical assistance role in any DFID projects in the future?

**David Gauke:** You always have to answer that question with “up to a point”, because there must come a point where there would be a constraint. Certainly from my point of view, however, I have always been very supportive of the work that HMRC does in—

**Q215 Mr McCann:** I am not a communist; you would get paid for it, I would imagine.

**David Gauke:** I am delighted to hear that, on all grounds. There are always two issues. There is DFID paying for it, but this is highly skilled work and there is also the issue of ensuring that we have the right individuals to be able to do it. I think HMRC has shown real willingness to engage in this. The Permanent Secretary for Tax, for example, has spent a considerable amount of time on this issue, and provided a lot of support to the Rwandan tax authority in particular. There is a real desire and willingness on the part of HMRC to provide that technical support and, speaking as the relevant Minister, I am very supportive of that. That is something where we can really add value, if you like. It is important that the capability of developing countries in assessing and collecting tax is something that we focus on. That argument is made by many people, NGOs and others, and it is absolutely right.
Where we can do that best is by providing some of that technical support. I am pleased with the record that HMRC has over many years. I will not claim that year zero was two years ago. It has been over many years. Certainly, this Government are very keen to encourage that, and as a Minister I am very keen to encourage that.

Mr McCann: Thank you very much.

Q216 Mr Gyimah: This is to HMRC. Firstly, one thing we have not actually heard from you is whether you think transfer pricing abuse is a serious problem. It would also be good to hear what you think HMRC can do to tackle this. While you are answering that, we have also heard from the CBI of businesses offering to co-operate with HMRC in the field of transfer pricing. It would be interesting to hear whether you have taken these offers up.

David Gauke: I think probably Peter is the best person to answer.

Peter Steeds: Yes, I think that is a question that comes to me. Your first question was around transfer pricing compliance, and the extent to which it is a problem. Transfer pricing is a very big compliance for all multinational businesses, and it is part of their bread and butter compliance structure, because they have to price every intra-company transaction they have going cross-border. The majority of multinational enterprises will look to do that with one objective in mind, and that objective is to ensure that there is no double taxation at the end. The basis on which they file will be compliant with the tax rules in both jurisdictions—the jurisdictions at either end of the transactions. It is true to say that there is a certain amount of what could be styled aggressive tax planning—using transfer pricing to move profits into low-tax jurisdictions. My experience is that that is very much the minority of circumstances. The issue, both for developed and developing countries, is being able to tell the difference between those two, and then to direct your resources at the latter and try to support multinationals in complying in the first instance. From HMRC’s perspective, our objective is to enable developing countries and emerging countries to both have effective transfer pricing legislation and build their compliance skills so that they can work effectively with large businesses, audit large business effectively and negotiate settlements with large business effectively, and do effective risk assessment to pick the difference between those two categories of circumstance that I have previously described. That is the first part of the question. Could you just remind me of the next part, please?

Q217 Mr Gyimah: The second part of the question was to do with business having made offers to co-operate, and whether or not you have taken them up on those offers.

Peter Steeds: I am not particularly aware of specific offers that we have had to work with business to assist developing countries. We work closely with business and with practitioners here, and we would be very interested and would respond very positively to those sorts of invitations, for two reasons. Firstly, HMRC has limited capacity in terms of people with the necessary skill set. This is a pretty scarce resource. Secondly, a working partnership between HMRC and business would give a much better perspective to developing countries in terms of their understanding of how this system works.

Q218 Mr Gyimah: What can HMRC do to help developing countries in this?

Peter Steeds: I think I have already referred to some of those things. We support a lot of training programmes; we have outward secondments, and we have had some inward secondments. I am not sure if the ones that I am particularly thinking about quite come into the developing country category, but we have had a series of secondments from the Chinese tax administration, and we are currently discussing some further secondments.

It is also important to bear it in mind that HMRC is seen as a world leader in transfer pricing, so we also interact with developed and emerging countries. We are still taking secondments from some of those countries. I think the final thing I want to say is that the Tax Inspectors Without Borders programme, which is promoted by the Tax Justice Network, looks very interesting, and that is something that we would also be interested in contributing to. Again, however, it is a question of balancing the resource capability that we have.

Q219 Mr Gyimah: Thank you for that. What I was driving at is that the CBI suggested that you offer advice on how to detect and deter tax evasion from either corporates or high net-worth individuals, and I just wanted to know whether that is something that you are already doing, and if you are, whether you would be willing to scale that up.

Peter Steeds: I can only really speak for the transfer pricing area. Perhaps Alison can talk about other areas. One other interesting area in transfer pricing is that the OECD has held its first Global Forum on Transfer Pricing this year, in March, which was attended by 250 delegates from 90 countries, including lots of developing countries. Their work programme for the first year is to look at risk assessment to be able to enable particularly non-OECD members to select appropriate cases for audit. HMRC has a strong role in that. Our published risk assessment guidance is almost the foundation of the work going on through that group.

Alison Shallard Brown: I think there are two further examples to add to that. We have a long-term capacity building programme in Ethiopia, supporting the Ethiopian Revenue and Customs Authority, and we have covered a broad range of managerial and technical topics there, with a particular focus on risk management and improving compliance techniques. The particular achievements that the Ethiopian Revenue and Customs Authority have made as a result of that are shown in their tax yield; since 2002 they have gone up from collecting ETB8.2 billion per year up to ETB70 billion for the last year.

Another area in particular where we are working on compliance issues is through the new DFID iFUSE programme, the Investment Facility for UK Specialist Expertise, which is a new fund designed to help us
mobilise technical expertise in Whitehall. This year we will be delivering some technical assistance to Uganda, which again will be focusing on tax investigation and how we can help to build capability and train trainers in Uganda to deliver those skills.

**Q220 Mr Gyimah:** Thank you. I have a final question on technical assistance. We heard in one of our previous evidence sessions that senior experts from developed countries, which probably ties into what you just referred to, such as retired accountants, might be mobilised to provide technical assistance to revenue authorities on a pro bono basis. You mentioned mobilising expertise in Whitehall, but do you think this is something that could be encouraged? **Alison Shollard Brown:** At the present time, it is not something that we do within HMRC. We use our own staff and administrators, but yes, it is an interesting idea to explore the different kinds of partnerships that we could have, and how we might make best use of retired expertise too.

**Q221 Chair:** There are just one or two points I would like to pick up on arising from the questions and answers of this session and the previous one. It is clear to me that HMRC provides a lot of support and advice to tax authorities in developing countries, but I wonder how much that is complemented by decision-making in the UK. If, for instance, you find in a company’s balance sheet profit that you think should be more reasonably taxed in a developing country, rather than in the UK, would you seek to push the tax revenue in the direction of a developing country? Or when you are looking at the financial affairs of UK companies, are you maximising or ensuring that you obtain tax that is due in the UK? In other words, is it a joined-up policy? **Peter Steeds:** Yes. I think the answer to that is that our primary focus would certainly be looking to see that the right amount of tax was being paid by the UK resident companies. We would focus on what we see as the high-risk transactions, which would often perhaps be unlikely to be transactions with developing countries, partly due to the size of the markets in many of those countries. We would look far more at high-risk transactions, for example, transactions that would move profits into low-tax jurisdictions.

**Q222 Chair:** Other than the UK? **Peter Steeds:** Yes, other than the UK, absolutely. We would see the UK as a “normal rate” jurisdiction. What we would do, though, if we saw something that we thought was particularly abusive to a third country, is make, and we have made, voluntary exchanges of information with that country, where we have the appropriate treaty provisions. We work with treaty partners in that way. However, I have to say that it would not be a primary focus of our inquiry.

**Q223 Chair:** I am interested in the qualification you put in there: “where there is an appropriate treaty”. We had a discussion in the previous session with Stephen O’Brien about the benefits of automatic information exchange, and I think he told us that his Department was strongly committed to adopting a new international regime that would allow, as a norm, automatic exchange of information, as it currently is within the EU. Perhaps I should ask the Minister how committed the Treasury is to that. Where are you seeking to negotiate some global agreement on automatic information exchange, and what do you think is the timetable for achieving it? **David Gauke:** In principle, automatic exchange is exactly what we should be aiming for. There are certain caveats. For example, from our perspective we need to ensure that there is sufficient protection of taxpayer confidentiality, in terms of ensuring that other regimes are comparable to our own. For example, there has been a lot of progress, as you mentioned, with regard to the EU, but one has to look at other jurisdictions in light of whether the same protections exist. It is difficult to put necessarily a timetable on it, and one should also bear in mind some of the burdens that may be imposed on businesses. There are practical considerations for businesses and indeed tax authorities, because there is a danger of being swamped with information that is not always helpful. In principle, however, automatic exchange of information is the right direction to be going in, and where we can make progress in a way that is practicable, we can do. However, it is difficult for me to give a timetable.

**Q224 Chair:** The US Foreign Account Tax Compliance Act unilaterally imposes obligations on banks to report major transactions that US nationals or US companies have in foreign banks. Why couldn’t we just go ahead and enact similar legislation in the UK, so unilaterally we would achieve at least a certain measure of automatic information exchange? **David Gauke:** The FATCA legislation is a good illustration of some of the challenges and difficulties that can exist at a practical level. Certainly, there have been considerable concerns across the European Union about the challenges that the FATCA legislation has imposed on banks in particular, but also on other financial institutions. The Treasury has been very engaged in dealing with the US authorities to try to find a practical way whereby their objectives can be met without imposing unnecessary burdens on businesses here in the UK and elsewhere in the European Union. That provides an illustration of some of the challenges that exist there. It is very difficult for the UK or the EU to try to impose on third parties and third countries in the way that the US does. Partly, we have less of a tradition of extraterritorial impositions than the US does, and partly there is striking the right balance on that. Are we moving in a direction of more exchange of information? Absolutely we are, and I welcome that. Steve, is there anything you want to add on FATCA? **Steven Effingham:** One point perhaps worth adding on FATCA is that, although the aim of FATCA is information exchange and there is an extraterritorial imposition, in order to make that stick the US has had to design a very complex and burdensome system of withholding and pass-through payments to ensure that transferring information is an easier and better option for financial institutions. A lot of the discussions that
we in the UK and our colleagues in the European Union have been having with the Americans are around how that system can be made to work. The practical difficulties of applying a single rule even to five European jurisdictions, let alone to the whole of the world, is proving a real challenge for all concerned. Even though the US has the advantages to which the Minister alluded, it is finding that simply applying automatic exchange on a global scale is far from a straightforward venture.

Q225 Chair: Thank you. If I could go back to Peter Steeds’ comments about what I think you called “high-risk transactions”—where an activity, perhaps a sale of services by a company in a low-tax jurisdiction, transfers profits from a higher tax regime to a lower tax regime—you said this is something you would look at. I imagine some of those lower tax regimes could be the Channel Islands, the Isle of Man, Gibraltar and other British dependent territories. To what extent are those lower tax regimes covered by OECD agreements, and to what extent does your Department—I mean the Treasury—impose certain standards upon regimes operating broadly under UK protection?

David Gauke: Let me start by saying that as far as the Crown Dependencies are concerned—Jersey, Guernsey and the Isle of Man—my understanding is that they are on the correct OECD lists in terms of exchange of information and so on, and obviously we are keen to encourage that. There have been times when a Crown Dependency has been criticised in terms of the EU Code of Conduct on tax, but steps have been taken to correct that. That is more to do with tax competition, rates and so on. As far as exchange of information is concerned, their record is not bad. Steve, do you want to add anything to that?

Steven Effingham: No, I think that covers it. There is clearly a commitment on the part of the Crown Dependencies to meet the international standard. They have moved at slightly different paces in terms of, say, signing up to automatic exchange under the Savings Directive, but since the G20 launched the Transparency Initiative back in 2009, I think there has been a significant shift in attitude in the Crown Dependencies. Certainly the number of tax information exchange agreements they have signed with other countries, including with us, has gone up enormously as they have sought to meet the standard set by the G20 and the OECD.

Q226 Chair: Thank you. Finally, we legislated some years back to require banks to report on politically exposed people—Ministers, Members of Parliament, senior civil servants, judges, senior military officers, and so on—whether UK nationals or not. I understand from talking to my bank manager that if £20,000 was deposited in my account, they would start with a conversation with me, and if I could assure them that it was my South African godmother’s legacy, they would be satisfied. If they were not satisfied, they would have to report to the Treasury. How many such reports, in respect of a) UK citizens and b) foreign nationals, do you receive a year?

David Gauke: I certainly do not know that information. This would be something for HMRC. I assume, but I do not know the answer.

Steven Effingham: I think it may be for a separate part within Treasury, but we can certainly dig into that and see if these figures are retained, and if possible we would of course report to the Committee.

Q227 Chair: The concern from a development angle is this. Often in Africa, Africans will point the finger at Britain and London and say, “When our ne’er-do-well leaders steal assets—the Abacha billions, for instance—and bank them in London, London does little to help us repatriate stolen assets.” There was a Nigerian case recently, where the Governor of Delta State, I think, was convicted through the British courts—or certainly there were convictions. How hungry is the Treasury to ensure that, where there is a transfer of criminally obtained assets from a developing country to London, we expose it, bring culprits to justice, and return assets to the countries in question? Perhaps, again, this is a matter of giving us a note. Could you instance cases of where this has happened over perhaps, I would say, the last 10 years, to see if there is a trend to do this more frequently and more often, and make whatever policy comments you wish to make?

David Gauke: First of all I would say, of course, we are very supportive of that policy, and indeed it is the law. I think this is probably a matter for SOCA as much as anything, and they may well be able to enlighten the Committee on that perhaps more than we can do, but we can certainly find out what the position is.

Q228 Chair: Should we leave it that we write to SOCA with that question, or that we leave the question with you and you consult with SOCA?

David Gauke: I am entirely relaxed—whatever would be most helpful, to be honest, from your perspective.

Q229 Chair: If you could let us have what information you can from Treasury and/or Revenue sources, we will, as you suggest, make our own inquiries of SOCA.

David Gauke: Fine.

Q230 Chair: If there are no other questions from colleagues, I would like to thank you very much for your attendance. We are finishing on time.

David Gauke: Thank you very much.
Written evidence submitted by ActionAid

About Us

Founded as a British charity in 1972, ActionAid is an international NGO working in 45 countries worldwide, and our positions and recommendations reflect the experiences of our staff and partners in Africa, Asia, the Americas and Europe. Our vision is a world without poverty and injustice in which every person enjoys the right to a life with dignity. We work with poor and excluded people to eradicate poverty and injustice. In 2003 we became ActionAid International and moved our global headquarters from the UK to South Africa. Our rights based approach, which looks at the systemic causes of poverty, forms the foundation for our work on development. We continue to play a leading role in the debate in the UK and globally around tax justice, aid effectiveness and accountability for developing countries.

For more information on our work on tax justice, and to discuss further written or oral evidence on any of the subjects covered in this submission, please contact Sebastian Dance, ActionAid’s government relations adviser, sebastian.dance@actionaid.org.

Summary

1. We are delighted that the International Development Committee is conducting an inquiry into tax and development. Tax is, as the founding communiqué of the African Tax Administration Forum states, an indispensable condition on the path to “free African countries from their dependence on foreign assistance and indebtedness.”1 The same could be said of developing countries in every part of the world.

2. Tax is crucial to developing countries’ long-term capacity to alleviate poverty, build effective and accountable states, and foster sustainable, equitable growth. As a recent paper from the OECD underlines, increased tax revenues will be indispensable to achieving the Millennium Development Goals.2 Yet all too often at present, tax systems in developing countries, alongside global tax rules that affect them, fail to deliver these outcomes. In too many instances, foreign investors and top earners are not taxed sufficiently, and the payments they make to governments are misused; as a result, countries are looking to the poor, in particular the informal economy, to expand tax revenues.

3. We are encouraged by the growing resolve in many developing countries, particularly in Africa, to mobilise more domestic resources, and to tax multinational companies more effectively. There is much more that the UK government can and should be doing to assist these efforts, including:
   — developing a cross-Whitehall tax and development strategy, which will ensure coherence between UK tax policy decisions and DFID’s development work;
   — increasing the financial and human resources within DFID devoted to tax and development; and
   — requiring tax havens and multinational enterprises to be more transparent, enabling developing countries to identify cross border avoidance and evasion.

4. It appears at present that there is little coordination between tax policy developed at the Treasury, technical assistance delivered by HMRC, and capacity building work supported by DFID via country offices and multilateral bodies. To maximise the value for money gained from UK aid, and the benefits from DFID’s work to promote the private sector in developing countries, it is essential that these three departments work together under a coherent tax and development strategy.

The Importance of Tax for Development

5. Many developing countries already fund the majority of their budget through taxation. For example, taxes constitute 72% of government revenue in Zambia3, and 71% in Ghana.4 So it is concerning that, once oil revenues are factored out, tax revenues for Africa as a whole have been stagnant over the last three decades.5

6. Trade liberalisation during that period caused falling tariff revenues in developing countries, resulting in policy advice that focused on pragmatic means of increasing tax revenues as quickly as possible, such as the

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2 OECD Development Centre, “Revisiting MDG Cost Estimates from a Domestic Resource Mobilisation Perspective”, December 2011. Available at http://www.oecd.org/document/27/0,3746,en_2649_33731_49302043_1_1_1_1,00.html


introduction of VAT, without due consideration for the impact of such reforms on poor people. Few developing countries assess the distributional impact of tax reforms on different parts of the population in the way that the UK does in each budget.

7. Corporate taxation constitutes an important proportion of tax revenues in developing countries. In Zambia, for example, corporate income tax, withholding taxes and mineral royalties, all borne by companies, constitute 31% of tax revenue. With this in mind, tax avoidance and evasion by multinational companies significantly reduce the amount of revenues available.

8. The OECD estimates that tax havens cost developing countries three times what they receive in aid. South Africa’s finance minister Pravin Gordhan has described aggressive tax avoidance as “a cancer eating into the fiscal base of many countries”; last year the Treasury noted that “tax avoidance in developing countries deprives governments of the vital income needed to build and maintain their public services.” Given the government’s commitment to providing value for money for UK taxpayers, it makes very little economic sense to allow this situation to persist.

THE IMPACT OF TAX DodGING BY UK-BASED COMPANIES ON DEVELOPMENT

9. Recent ActionAid research showed for the first time the full extent of tax haven use by FTSE 100 companies. Ninety-eight of these multinational groups are using tax havens, where 38% of all of their subsidiaries located. High street banks are the heaviest users, with 1,649 companies operating in tax havens shared between Barclays, HSBC, RBS and Lloyds. The data also illustrate the risks for developing countries: the biggest 10 tax haven users have a total of 3,833 subsidiaries in tax havens, but they also have 1,951 in developing countries.

10. Some 40% of all world trade takes place between companies that are part of the same multinational group. These “transfer pricing” transactions play an important role, not just in distributing goods and services between group companies, but also in distributing profits and tax liabilities. Yet the system by which they are regulated provides ample room for companies to shift their profits away from countries in which the economic activity occurs, which have higher tax rates, and towards those in which the liability is much lower, all without breaking the law.

EXAMPLE: SABMILLER

11. ActionAid’s report Calling Time; Why SABMiller should stop dodging taxes in Africa, showed how one major FTSE100 company uses transfer pricing payments to shift an estimated £100 million of taxable profit from developing country subsidiaries where genuine economic activity is taking place into tax havens, where it incurs a much lower tax rate. This includes royalty payments for the use of trademarks, management service fees, procurement payments and interest on loans from sister companies, all of which are treated as tax deductible.

12. The overall impact of the large outflows on developing countries is that their tax receipts are dramatically diminished. For example, the net effect of the outflows from SABMiller’s Ghanaian brewing subsidiary in 2008 and 2009 was an overall pre-tax loss. ActionAid estimates that payments to Switzerland, the Netherlands and Mauritius from SABMiller’s subsidiaries in Africa and India resulted in a total tax loss to governments in those countries of £20 million, enough to put 250,000 children in school, and equivalent in Africa to almost one-fifth of the company’s estimated tax bill.

13. The kinds of tax avoidance employed by multinational companies in developing countries are not available to domestic entrepreneurs. For example Marta Luttgrodt, who works 12-hour days running a small bar in Accra, must pay £47 per year in taxes, part of the government’s scheme to tax informal sector traders. In contrast, the SABMiller brewery from which she purchases supplies paid no income tax at all as a result of its transfer pricing payments. “We small businesses are suffering from the authorities,” Marta told us. “If we don’t pay, they come [to lock our stalls] with a padlock.”

14. The types of payments channelled from developing countries to tax havens in the example of SABMiller are by no means unique: “tax-efficient supply chain management” is a growing part of business restructuring, and the exploitation of royalties on intellectual property to shift profits is challenging for the UK as well as for
developing countries. “Your research findings seem to be borne out by the experience that we know in tax practice in this country,” Ghana’s Commissioner General for taxation told ActionAid.13

A COMPREHENSIVE TAX AND DEVELOPMENT AGENDA

15. The previous government adopted an international leadership role on tax and development. DFID’s 2009 white paper stated that “effective tax systems are central to effective states” and noted the “increasing concern that tax systems in developing countries are undermined by international banking secrecy, including in tax havens.”14 Gordon Brown ensured that the 2009 London G20 summit committed to “developing proposals... to make it easier for developing countries to secure the benefits of a new cooperative tax environment.”15 Treasury minister Stephen Timms initiated the creation of the OECD’s task force on tax and development, in which ActionAid participates.

16. In contrast, the current government has adopted a more passive approach in international forums such as these. The government’s position is that “the best way to prevent” tax avoidance in developing countries “is by helping these countries develop robust and stable tax systems which enable them to collect the tax they are owed.”16

17. This issue should be receiving much more attention from DFID, but it must also be part of a coherent cross-Whitehall strategy. The dichotomy between international reforms and domestic capacity-building rarely occurs in our discussions with revenue officials and other stakeholders in developing countries, who recognise that both are needed in the long term. Based on these discussions, we believe that the step change in tax collection that is needed cannot be achieved without action in all three of the areas discussed in more detail below.

Recommendation 1: DFID should lead the development of a cross-Whitehall strategy on tax and development that ensures tax policy is made in a way that maximises the value for money delivered from UK taxpayers’ contribution to overseas aid.

(i) Strengthening DFID’s tax and development work

18. When it is done well, tax capacity building generates results: past assistance from DFID and other donors helped Rwanda to quadruple the amount of tax it raised between 1998 and 2006, and Uganda to increase its tax-to-GDP ratio from 7.2% in 1991 to 12.6% in 2003. There is considerable unfulfilled demand from developing countries for tax capacity building work, to which DFID should respond through increased quantity and quality of technical assistance.

Devoting more resources to tax and development

19. In August 2011, ActionAid asked the Treasury, DFID and HMRC for a list of activities supported by each department that build tax capacity in developing countries. We received a comprehensive spreadsheet of information from HMRC.17

20. DFID has taken some time to gather the information because it is not available centrally, and is handled by individual DFID country offices. Given the emphasis placed on tax capacity building in the government’s response to campaigners, the fact that DFID does not maintain an overview highlights the lack of focus on this vital area of policy. Last year, the IMF, World Bank, OECD and UN recommended in a report to the G-20 that donors report specifically on the resources devoted to tax and development.18

21. The information from HMRC shows that staff time equivalent to three or four full time positions is invested in projects that support tax capacity building in developing countries. Tax officials from developing countries speak highly of this assistance, which is delivered by experienced, practising officials. There seems to us considerable room for DFID funding to increase the provision of this technical assistance.

22. The lack of central coordination by DFID—of its own departments and of the strategic direction across government—is concerning. We understand that DFID HQ has only one member of staff focused on the tax and development agenda, working on it part time.

Recommendation 2: Given its central role in reducing aid dependency, tax should be a more important priority for DFID, with more aid resources and dedicated HQ time.

13 ActionAid interview, 23 September 2010. This comment, although made in response to our evidence related to Accra Brewery, was general and not in relation to a specific company.
14 DFID, 2009, “Eliminating World Poverty: Building our common future”.
16 Grice, A op cit.
17 We have attached the HMRC spreadsheet in annex
Supporting efforts to hold governments accountable for tax policy

23. Civil society organisations, journalists and parliamentarians all play an important role in driving forward changes in tax policy and administration, and promoting fair, open and transparent policymaking. For example:

— As a result of our report on SABMiller, revenue officials from Zambia and several other African countries met under the auspices of the African Tax Administration Forum (ATAF) to discuss its implications. As a result, ATAF is now developing a mutual assistance treaty that will better equip its members to work together to investigate multinational companies’ tax affairs.19

— Zambia’s new government introduced measures in its first budget to more effectively tax the extractive sector. This reform was an election commitment resulting from a significant public debate during the election campaign driven by civil society organisations, the media, and parliamentarians.

— ActionAid and its partners across developing countries monitor budgeting-processes and help local communities to engage. For example our partner in Ghana, the Integrated Social Development Centre (ISODEC) published a “Taxation Ghana Made Simple” guide for organisations wishing to engage in budget advocacy, holds regional public meetings to raise awareness and solicits opinions on budget proposals, and each year publishes a budget review.

**Recommendation 3:** DFID should devote more resources to support programmes that engage civil society organisations, journalists and parliamentarians in the tax policymaking process, as well as investigative work that holds governments to account for the taxation of companies and top earners.

Raising the quality of technical assistance

24. While technical assistance has been at the root of many notable successes in the history of development aid, in many instances aid has been wasted on projects that are poorly coordinated between donors, ignorant of the realities of public administration in developing countries, and unlikely to have a lasting impact because it is not based on the priorities identified by developing countries themselves.20 We are already concerned that, in the rush to support stronger tax administrations, bilateral and multilateral donor agencies are offering assistance that fails to learn these lessons.

**Recommendation 4:** The African Tax Administration Forum (ATAF) is developing a diagnostic toolkit, which will allow developing countries to identify their own needs and priorities for capacity building. DFID should ensure that such approaches are central to the delivery of technical assistance on taxation, including by the multilateral agencies that it funds.

**Recommendation 5:** Some businesses have suggested that they would be willing to support capacity building in African tax authorities. This suggestion should be treated with caution, as it would be a clear conflict of interest for “capacity building” on tax policy and administration to be provided by taxpayers, many of which are active lobbyists.

(ii) Policy coherence across Whitehall

25. We are concerned that several UK positions on international tax policy risk undermining efforts to help developing countries raise more tax revenues, which represents poor value for money for UK taxpayers. We discuss two here.

Spillover analysis

26. The aforementioned report from the IMF, World Bank, OECD and UN to the G-20 included the following recommendation:

> 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...in moving, for instance, from residence to territorial systems.

27. The committee may be aware that the government is currently undertaking a major reform of corporate taxation.21 This is an example of a UK tax policy reform that has the potential to impact on developing countries, because of the extent of UK companies’ operations in both developing countries and tax havens. Particularly noteworthy are plans for Finance Bill 2012 to relax anti-tax haven abuse legislation called Controlled Foreign Companies (CFC) rules. ActionAid is concerned that the proposals will eliminate a significant deterrent that discourages UK-based companies from shifting profits from developing countries to tax havens.

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21 The core of these reforms is to move from a residence tax system, under which UK-based companies are liable for tax on their worldwide earnings with credits for taxes paid overseas, to a more territorial system, under which overseas earnings are exempt from UK tax.
28. We estimate that the reforms may cost developing countries as much as £4 billion, and have urged the Treasury and DFID to conduct their own spillover analysis, as recommended by the international organisations. No such analysis has been undertaken.

**Recommendation 6:** In line with the government’s commitment to getting value for money from its aid, it is essential that a development spillover analysis for the CFC reforms is conducted immediately, or commissioned from an international organisation such as the IMF or OECD. This should incorporate:
- the potential change in companies’ behaviour that may result;
- the characteristics of developing countries (for example investment patterns, tax legislation, enforcement capacity) that would be likely to increase exposure to this impact; and
- the measures that developing countries or the UK could take to help mitigate any impact.

Appropriate international tax rules

29. At present, the dominant international tax rules in areas such as transfer pricing and information exchange are those set by the OECD. Although the OECD is making commendable efforts to reach out to developing countries in its tax work, standards are ultimately negotiated between its 35 members, and designed with them in mind. Yet it is these standards that donors are encouraging developing countries to adopt.

30. The United Nations tax committee is an efficient, effective body that has developed alternative standards tailored to the circumstances of developing countries. For example, its model tax convention is used by developing countries in tax treaty negotiations, and it is currently developing a practical manual on transfer pricing in developing countries. The committee is constrained by a lack of financing.

31. Last year, the UN’s Economic and Social Council considered plans to strengthen its tax committee. These were supported by the G77 group of developing countries, with vocal agreement from all developing country members of the G20. Unfortunately, the UK was among countries that opposed the move, citing its preference for work to be undertaken within the OECD.22

**Recommendation 7:** When this discussion re-emerges, as is likely within the next few years, the government should support a stronger UN tax committee as part of a coherent tax and development strategy.

(iii) Increasing tax transparency

32. Developing countries’ tax administrations require not only improved capacity, but also increased access to tax information. This requires developed countries to agree to and implement changes in their approach to transparency. ActionAid supports two reforms in particular.

Transparency of multinational companies

33. Last year ActionAid participated in a working group commissioned by the OECD and convened by the Oxford University Centre for Business Taxation to consider proposals for greater corporate transparency, in particular country-by-country reporting by multinational companies.23 The report concluded with a list of recommendations for further research, many of which have not been adopted by the OECD.

**Recommendation 8:** We urge the government to ask the OECD to take forward these recommendations in full.

34. The committee will no doubt take an interest in the corporate transparency measures currently proposed by the European Commission, which include country-by-country reporting of some information. While we support this additional transparency, it is worth being aware of a number of limitations which mean that these reforms are unlikely to help meet the objective of ensuring that tax payments made by multinational companies in developing countries are adequate:
- they are limited to the disclosure of payments to governments, but do not include the other financial information needed to interpret this, such as turnover and profits;
- they may not cover all countries in which companies have a presence, since they are likely to be limited to “production countries”, therefore excluding offshore jurisdictions to which profits may have been shifted for tax purposes; and
- they are restricted to the extractives and forestry sectors.

35. In the absence of an international standard, many businesses have begun to report their “total tax contribution” in developing countries. This is a misleading statistic, which combines taxes borne by the company itself with those borne by consumers and employees, such as VAT and income tax.

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22 Individual countries’ written positions can be viewed at http://www.un.org/esa/ffd/tax/2011SGReport/RepliesMS.htm
Multilateral information exchange initiatives

36. Two problems faced by developing country revenue authorities are the lack of information on individual and corporate taxpayers’ offshore affairs, and legal restrictions that prevent them from discussing a multinational taxpayer with each other.

37. There are a number of encouraging developments in this area, including a commitment made by all G20 members to join a multilateral convention on mutual assistance in taxation, and the establishment of regional conventions, such as those under development by ATAF and the South African Development Community. Many developing countries are also concluding bilateral information exchange agreements.

Recommendation 9: The government should support developing countries with technical assistance to develop and join conventions that they expect to find useful. It is important that this is based on the principles that we outlined earlier: developing countries should not be discouraged from adapting the standards and model conventions developed by OECD countries for their own use.

Recommendation 10: The government should also ensure that the G20 continues to exert pressure on tax havens to improve tax information exchange, and to ensure that developing countries benefit from this, as per its 2009 commitment.

Recommendation 11: We share other organisations’ concerns that the UK’s tax cooperation agreement with Switzerland may undermine global efforts to help tax authorities in developing countries gain the information they need from tax havens, because it is a bilateral deal that leaves banking secrecy intact. We believe that this is another example of a tax reform that warrants a spillover analysis of its impacts on developing countries.
## Annex

**TECHNICAL ASSISTANCE DELIVERED BY HMRC, 2009–11**

**INFORMATION SUPPLIED TO ACTIONAID BY HMRC IN DECEMBER 2011**

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Notes

HMRC did not include country names in order to preserve the confidentiality of requesting authorities.

“International Revenue Authority” under “Aegis” refers to direct requests made to HMRC by revenue authorities in developing countries.

The Commonwealth AMP and CTI events are principally attended by low income and low middle income African countries.

February 2012
Supplementary written evidence submitted by ActionAid

Additional evidence from ActionAid, April 2012

1. Following the oral evidence sessions of 28 February and 24 April, we have a number of clarifications for the committee.

ActionAid Staff in Developing Countries

2. Martin Hearson was asked in oral evidence whether ActionAid employs any British expatriate staff in developing countries on permanent or long-term contracts and who do not pay tax in the countries in which they work. We have now investigated this question and can confirm that all of our expatriate staff are registered taxpayers in the countries in which they work. We are aware of only one exception to this, in Cambodia, which is the result of a local law concerning expat NGO staff which we expect to be reversed soon. We would like to emphasise that the vast majority of our staff are nationals of the country in which they work.

SABMiller

3. A number of statements given by Graham Mackay, SABMiller’s Chief Executive, in his oral evidence merit some clarification:

3.1 Mr Mackay stated that “our production is all local”, a point that is hard to reconcile with SABMiller’s own information. Its website states that, “In 2010 we established a global procurement business called Trinity Procurement. For those products and materials such as packaging that all our businesses require, we are able to establish group-wide buying deals and benefit accordingly.” Mr Mackay has previously stated that “Taxation was a key part of our decision to locate [this] new global procurement business not in the UK but in Zug in Switzerland.”


As a further example, Zambian Breweries’ 2010 accounts show that around 80% of its cost of sales was attributed to goods and services sourced from SABMiller procurement hubs in Mauritius and South Africa, rather than locally.

3.2 Mr Mackay suggested that SABMiller has a high effective tax rate, which places the company in the “upper quartile of the FTSE100”. The company’s effective tax rate according to its 2011 annual report was 28.2%, which exceeds the UK statutory rate, but not that of many of its major operating markets. For example, its biggest single market is South Africa (23% of pre-tax profit) where the statutory rate is 34.55%; its biggest region is Latin America (31% of pre-tax profit), where the statutory rate in four of its six operating countries exceeds 30%.

3.3 We have attached a copy of SABMiller’s response to our allegations, which we sought ahead of the publication of our report, for the committee’s information in the light of Mr Mackay’s comments about our correspondence. Elements from this response were incorporated into the final published report, and the response was published on our website along with the report on the day of publication.

Public Availability of Accounts

4. Emmanuel Mutati, Chief Executive of Mopani Copper Mines, explained to the committee that his company’s accounts are filed with the appropriate official body in Zambia and, suggested that they are available for public access. We can inform the committee that, in common with many developing countries, our colleagues in Zambia have been unable to gain access to these accounts (or indeed those of many other major multinational companies) through this channel, despite repeated efforts. This is of great concern to civil society organisations in developing countries, but it also creates obstacles to the effective administration of transfer pricing by revenue authorities, by limiting the availability of ‘comparables’. We contributed to the report on this subject prepared by the OECD secretariat, to which Chris Lenon of the Business Advisory Committee to the OECD referred, and we encourage the committee to seek a copy of this report for a useful summary of the issues in this area.

The Arm’s Length Principle

5. We would like to make an observation concerning the point made by Mr Lenon about the arm’s length principle. We agree that a key reason that developing countries get a raw deal from transfer pricing is that most of the activities undertaken by multinational companies in developing countries are low value-added, and therefore result in a low allocation of taxable profits. But the current system of transfer pricing actually plays a causative role in the business decisions that lead to this unfavourable distribution of high- and low-value activities.
6. As was observed by a number of witnesses, the major issues in transfer pricing are intangible assets, group services, and the reorganisation of business supply chains. Transfer pricing encourages the location of these business activities in low-tax jurisdictions. Businesses will choose to centralise functions for a variety of reasons, but the fact that they frequently do so in low-tax jurisdictions suggests that the tax motive is one driver. An article in the Financial Times by a KPMG tax adviser explains that, "of the supply chain reorganisations we advise on, there is a rough 50:50 split between those based around a low tax location and those where tax savings do not feature."\(^{26}\)

7. For example, SABMiller states in its written evidence that it has centralised the administration of its intellectual property management and its management services. In doing so, it has moved many of the higher-value activities of its business out of developing countries and into low-tax jurisdictions (on paper, the Netherlands and Switzerland). Regardless of the motivation for this centralisation, it not only affects the global distribution of SABMiller’s tax liability, but also the extent to which its investments result in positive spillovers such as knowledge transfers and economic linkages in the local economy.

**Written evidence submitted by ActionAid, the CBI, and Christian Aid**

ActionAid is an international NGO working in 45 countries worldwide, headquartered since 2003 in South Africa. Its rights based approach, which looks at the systemic causes of poverty, forms the foundation for its work on development. For more information please contact Sebastian Dance, Government Relations Adviser, sebastian.dance@actionaid.org 020 3122 0630.

Christian Aid is a Christian organisation that works globally in over 40 countries for profound change that eradicates the causes of poverty, striving to achieve equality, dignity and freedom for all, regardless of faith or nationality. For more information please contact Sol Oyuela, Senior UK Political Adviser, SOyuela@christian-aid.org 0207 523 2109.

The CBI is the UK’s premier business lobbying organisation, speaking for more than 240,000 companies of every size, including many in the FTSE 100 and FTSE 350, mid-caps, SMEs, micro businesses, private and family owned businesses, start ups, and trade associations and in every sector. For more information please contact Richard Woolhouse, Head of Tax & Fiscal Policy, richard.woolhouse@cbi.org.uk.

1. While ActionAid, Christian Aid and the CBI have made separate submissions in response to the Committee’s call for evidence, we wish to let the Committee know about one very important issue on which we agree. People who work for member companies of the CBI, as well as Christian Aid, ActionAid and their partner organisations, share a common goal of helping to improve the living standards of those in developing countries. We may not agree on all the ways in which this might be achieved—or indeed what all of the root causes are. But we do agree that a properly functioning tax system—one based on good tax policy, and an efficient tax administration—is critical to the functioning of a stable, prosperous state that responds to the needs and wishes of its citizens.

2. There is currently a substantial demand from developing countries, in particular many in Africa, for support from the UK and other developed countries to help them raise more tax revenue. This includes capacity-building to assist with the formulation and administration of tax legislation, in particular in the area of international taxation. As NGOs and UK businesses working in developing countries, we encourage the UK government to devote more resources to supporting this demand, including through the provision of funding and technical expertise. Technical assistance should at all times be driven by demand from developing countries themselves, and we support the work of the African Tax Administration Forum to develop a diagnostic toolkit to assist countries in assessing their own needs.

3. We strongly urge DFID to take a more active role in the coordination of tax capacity building work, through both the support of HMRC projects in these countries, as well as through its country offices, in conjunction with the aid agencies of other countries, and via multilateral organisations and the technical assistance programmes they offer.

4. We would emphasise that the practical work that HMRC has already done in terms of training, and ongoing support, has proved very valuable in countries such as Rwanda, and an expansion of these capacity-building efforts would be enormously beneficial.

5. This effort needs to be on-going. These capacity issues cannot be solved by a single conference, but by the patient sharing of experience and building of relationships between tax professionals and other stakeholders such as NGOs.

6. We also believe it is important for DFID to report publicly on the whole of the government’s work on tax and development.

*February 2012*

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Written evidence submitted by Christian Aid

1. INTRODUCTION

1.1 Christian Aid is a Christian organisation that insists the world can and must be swiftly changed to one where everyone can live a full life, free from poverty. We work globally in 45 countries for profound change that eradicates the causes of poverty, striving to achieve equality, dignity and freedom for all, regardless of faith or nationality. We are part of a wider movement for social justice. We provide urgent, practical and effective assistance where need is great, tackling the effects of poverty as well as its root causes.

1.2 Christian Aid has been working on tax and development issue for a number of years, and became the first leading NGO to make it a major campaign priority in 2008. Since then the importance of the issue has been recognised by the G20, the UN, the OECD, the IMF and by many large businesses. Christian Aid was in 2010 identified as one of the 21 most influential organisations in the world of tax by International Tax Review. Christian Aid is a member of the OECD Informal Taskforce on Tax and Development, the Taskforce on Financial Integrity and Economic Development, the Tax Justice Network and the International Tax and Development Centre.

1.3 We welcome the opportunity to provide written evidence to the International Development Committee on taxation and development. We are happy to provide further written/oral evidence on any of the subjects covered in this submission via Sol Oyuela, Senior UK Political Adviser

1.4 We would like to draw attention to the submission presented by CTPD28, a Christian Aid partner in Zambia. Given their extensive work in the country on tax and development issues, we consider they are better placed than Christian Aid to comment in depth on the situation in Zambia, therefore we will not extensively address Zambia’s situation in this submission. We are also signatories to a joint submission by Christian Aid, ActionAid and the Confederation of Business and Industry (CBI) highlighting our common concern for the need to support developing countries in mobilising revenue through capacity building and technical assistance.

2. WHY TAX MATTERS FOR DEVELOPMENT

2.1 Effective tax systems are essential if developing countries are to end their reliance on aid. Developing sustainable and effective tax regimes providing revenues for essential public services is key to ensuring that in the long-term developing countries are free from reliance on Official Development Assistance (ODA) for development needs.29 The OECD recently highlighted the crucial role of domestic resource mobilisation in financing the MDGs.30

2.2 Yet the ability of developing countries to collect revenue is undermined by tax abuse, facilitated by financial and corporate secrecy. Christian Aid estimates abusive tax practices relating to international trade cost developing countries $160 billion each year.31 Other organisations, such as the UNDP,32 have provided a range of estimates. While estimates vary, it is recognised by all organisations undertaking such studies, including the OECD, that the revenue lost to tax dodging is vast, significantly more than the levels of ODA currently (or ever likely to be) available to developing countries.33

2.3 There are three inter-related issues hindering the development of effective tax regimes in developing countries: (a) lack of capacity to collect revenue; (b) limited policy space to devise and implement appropriate tax policy; and (c) a global financial system governed by rules and norms detrimental to developing countries which they had (and continue to have) a limited voice in determining.

2.4 These issues combine, resulting in a situation whereby developing countries have narrow tax bases and high levels of abuse, evasion and avoidance of tax. This triple challenge of expanding the tax base, countering abuse, and building trust in the tax system is faced by many of the countries in which Christian Aid works.

2.5 Our submission will focus on the three issues outlined above, highlighting the connections between them. DFID’s focus on building the capacity of governments to increase tax revenue collection is welcomed (though can be improved) and an important aspect of the solution to this problem. However this is not enough to enhance the effectiveness of tax regimes for better development outcomes; such efforts must be coupled with work at the international level to ensure that policies and practices of actors at the global sphere do not undermine the capacity and space for developing countries’ governments to enhance the effectiveness of tax regimes. To genuinely address tax and development, DFID must work across Government to promote a coherent approach to addressing this challenge, to ensure that DFID’s aid efforts deliver value for money in a bigger context.

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33 See http://www.guardian.co.uk/commentisfree/2008/nov/27/comment-aid-development-tax-havens
3. THE NATIONAL CONTEXT: THE IMPORTANCE AND LIMITATIONS OF CAPACITY BUILDING

3.1 Governments need to be able to formulate and implement tax policy responsive to their national contexts, as well as be held accountable by citizens for the funds raised and spending made. Christian Aid is working in developing countries supporting local partners to ensure that governments are responsive and accountable to citizens, both in identifying needs and how governments raise and spend revenue (for example, monitoring budget spending and campaigning to improve its allocation). With DFID’s support, Christian Aid’s Governance and Transparency Fund supports in Dominican Republic Centro Montalvo which has formed the “Educacion Digna” coalition, calling for the government to meet the law requiring 4% of GDP to be spent on education. It is vital to combine efforts to increase revenues with efforts to ensure these revenues are spent effectively, with a clear development outcome. Moreover, an increasingly tax aware civil society is likely to play an effective part in expanding the tax base to the large informal sector, not least from tax payer education and building trust in the tax system. Christian Aid would welcome additional support to civil society for such initiatives.

3.2 There is currently a substantial demand from developing countries, in particular in Africa, for support from the UK and other developed countries to help them increase tax revenue. Such is the consensus on this area that Christian Aid, ActionAid and the Confederation of Business and Industry (CBI) have submitted separate evidence urging DFID to proactively coordinate the capacity building work that is undertaking through its country offices, HMRC and via multilateral organisations.

3.3 DFID provides technical support directly to revenue services in developing countries, which we encourage. For example, in Zambia DFID is one of only two governments providing support to the revenue authority. However, we understand DFID is now looking to move away from this to focus on governance which could leave Zambia’s revenue authority short of the support it needs. Also in Zambia, DFID’s efforts to strengthen the policy unit in the Ministry of Finance, has been described as delivering “mixed results”. Overall there is limited reporting on the strategic direction of DFID’s work in relation to tax, the initiatives that are being supported and how aid spending is being allocated. This makes it difficult to assess DFID’s work in the area, and therefore there is a need for more transparency with regard to DFID’s work in the area, including improved reporting.

3.4 While strengthening tax revenues authorities and expanding the tax base is crucial, such efforts must be coupled with work to improve taxation policy making at the national level. For example, the OECD shows that policies of tax exemptions and holidays offered by many developing countries have delivered limited results in terms of increased revenues or investment. In Ghana, the ability of the Revenue Authority to enforce effective transfer pricing legislation is hindered by its inability to estimate the cost of transfer pricing abuse. While a strong evidence base is vital for effective policy formulation, capacity constraints mean robust research is rare.

3.5 Policy and technical assistance provided by DFID should be coordinated with other donors and demand driven in line with the Paris Principles on Aid Effectiveness. In Zambia for example, while the revenue authority is receiving donor’s support, a lack of coordination with other ministries means that the Ministry of Finance, which usually undertakes policy development, is being usurped of its policy making responsibilities to the extent that a “serious imbalance of power” is noted.

3.6 This shows the importance of donors and others working on tax to consider the wider policy context in which capacity-building interventions happen. Christian Aid strongly welcomes DFID’s support to the International Tax and Development Centre, and encourages DFID to ensure that policy support on tax is impartial and needs based.

3.7 However domestic capacity building is limited by global constraints; it is to these factors that we now turn.

4. THE GLOBAL CONTEXT: THE NEED FOR UK GOVERNMENT POLICY COHERENCE

4.1 Globalisation has made tax an international issue; capital can cross borders instantly, the growth of international trade and multinational companies creates challenges for taxation policy. The constrained power of developing countries at the global level makes it difficult for them to assert their right to independent tax policy, and to influence global norms which have been developed to serve the purposes of developed countries. This severely hinders their ability to effectively tax their economies and become independent from aid.
4.2 Capital flight and tax evasion and avoidance, as referred to in the ToR of this enquiry are areas of significant concern for developing countries. Capital flight from developing countries is vast, $8.44 trillion 2000-09,50 in Africa it is of such a level that despite being the poorest continent in the world it is a net creditor to the rest of the world, a situation that guarantees that it will remain the poorest continent.42 However, actions at developing country level are not sufficient to tackle the problem.

4.3 The main causes of capital flight in Africa have been assessed by the US based think- tank Global Financial Integrity to be: corruption (3%), criminal proceeds (30–35%) and the processed of commercial tax evasion, primarily transfer pricing abuse (60–65%).43 Domestic capacity building alone cannot address these problems. The Zambia revenue authority has 0.099 tax officials per 1000 people, nearly three times higher than the sub-Saharan African average of 0.037, but more than eight times lower than the world average of 0.82.44 Given developed countries themselves struggle to run effective tax regimes with significantly more capacity it’s implausible that developing countries will be able, in the medium term, to effectively bridge the capacity gap to make the gains required to meet the Millennium Development Goals. To address this problem effectively one must focus on the global mechanisms enabling capital flight. The international policy responses that can be implemented to solve this problem must be led by both developed and developing countries, as today, developing countries lack the agency to do so.

4.4 Global financial secrecy undermines the effectiveness of developing countries tax regimes. Tax evasion and avoidance is facilitated by tax havens (or secrecy jurisdictions) which provide financial and banking secrecy making it very difficult for developing countries to trace funds that flow to such jurisdictions, and to obtain information from such jurisdictions to conduct investigations.46 Developing countries need ways to access information without high administrative burdens. The current ‘on request’ information exchange agreements have shown limited effectiveness.47 Automatic Exchange of Information (currently applied within the European Union through the Savings Directive) would provide developing countries revenue authorities with the information necessary to more effectively trace and tax funds. Yet, while much progress has been made through the G20 and Global Forum,48 many more agreements are required. Today, developing countries lack the influence to effect change in relation to tax havens, yet are bearing a high cost. Christian Aid is part of a global campaign which in the context of the G20 in November 2011 delivered a petition to President Sarkozy, signed by 40,000 people around the world, calling for an End to Tax Haven Secrecy. Christian Aid believes that the UK Government is in a unique position of influence over the matter given the significant power that it holds over the global financial sector (and in light of the UK Crown Dependencies and Overseas Territories), and should therefore lead and support action to end tax haven secrecy, including at the G20.

4.5 Developing countries need to counter transfer pricing abuse, but their scope to act is limited. One of the primary methods by which tax is avoided is through abusive transfer pricing.49 Effective regulation of transfer pricing under the current global norm of the arms length principle is difficult50 and was recently confirmed by the system’s arch proponent—Jeffrey Owens, Former Director of the Centre for Tax Policy and Administration at the OECD.51 This applies especially to developing countries facing capacity constraints. However given the OECD’s composition, developing countries have lacked, and will continue to lack, any meaningful say in the development of these guidelines. This is significant as there are substantial questions on both the practicality and applicability of these guidelines for developing countries,52 yet without the ability to influence their development it is impossible for developing countries to address this problem.

4.6 International policy space must be created for developing countries needs to be considered. This is an area with scope for DFID, and other parts of the UK government to improve efforts to support developing countries. The United Nations is a more legitimate and representative organisation to lead on international

45 Eg see http://www.publications.parliament.uk/pa/pc201011/cmhansrd/cm101206/text/101206w0004.htm#10120650000439 and http://www.publications.parliament.uk/pa/pc201112/cmhansrd/cm111010/text/111010w0005.htm#111011130000459 on the UK moves to devote an extra £900 million and 2,250 staff to address tax evasion and avoidance.
46 http://www.cmi.no/publications/file/4045-taxation-mozambique-tanzania-zambia.pdf—is perhaps the most comprehensive analysis of the impact of tax havens on development.
47 See http://www.nsnunes.nl/public/271011_1.htm for the difficulties the Netherlands faces in utilising such treaties.
48 The Global Forum on Transparency and Exchange of Information for Tax Purposes— http://www.oecd.org/site/0,3407,en_21571361_43584757_1.1_1_1_1,00.html
49 The manipulation of the pricing of trades between related companies, usually with the aim of lowering the tax burden by shifting profits to a lower tax/no tax jurisdiction.
50 Eg PWC note that it is the most difficult area of international taxation (http://www.pwc.com/pk/en/tax-services/transfer-pricing.jhtml)
taxation issues. The UN has a Committee of Experts on International Cooperation in Tax Matters,\(^53\) which is chronically under-funded and under-resourced, but still valued by many for what work it does despite limited resources. For example, the UN model tax treaty (for which the tax committee is responsible) is relied on by many developing countries for double taxation treaties\(^54\) as it “preserves a greater share of tax revenue to the country where investment or other activity tax takes place, while the OECD Model preserves a greater share to the country of the investor, trader, etc.”\(^55\) This consideration is vitally important in the development of transfer pricing legislation, and a key reason why the UN needs resources to enable its transfer pricing work to fully address the needs and requirements of all the countries of the UN, especially developing countries. Such are the limits to the Tax Committee’s resources that Christian Aid co-sponsored a conference to advance the work of the Committee on transfer pricing.\(^56\) While we were pleased to help advance the work of the UN in such a vital area, this is not a long-term sustainable model. In a report by the Secretary General to the ECOSOC General Assembly\(^57\) the challenges faced by the tax committee were made clear, and all options suggested recognised the need to enable the committee to undertake more work. Christian Aid, along with many other CSOs,\(^58\) supports the recommendation of creating an intergovernmental Commission for tax, and retaining the current Committee of Experts as a subsidiary body of the Commission. We strongly urge DFID, and the UK government as a whole, to support this.

4.7 Similarly there are concerns on the policy recommendations being made by the International Financial Institutions (IFIs) on taxation\(^59\) and we would similarly urge the UK to use its influence in the IFIs to ensure policy recommendations are in response to the needs of developing countries.

4.8 Ensuring tax compliance by multinational companies: More can be done to ensure tax compliance by multinational companies (MNCs) operating in developing countries. At Cannes the G20 acknowledged the need for MNCs to be more transparent in their operations,\(^60\) but concrete actions to take this agenda forward are yet to be agreed. Given most MNCs are headquartered in developed countries (the UK is actively encouraging more MNCs to headquarter in the UK)\(^61\) it is difficult for developing countries to effectively ensure compliance on the global policy level. Given the UK is seeking to gain from MNCs headquartering in the UK there ought to be a responsibility on behalf of the UK to the countries where MNCs operate to ensure high levels of transparency, accountability and tax compliance.

4.9 Christian Aid has been advocating for the adoption of a Country-by-Country reporting standard by MNCs.\(^62\) This would allow revenue authorities to have more information to identify which companies should be selected for audit, and also allow citizens to have access to more information about the companies operating in their society. The potential for the private sector to drive development is vast, as DFID has recognised,\(^63\) but this can only provide real benefits for those living in poverty if the returns from the private sector are shared. Therefore, there is a clear need as DFID increasingly promotes private sector led development to also promote mechanisms by which the contribution of the private sector to development can be more effectively assessed, such as a Country-by-Country reporting standard. We recommend that DFID and the UK government support its adoption including as part of the current EU proposals for the Transparency and Accounting Directives.\(^64\)

5. PROMOTING A COHERENT APPROACH TO TAX AND DEVELOPMENT FROM THE NATIONAL TO THE GLOBAL

5.1 A coherent UK approach to tax and development means not only supporting developing countries at the national level, through capacity building efforts, but also making sure UK national level policies are development friendly and the UK is helping ensure developing countries have real space and voice in the international sphere, where crucial tax policy decisions are made.

5.2 We encourage DFID to play an increasing role in ensuring policy coherence for development in UK policy on taxation, as it impacts development and poverty reduction in developing countries. It is well established that policy decisions in developed countries can have an impact on developing countries.\(^65\) and

\(^{53}\) A subsidiary body of the Economic and Social Council.
\(^{54}\) Treaties between states to eliminate double taxation.
\(^{57}\) http://www.un.org/esa/fidf/tax/SGR_InstitutionalArrangements_AUV.pdf
\(^{58}\) See CSO letter in advance of 2011 ECOSOC General Assembly— http://www.cidse.org/uploadedFiles/Publications/Publication_repository/ECOSOC%20letter%20on%20ax%20committee%20final%2028/0June%202011.pdf
\(^{59}\) http://www.christianaid.org.uk/images/imfoccpaper.pdf and
\(^{60}\) http://www.actionaid.org.uk/doc_lib/fidf_tax_policy_developing_countries.pdf
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\(^{62}\) http://www.hm-treasury.gov.uk/dconsult_cfc_detailed_proposals.pdf—pg 93.
\(^{63}\) http://euroud.org/uploadedfiles/whats_new_reports/cbc%20report.pdf for full details on country by country reporting.
\(^{64}\) http://www.dfid.gov.uk/News/Speeches-and-articles/2010/Wealth-creation-speech
this is certainly true in the UK. For example in the last year UK policies regarding Controlled Foreign Companies and an agreement over taxation of UK assets in Switzerland have both caused concern on their potential impact on developing countries.66 The Swiss deal, by preserving secrecy, is retarding a global progress towards information exchange, beneficial for both developed and developing countries alike.67 Global progress on this agenda is vital for the poorest developing countries that lack the clout to force changes unilaterally. Despite this, the response from the UK government has consistently been that these are matters regarding UK taxation only.68 Ensuring policy coherence for development is vital, especially in taxation matters, as the IMF, World Bank, OECD and UN have made a clear recommendation that developed countries undertake ‘spill over analyses’ of proposed changes to the tax system that may have a significant impact on the financial circumstances of developing countries.69 We recommend that the UK government commits to follow this recommendation, and encourage other countries to follow suit.

5.3 DFID should lead in encouraging policy coherence for development across Whitehall. In his “Beyond Aid” speech, the Secretary of State for DFID made it clear that he saw this as part of DFID’s role: “development is about more than aid. It requires a whole of government effort...previous Cabinets have thought about development. But they have not done enough to address development implications and impacts of policies...As Development Secretary in the Cabinet it is my job to ensure that this happens”.70 While encouraging to hear that the DFID Secretary of State sees this as part of his role, there is little evidence that this role is being fulfilled regarding tax and development at present and we believe that DFID could scale up efforts in pushing for UK tax policy, and UK government positions in international fora to be mindful of the development needs of poor countries and ensure any changes in policy do not have a negative impact on developing countries. Such policy coherence can also help ensure Value for Money for DFID spending, and ensure efforts to ring-fence the aid budget for the benefit of the poorest are not undermined by simultaneous loss of capital by developing countries due to tax dodging and capital flight.

5.4 The approach that the UK, and other governments, take to coherent tax and development policy will be key to answering the question posed by the committee on how effective international efforts to promote tax disclosure and transparency are likely to be. The level of commitment to international efforts will determine their effectiveness. A clear commitment by the international community to seriously tackle these issues, including the various recommendations included in this submission are likely to be effective in promoting tax disclosure and transparency. Today, such a clear commitment is absent. While the UK cannot create such an international commitment unilaterally there is scope for the UK to become a world leader, especially given the Prime Minister’s commitment to transparency, including in taxation.71 Through adopting unilateral measures, and supporting multilateral ones, UK leadership would significantly increase the effectiveness of developing countries to generate, collect and spend revenue and continue fighting poverty, today and in the future.

February 2012

Supplementary written evidence submitted by Christian Aid

In Christian Aid’s oral evidence to the Committee on 28 February 2012 we agreed to provide further written evidence on the issue of our estimate that developing countries lose $160 billion a year in lost tax revenue due to transfer pricing and false invoicing. We would also like to provide some further clarifications around some topics raised in our oral evidence.

Christian Aid’s Research Methodology

As we indicated in oral evidence, Christian Aid has previously given evidence to the IDC on our methodology on reaching our figure of $160 billion. This was on 4 March 2009, in evidence given by Dr David McNair.72 We also indicated that one of the reports criticizing Christian Aid’s research that was cited in written evidence by Jersey Finance was based upon flawed assumptions of Christian Aid’s research. The report “Transfer Pricing and Child Mortality” makes much about Christian Aid’s report analysing at too broad a level of trade data stating “some product categories simply contain too great a range for the [analysis] to have any meaning, for example: pharmaceutical products, which contains everything from aspirin to the latest heart disease pills [...]”. However this is not the case, we actually used the most detailed commodity data available (eg “vulcanized rubber conveyor or fence the aid budget for the benefit of the poorest are not undermined by simultaneous loss of capital by developing countries due to tax dodging and capital flight.

5.4 The approach that the UK, and other governments, take to coherent tax and development policy will be key to answering the question posed by the committee on how effective international efforts to promote tax disclosure and transparency are likely to be. The level of commitment to international efforts will determine their effectiveness. A clear commitment by the international community to seriously tackle these issues, including the various recommendations included in this submission are likely to be effective in promoting tax disclosure and transparency. Today, such a clear commitment is absent. While the UK cannot create such an international commitment unilaterally there is scope for the UK to become a world leader, especially given the Prime Minister’s commitment to transparency, including in taxation.71 Through adopting unilateral measures, and supporting multilateral ones, UK leadership would significantly increase the effectiveness of developing countries to generate, collect and spend revenue and continue fighting poverty, today and in the future.

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transmission belts”) but to make the report a more practicable size these were then aggregated for publication, a fact that was clearly indicated in the report.

The methodology has been further debated at the World Bank71 with the conclusion being a general agreement that it would be difficult to have done much better with the data that was available.

We acknowledge that the accuracy of any figure would be improved by improved data, but in the years since we published our research there has been increasing acceptance that there is a significant problem regarding developing countries ability to collect tax revenue, and that the issue raised by our research, transfer pricing, is one of the biggest issues within this (see original submission). While we therefore encourage further research into the scale of the problem, we would encourage an even greater focus on solutions to the problem.

VAT

In the evidence presented in the session immediately following ours, there was discussion about the impact of VAT style consumption taxes and we thought it would be useful for us to clarify our own position on this issue.

The role of VAT in developing countries is an area of ongoing debate, and is an area where more research and understanding is required. The main concerns of Christian Aid is the potential for VAT to be a regressive tax, though we accept that this impact can be reduced by either zero-rating or exemptions of essential goods and services. However in the specific question posed by the committee on the relative focus on direct or indirect taxes, as stated in oral evidence, we would be wary of paying too little attention to direct taxation.

The levels of inequality both generally, and especially within tax systems in many developing countries74 is such that attention must be given to tax policy with very strong levels of progressivity. Also many developing countries are already heavily dependent on indirect taxation.75 So as developing countries seek to increase the overall tax take to rely on indirect taxation for this would increase this reliance still further and help perpetuate inequality, especially where government spending is not adequately targeted at the poor. Furthermore while the argument in favour of VAT style taxes for developing countries has often stressed the efficiency of the tax, there are questions over just how accurate this interpretation is.76

The main point we would stress is that developing countries need to be able to have both the capacity and space to be able to devise a tax policy mix that will deliver the revenue, equity and fairness required for sustainable development. What role VAT may play in this process is likely to vary, and this needs to be acknowledged in the advice that is being given to developing countries; a situation that does not appear to be the case currently.77

**Automatic Information Exchange**

Relating to our response on what kind of information should be included in the automatic exchange of information, we would like to add the following comments.

The Multilateral Convention on Mutual Assistance in Tax Matters states that: “The Parties shall exchange any information, in particular as provided in this section, that is foreseeably relevant to: the assessment and collection of tax, and the recovery and enforcement of tax claims, and the prosecution before an administrative authority or the initiation of prosecution before a judicial body. Information which is unlikely to be relevant to these purposes shall not be exchanged under this Convention.”78

This is a good starting principle; in practice this would likely to include mean information such as; beneficial ownership information, bank account numbers, Tax Identification Numbers and assets, though this is not an exhaustive list.

OECD

Lastly we feel it is also appropriate to clarify our position regarding the OECD. We sit on the OECD Taskforce on Tax and Development, and we acknowledge and support the work of the OECD in the realm of tax and development.

However, in order to find solutions to issues of taxation that work for all countries we believe that all countries must be included in this process. Given the limited membership of the OECD, and the remit that it derives from that, we believe the current approach does not facilitate this. Notwithstanding some important

72 Eg in Brazil.
73 On average developed countries get 35% of their taxes from direct taxation, this is significantly higher than Bangladesh (20%) and Ghana (22%), and especially Latin America (4%)—see http://www.christianaid.org.uk/images/complete-taxadvocacy-toolkit.pdf Chapter 1 page 4.
74 http://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&frm=1&source=web&cd=1&ved=0CCkQFjAA&rurl=http%3A%2F%2Facademiccommons.columbia.edu%2Fdownload%2Ffedora_content%2Fdownload%2Ffac%3A126734%2FCONTENT%2FSuglizs_Development_Oriented_Tax_Policy.pdf&ei=y4BfT6jYKu5g0QWcyGkBw&usg=AFQjCNG7G8dcfeM2Ji3b0Pe5E1n-tAj1KA
75 http://www.brettonwoodsproject.org/art-561926
progress being made by the OECD, we advocate a more inclusive alternate approach (eg through the UN tax committee) given the limits outlined above.

We would also like to reiterate our support for the IDC conducting this enquiry into tax and development and offer any further assistance you may require. Ensuring developing countries are able to collect and effectively spend their own resources will not only ensure that value for money of UK aid, but more importantly will allow for a future where developing counties move beyond aid dependency.

29 May 2012

Written evidence submitted by The Centre for Trade Policy and Development (Zambia)

The Centre for Trade Policy and Development’s Role and Engagement with Tax Issues

1. The Centre for Trade Policy and Development (CTPD) is a non-profit making, membership based trade policy think tank which aims to promote equitable, pro-poor trade policies and practices, based in Lusaka, Zambia. CTPD provides analytical research, capacity building and facilitation services in trade and investment sectors to civil society, local private sector, small scale producer groups and government.

2. We are grateful for the opportunity to contribute towards this important investigation by the International Development Select Committee. CTPD have been engaged on tax related issues five years. Our aim is to ensure that the people of Zambia receive tangible benefits for the trade undertaken within the country. Our programme of work in this area promotes accountable and responsive economic governance, particularly in participatory policy reform in addition to investing in the poor as well as the exploitation of natural resources and utilization of public revenue. Through this work CTPD desires to contribute to the affected communities increasing their demand for equitable benefits from exploitation of natural resources.

3. CTPD have been particularly active in relation to issues of mining taxation. Alongside partners from other civil society organisations, we have been actively campaigning for a windfall tax on the mining companies. CTPD have also been very involved with tax issues relating to the Mopani mine, majority owned by the FTSE listed Glencore group. A pilot audit report commissioned by the Zambia Revenue Authority (ZRA) that was subsequently leaked to the Zambian press suggested systematic tax evasion by the company. CTPD has campaigned vigorously to ensure that Mopani pays all the taxes it owes to the ZRA, and was one of five organisations to submit an OECD complaint on this topic to the Swiss and Canadian national contact points.

4. CTPD is a partner of several international NGOs, including ActionAid and Christian Aid. We have also assisted ActionAid in their investigations into the Zambian tax affairs of SABMiller, providing in depth analysis of the implications of the Zambian corporation tax system for multinational companies.

5. In August 2011, CTPD launched the Zambian Tax Platform. The main aim of the initiative is to increase stakeholder engagement and public debate around tax issues in a simplified manner, so as to add value and influence the policy process in Zambia. The Tax Platform also links to other similar networks both locally and internationally. The Platform seeks to link civil society, business and government officials to promote effective tax policy making in Zambia.

Tax and Development in Zambia

6. In Zambia, two thirds of the population live below the poverty line. Average life expectancy is 46 and just £15 is spent on each school pupil a year. At the same time, Zambia has recently been officially classified as a middle income country and the country is rich in mineral deposits. It is clear that tax policies, both of the Zambian government, but also of the wider international community, are vital to deliver long term prosperity to the people of Zambia.

7. Taxation has several important functions, including: raising revenue for spending on agreed national and local development plans; influencing the economic behaviour of companies and individuals; and encouraging tax-paying citizens to hold their governments accountable. Combined with economic growth, taxation can help developing countries like Zambia deliver social and economic development and reduce aid dependency.

8. In its 2010 country report on Zambia, the IMF stressed the need for enhanced revenue mobilization, especially from the mining sector. The IMF calculated that Zambia’s revenues and grants total 19.7% of gross domestic product (GDP) in 2009 and its expenditure 22.4%, leaving a gap of 2.7% of GDP to be bridged by financing. Mining taxes total 1% of GDP (this is projected to rise to 2% by 2010, but the gap will still stand at 1.6%). Furthermore, Zambia’s capital spending is low compared to neighbouring countries, and this should rise.

TAX AND MINING COMPANIES

9. Zambia’s large mineral reserves are its richest natural endowment. Copper mining is the main source of foreign exchange earnings and an essential part of the country’s developmental plans.

10. There are many ways to tax mining, but these are some of the main ones:

(a) Royalties—payable as a percentage of the market value of minerals. These are the principal way governments extract an economic rent for allowing a mineral to be dug out of the ground and removed from the country.

(b) Income taxes—employees in the mining sector, like other workers, pay a proportion of the salary in tax through Pay As You Earn (PAYE). When applied to companies, income tax is usually called company tax or corporate tax, and it takes a percentage of the taxable income (ie the profit) of the mining companies.

(c) Other corporate citizenship taxes will also apply to mining companies in the course of their work, such as customs duty on goods imported into the country, or VAT on goods bought locally. These are sometimes the subject of remissions (exemptions or deductions), as has been the case in Zambia.

(d) Companies are often charged withholding taxes on interest, management and consultancy fees, dividends, rent, commissions and payments to non-resident contractors, although these may be the subject of remissions.

(e) Export taxes—export taxes can be applied to exports of raw materials as an incentive for further in-country refining and processing.
11. Existing empirical evidence continues to show that in spite of the relative importance of the mining sector to the country its contribution to the GDP as well as to promoting inter-sector linkages is relatively small. This is due to the detachment of mining from Zambia’s social and economic activities.

12. Zambia’s mining tax regime is strongly focused on attracting foreign investment through low rates and an assortment of incentives. But this needs to be balanced with the urgent need to raise more revenue from mining in order to invest in infrastructure and the country’s economic development. The optimal balance between these two objectives has not yet been struck.

13. The Zambian Revenue Authority has a particular problem effectively administering variable corporate profits tax. It’s a widely held view in Zambia that many large companies effectively chose the amount of corporation tax they wish to pay. Zambia’s most recent EITI disclosures (for 2008, disclosed in 2011) illustrate this: of 16 extractive companies operating in Zambia, only seven reported paying any corporation tax. The total tax paid by these seven companies was 443 billion kwacha (£54 million), which is small compared to the size of the country’s mining sector. In part, this is due to a lack of capacity within the ZRA, but more fundamentally it is a result of the difficulty the ZRA has in enforcing transfer pricing rules.

14. A report by PWC Zambia states that “In Zambia transfer pricing legislation exists. Section 97A of the Income Tax Act introduces the arm’s length principle…. The enforcement of the legislation by the ZRA has however not been as aggressive as expected.” Transfer pricing legislation is extremely complex for developing countries to enforce effectively as revenue officials lack access to the necessary information. Much of the country’s mining activities are structured to minimise taxes, for example as branches of companies registered in tax havens.

15. The revenue-based windfall tax, repealed in 2009, is a simpler way to tax windfalls than the existing variable profit tax, which has not yet delivered any revenue. Had it remained in force, the windfall tax could have contributed many hundreds of billions of kwacha to government coffers. Given the limited capacity of the Zambian authorities to assess mining companies’ claims on profitability levels, the windfall tax should be re-introduced, at least until such a time that Zambia is able to administer a profits based tax effectively.

16. Public discontent concerning the lack of revenue generated through mining taxation is fuelled by the secrecy of government relations with mining companies. This needs to be resolved by greater public dialogue on key tax issues. Greater transparency, which assured citizens that companies were making a fair contribution and not shifting profits into tax havens would help to resolve this issue.

17. It is also important to remember that developing the mining sector implies more than attracting foreign investment. The structural transformation of the production side of the economy, including diversification, requires government investment, which requires revenue. In the long-term view, mining copper is not an end in itself, but a means to becoming a more advanced economy.

Example: Grant Thornton’s Pilot Audit Report on Mopani Copper Mines

18. Mopani is the second biggest copper and cobalt producer in Zambia. It operates the Mufulira mine, which is the largest underground mine in Africa and employs 10,000 people.

19. 73% of the company is owned by Glencore, the Swiss based commodities trader, which has recently floated on the London stock exchange. Ownership is via a string of holding companies in well-known tax havens including the British Virgin Islands, Bermuda and ultimately Switzerland. The government of Zambia holds 10%, with the remainder owned by a Canadian company, First Quantum Minerals.

20. A pilot audit report, commissioned by the Zambian government and carried out by Grant Thornton and Econ Poyry, examined mining activities from 2006 to 2008. A draft of the report, described by the Zambian Revenue Authority as which the Zambian Revenue Authority has described as “confidential, preliminary and incomplete” was leaked to the Zambian press in February 2011. Glencore has argued that the report “contains fundamental factual errors” and refuted its conclusions.

21. The auditors found that Mopani Copper Mine “resisted the pilot audit at every stage”. The company’s book keeping was incomplete, several legally required documents were lacking and the general ledger analysis showed several loopholes and couldn’t be matched with the trial balance.

22. The report accuses Mopani of selling copper to Glencore in Switzerland at below market price—contravening OECD rules on arms-length pricing and effectively shifting profits from Zambia to Switzerland.

23. According to the report, Mopani hedged its copper sale prices, but “the hedging pattern of Mopani is more equal to moving taxable revenue out of the country than true hedging.” Glencore’s freight charges were
based on fixed fees to Rotterdam, even when the actual shipments were made to closer ports, artificially increasing shipping costs.

24. The auditors also found what they described as an inexplicable doubling in the operational costs of the company from 2005–7. The mine is loss-making, and Mopani has paid no corporation tax since it purchased the mine from the government over ten years ago.

25. Calculations by ActionAid based on the figures within the audit report suggest that the practices outlined in the report, if correct, would have cost the Zambian government up to £76 million a year in lost corporation tax. That’s more than the £59 million a year the UK government gives Zambia in aid. In addition, the Zambian government would be losing out on dividend payments relating to its 10% share in the company. ActionAid estimates that this would be as much as £30 million a year.

26. In response, Glencore has argued that this was an interim pilot audit and that the rise in costs is a result of Mopani processing copper mined by third parties. However, the audit states that third party transactions were incorporated into its analysis, and that "Mopani have used every opportunity available to hamper the progress of the audit".

27. The auditors stated that "the Mopani cost structure cannot be trusted to represent the true nature of the costs of the Mopani mining operation." Their conclusion was "The pilot audit has shown that there is a high need for a determined effort at collecting the taxes that are assessed under the laws implemented by the Zambian parliament."

28. CTPD has worked closely with communities living near the mine in Mufulira, which have long suffered from the environmental impact of the operations. Sulphur dioxide emissions in the area continue to exceed safe levels. Sulphuric acid used in the mining process has also leached into the water table, with majors incidents in 2005 and 2008.

29. We continue to press the government to resolve the situation, ensuring that Mopani Copper Mines pays the full amount of overdue taxes.

TAX AND OTHER MULTINATIONAL COMPANIES

30. While mining remains the key export industry for Zambia, there are also significant problems with the taxation of multinationals and large businesses in other sectors of the economy.

31. CTPD advised ActionAid on the Zambian tax affairs of SABMiller. The final analysis in ActionAid’s “Calling Time” report showed that SABMiller avoids an estimated £1.6 million in corporation tax in Zambia each year. The company achieves this by making significant payments to subsidiary companies in Switzerland & the Netherlands for management & royalty fees. These fees were 36% of operating profit in 2009.

32. In its response, SABMiller’s Zambian subsidiary (Zambia Breweries) claimed it is regularly audited by the ZRA. This suggests that current international tax rules don’t work for developing countries like Zambia, and that the ZRA has been unable to effectively audit multinational companies like SABMiller. In the meantime, Zambia’s Auditor General, however, has confirmed that it is investigating the allegations.

33. Ultimately, building public faith in the corporate tax regime requires an end to the culture of secrecy around taxation and more communication with civil society and companies. A more effective tax system requires more transparency and information.

RECOMMENDATIONS

34. DfID should continue to support capacity building for the ZRA.

The ZRA now has more mining accountants than before and a dedicated Mining Tax Unit supported by the Norwegians via NORAD. Audits of some mining companies have taken place for the first time in 2010. The ZRA needs to receive continued support from the Government and donors, including earmarked funding to ensure that strategic improvements are made in the medium to long term. The Ministry of Mines also needs support—its engineering expertise is vital if Zambia is to audit and control mining policy effectively. There also needs to be a better relationship between the institutions involved—the ZRA and respective ministries for mines and finance—so that policy and resources are managed coherently.

35. The UK government should involve African countries in international processes with regard to tax cooperation.

Much of the current progress on tax cooperation has been pushed through the OECD, of which countries like Zambia are not members. A more equitable solution would be to pursue this agenda through the UN, where every state has an equal voice.

36. The UK government should support international progress towards a country-by-country reporting mechanism of key financial information for all multinational companies.

82 www.actionaid.org.uk/doc-lib/calling_time_on_tax_avoidance.pdf
This would provide both ZRA officials and civil society with the necessary information to monitor whether multinational companies are paying their fair share of tax in countries like Zambia, or if significant profits are being shifted into tax havens.

37. The UK government should support developing countries in their efforts to secure multilateral and bilateral tax information exchange treaties, particularly with tax havens.

38. DfID should assist in building the capacity of civil society to monitor hold government and companies accountable for their tax policies and practices.

February 2012

Written evidence submitted by SABMiller

1. EXECUTIVE SUMMARY

1.1 SABMiller is one of the world’s leading brewers, with more than 200 beer brands and some 70,000 employees in over 75 countries. Our business originated in Africa, where we have been brewing beer for over 115 years. The future of Africa and its economic development matters deeply to us. Our business growth depends on a healthy, growing economic environment in the communities where we operate.

1.2 SABMiller welcomes the Committee’s inquiry and its recognition that tax policy and economic development are closely linked. This submission sets out our recommendations for a better tax environment in order to drive economic growth, support public services and create inclusive development.

1.3 In summary, we encourage DFID to:

1. Promote fair tax systems which provide stability and certainty.
2. Consider tax in the wider context of the total development benefit that business brings to a country, through investment and job creation.
3. Encourage better revenue collection through improving authorities’ capabilities and resources.
4. Simplify tax policies and tax laws to improve investment and revenue collection.
5. Broaden the tax base to encourage legitimate enterprise and increase tax collection by bringing the informal market into the tax net.
6. Promote growth through supporting a common tax framework enabling local businesses to benefit from the global scale and skills of their parent company, which leads to greater local profitability and in turn greater local investment and growth.
7. Recognise legitimate incentives for investment, allowing developing countries to benefit from the range of incentives employed in developed countries to promote business investment.
8. Take care not to dis-incentivise trade through VAT and excise policies and encourage stronger border controls.

2. ABOUT SABMiller

2.1 SABMiller is one of the world’s leading brewers, with more than 200 beer brands and some 70,000 employees in over 75 countries. Our wide portfolio of brands includes premium international beers such as Pilsner Urquell, Peroni Nastro Azzurro, Miller Genuine Draft and Grolsch, as well as leading local brands such as Aguila, Castle, Miller Lite, Snow and Tyskie. We are also one of the world’s largest bottlers of Coca-Cola products.

2.2 SABMiller originated in Africa, where we have been brewing beer for over 115 years. The future of Africa and its economic development matters deeply to us. Beer is a local product: brewed, sold and consumed locally. So for us, a healthy, growing economic environment in the communities where we operate is the key to achieving business success. It is therefore in our interests to invest capital in local economies, to use small enterprises to supply and distribute our products, and to create jobs for local people and develop their skills.

2.3 We pay a significant level of tax and in many countries we are one of the top contributors to government income. See Appendix 1 for a briefing on SABMiller’s taxes paid, with a particular focus on Africa.

2.4 SABMiller has a long-standing history of integrating sustainable development into its core business decisions through our 10 sustainable development priorities. These range from addressing water issues to tackling the HIV/Aids pandemic, particularly acute in Africa. We address these issues across the value chain and not only within the boundaries of our own operations. In addition, we report the performance of each of country against the Ten Priorities, with the results published annually on our website.
3. **Recommendations to the Department for International Development on Tax and Development**

**A fair approach to tax**

3.1 We agree with the IMF that “fair and efficient tax revenue systems are essential to the long-term sustainability of public finances in low-income countries. Effective revenue collection can unlock vital resources for African countries to tackle the root causes of poverty and promote their long-term development in an equitable and transparent manner.”

Tax collection is essential if countries are to break out of the aid trap. The World Bank Group has argued that “tax policy and administration are a key part of a country’s private sector development strategy”. Businesses look for a fair system of taxation that is efficient, that provides stability and certainty. Because we invest for the long term, and our business growth depends on economic development, we have a vested interest in strong public services which support healthy and educated communities.

**Take a broader focus than just tax**

3.2 We recommend that tax is not considered alone but rather in the context of the total development benefit that business brings to a country, namely its wider contribution in terms of jobs created, investments made and therefore the growth that results. Indeed considering tax policy alone, apart from the broader economic context, could lead to policies which result in a lower net benefit for the economy.

**Encouraging better revenue collection through improving authorities’ capabilities and resources**

3.3 We believe that it is critical that revenue authorities are well equipped to understand the tax positions of the companies they are collecting revenue from. We support steps to improve management and administration of taxation in developing countries, including greater investment in both the capability and resourcing of local tax authorities, to ensure that businesses are taxed fairly and in order to optimise revenue collection. DFID should encourage private sector engagement and dialogue with revenue authorities, the African Tax Administration Forum (ATAF) and other similar organisations in order to build capability across revenue departments and to further understand the impact of revenue policies on business. We would support the establishment of a Regional Tax Academy in Africa to provide training for tax officials so as to improve skills and increase knowledge of tax systems, as well as training new candidates.

**Simplifying tax policies and tax laws to improve investment**

3.4 We agree with the World Bank, that in developing countries “tax constitutes a significant barrier to investment. Vague tax provisions, multiple tax instruments, arbitrary implementation of tax laws, limited opportunities for redress of taxpayers’ grievances, and laws that give excessive discretion to tax authorities trouble both investors and deter potential investors.”

Complying with complex tax codes can be a particular burden for small businesses, and discourage entry into the formal economy. When considering tax reforms, donors and governments should consider how a simplified tax system can encourage investment, business growth and revenue collection.

3.5 We support workshops such as those arranged by the International Tax and Investment Center (ITIC), a non-profit organisation whose aim is to bring together government, academics and industry in order to discuss and debate matters such as tax policy.

**Broadening the tax base to encourage legitimate enterprise**

3.6 We encourage DFID and governments in developing countries to partner and engage in discussion with local businesses to broaden the tax base through bringing the informal market into the tax net. We believe there are significant opportunities to increase tax collections through a focus on the large, informal sectors of the economy which currently contribute very little tax.

3.7 We urge DFID to continue promoting reforms in this area. For example, an ICF cross-country study has found that “a 10 percentage point decrease in the effective corporate tax rate is associated with an increase in the total number of registered businesses of two per 100 people of working age”. Building a package of incentives around business registration and tax breaks in the first few years may help small and informal businesses to enter the tax system for the first time. In particular, making it simpler and easier for businesses to register is an important issue. We do, however, recommend that such incentives are applied uniformly and fairly across various industry sectors.

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83 Carlo Cottarelli, IMF Director of Fiscal Affairs, Kenya, March 2011, Conference for Sub-Saharan Africa on Improving Tax Revenue Mobilization


Promoting growth through enabling effective business operations

3.8 We recommend that DFID and developing country governments promote the tax guidance embodied in the OECD Guidelines for Multinational Enterprises. These guidelines provide a helpful framework for developing responsible tax policies across a multinational business such as ours whilst at the same time enabling local businesses to benefit from our global skills and scale.

3.9 For example local businesses which are part of multinationals benefit from high quality centralised corporate services including financial consulting; human resources; corporate communication; marketing support; IT support and data processing. Centralising these services lowers the financial burden for local businesses by cutting administrative costs, enabling local businesses to focus more resource on growth and investment. The treatment of the costs incurred in providing the services should be in accordance with the OECD transfer pricing guidelines.

3.10 The ability of companies to offer brands to new markets outside of their home market is enhanced by using centralised brand holding companies, which make the brand available on a royalty basis to enhance local profitability. This allows for a team of specialist trade-mark experts in one place to manage international rights, rather than duplicating this resource across all markets. On some rare occasions brand rights may be purchased out of their home markets as a mechanism to provide finance for local investment and expansion.

3.11 The outcome of local businesses benefiting from global skills in this way is greater local profitability, which in turn leads to greater investment and growth.

Recognising legitimate incentives for inward investment

3.12 Developed countries provide a whole range of incentives for businesses to invest and provide employment in their markets, including tax allowances for capital investment. We do not think that developing countries should be prevented from doing the same.

Taking care not to dis-incentivise trade

3.13 Exports are commonly zero rated for VAT and excise. This avoids an irrecoverable VAT cost to customers abroad and is therefore important trade facilitation. However, governments have understandable concerns about tax fraud stemming from zero rated export goods being diverted to tax free home consumption. Businesses understand this risk. We typically carry out additional checks on the legitimacy of export customers, not least to ensure that we get paid. Whilst we take care to collect and check proof of export, complying with VAT requirements can prove difficult. The risk of not being able to meet onerous VAT proof requirements can hinder trade where it would add value to regional economies. Stricter border controls are often required in order to reduce smuggling, which of course leads to products entering the market outside of the tax net.

4. SABMiller’s Economic Contribution

4.1 Businesses create significant wealth and SABMiller is a good example. In 2011 SABMiller generated over US$21,072 million of economic value, of which the majority was distributed through the course of our business to our employees, shareholders and investors, suppliers and governments as well as to local communities through our Corporate Social Investment (CSI) activities. We invest heavily in developing markets. In Africa alone (excluding South Africa) in the last four years we have invested over US$1,760 million in acquisitions, new breweries, capacity expansion and malting facilities. As one of the co-founders of Business Action for Africa, SABMiller is committed to assisting poverty alleviation through market-based solutions.

4.2 We directly employ over 13,400 people across Africa (excluding South Africa). However, our businesses also drive employment throughout the value chain. Independent research by Professor Ethan Kapstein of INSEAD has found that the job multiplier (the number of jobs supported in the wider value chain from farmers who supply our barley to the retailers who sell our products) can be significant. For example, in Uganda Professor Kapstein found that every worker that Nile Breweries employs supports another 247 workers in the value chain and the broader economy (a further 90,400 workers).

4.3 Africa contains some 60% of the world’s uncultivated arable land and 70% of Africa’s population still depend on smallholder or subsistence farming. Brewing uses large amounts of agricultural raw materials, such as barley, maize and sorghum; and building inclusive local agricultural value chains is a critical part of SABMiller’s strategy in Africa. We currently directly source agricultural raw materials—barley, sorghum and most recently cassava—from some 20,000 smallholder farmers in Africa and this number increases significantly when farmers we buy from through brokers are taken into account.

4.4 We are the first brewer to produce a commercial-scale beer brewed from cassava. This recently launched in Mozambique, creating new employment and generating incomes for over 1,500 smallholder farmers. This

87 Average monthly number of employees on a full-time equivalent basis, excluding employees of associated and joint venture undertakings and including executive directors.
88 Revised 2011 Nile Breweries Socio-Economic Impact Report.
has the potential to be developed in many other markets around Africa, where cassava is the most widely-grown, but least commercialised crop. We aim to increase our local sourcing of raw materials to 50% of our total requirement in Africa in the next two years. Many of our smallholder farmers have previously been subsistence farmers. By creating market opportunities for subsistence farmers in our value chains, we are able to increase their productivity allowing them to feed their families and generate an income for the first time.

4.5 As our businesses grow, so does our economic—and social—impact. Our work with Professor Ethan Kapstein has helped us understand the broader socio-economic impact of our operations in Africa. For example Professor Kapstein found that our operations in Mozambique generate value-added of US$233m, which is the equivalent of 2.4% of GDP. Studies of this kind have helped us to understand the broader socio-economic impact of our operations in Africa (see Appendix 2).

5. Engaging with Local Authorities

5.1 We are keen to encourage local engagement in our business and most of our African markets have local partners and minority shareholders including governments or their investment agencies, who have expressly endorsed and approved our corporate structures including brand ownership, procurement and management agreements.

We regularly engage with revenue authorities and welcome engagement with regional organisations such as ATAF.

February 2012

Written evidence submitted by Christopher Lenon, Tax and Fiscal Affairs Committee of the Business and Industry Advisory Committee to the OECD

EXECUTIVE SUMMARY

The role of taxation in transforming developing countries in the 21st century is a key challenge. Government, civil society and business are all agreed on this. While transparency is a key enabler for developing country societies to ensure that government revenues are being spent on government services, the core issue to address is building the capacity of tax administrations in developing countries to manage tax policy, administration and collection. Aid budgets should have a key role to play in facilitating this (a role that to date has not been a priority) and donors should specify a target % of the aid budget which should be spent in this way, which significantly exceeds the current 0.7% average (source OECD).

Capacity building for tax administration/revenue institutions is the most important and fundamental infrastructure development for developing countries to move from aid to sustainable revenue to fund government expenditures. The transformation of lives in developing countries will not be achieved without these revenues.

INTRODUCTION

My name is Christopher Lenon, I am Chairman of the Tax and Fiscal affairs Committee of the Business and Industry Advisory Committee to the OECD (BIAC) and have held this role since April 2010. I am the lead business representative on the Tax and Development Taskforce established by the OECD in 2010 and participate in the subgroup on i) State building, Taxation and Aid, ii) Transfer Pricing and iii) Transparency. BIAC is working with OECD to establish a group of business experts in the field of transfer pricing to work within the OECD Capacity Building project for Developing Countries.

Prior to my current role I was Global Head of Tax for Rio Tinto plc based in London from 1993 to 2010. In that role, I managed the tax affairs of one of the largest global Mining companies. My experience of Tax in Developing Countries includes Brazil, Chile, South Africa, Namibia, Zimbabwe, Madagascar, Guinea, Indonesia, Malaysia, Mongolia and Papua New Guinea. I helped to develop the disclosure which Rio Tinto makes of its tax payments which developed from its participation in the Extractive Industries Transparency Initiative (EITI).

Given that the Committee is using Zambia as a case study, I should state that I have no direct experience of Zambia or the mining sector in Zambia. I have made some observations in my evidence from publically available information.

COMMENTS

An important recent advance in the development agenda has been the insight that tax, and a functioning tax system, are understood as perhaps the key factor to support sustainable development rather than Aid. Current estimates indicate that 0.7% of Aid worldwide is spent on developing the capacity of tax administration revenue institutions in developing countries. Business has proposed that a higher target percentage of Aid should be spent in this way by all Aid donors (including the UK government and the EC). Business has an important and positive role to play in this sphere through technical assistance for capacity building, and through investment in developing countries.
Aid flows will continue to play a strong part in addressing these domestic challenges, but aid alone will not bring about the required changes that are needed to boost strong, sustainable and balanced growth in these countries. The required gearshift in development will only happen as a result of also mobilising the foreign and domestic private sectors in order to boost their investment in infrastructure, agriculture, and other economic sectors, and through developing countries reaping the some of the benefits of that growth through functioning tax systems.

The private sector can play an important role in capacity building and domestic resource mobilisation, as it relates to taxation. As a first step, there has to be a predictable and attractive enabling policy framework in place to inspire market confidence and to attract private sector investment which generates tax revenues for countries. This entails: rule of law; clear, predictable and transparent legislative frameworks; open competitive markets for trade and investment; fiscal transparency; human resources development; good governance; anti-corruption; fair competition policy; and so on—issues relating to taxation should be considered in this context as well as the broader policy context. Bringing together both public and private sectors, such as via public-private partnerships and leveraging aid for attracting private investment, will be essential in order to generate the necessary financing for development while reducing risks for investors.

Capacity building for tax administration/revenue institutions is the most important and fundamental infrastructure development for developing countries to move from aid to sustainable revenue to fund government expenditures. By creating an environment which fosters investment (at all levels) it enables countries to benefit from inbound investment, greater economic growth and local economic activity in the country. It is a basis to develop the public infrastructure and services and a social benefit system in a sustainable way. It is an important tool in the eradication of corruption by funding public service salaries on a sustainable basis, and facilitates the transformation from informal to formal economies.

Good governance is a prerequisite for successful capacity building for revenue institutions. Transparency and accountability must apply to governments and business alike. To help facilitate this, aid should be allocated to provide support for the infrastructure which is required to establish and maintain a modern tax administration. Based on UK experience, this includes the hardware and software that a tax administration needs and the training and salaries to staff an effective administration.

Development activities related to tax must include active engagement of developing countries in dialogue towards adoption and continued development of international tax standards by developing countries. Adoption of accepted international tax standards by developing countries will contribute to predictable and more certain investment environments and is an important part of capacity building for tax administrations.

As my comments above indicate, I believe that the link between taxation and development is fundamental, however, the inclusion in the terms of reference of an estimate of $160 billion of annual tax revenues lost by developing countries due to alleged tax avoidance by multinational companies is unhelpful. Business does not recognise this figure and questions have been raised over both the analytical method and data used to arrive at this number, together with the definition of “developing countries”.

I would also question the particular concern with “the extractive industries where payments to governments are often not disclosed and may not contribute to development or poverty reduction”. Many multinationals (61 companies) are signatory to the EITI which was established in 2003 and have provided voluntary reporting of tax and wider economic contributions for a number of years. The International Council for Mining and Metals (ICMM) was established in 2001 to improve sustainable development performance in the mining and metals industry and has 21 mining and metal companies as members. Unfortunately, fewer countries have signed up to the EITI principles (11 countries of which Norway is the only OECD member, although the US and Australia have indicated they will sign. The UK is not a signatory). There are 23 “candidate countries” which include Zambia.

The criteria for full participation are:

1. Regular publication of all material oil, gas and mining payments by companies to governments (“payments”) and all material revenues received by governments from oil, gas and mining companies (“revenues”) to a wide audience in a publicly accessible, comprehensive and comprehensible manner.
2. Where such audits do not already exist, payments and revenues are the subject of a credible, independent audit, applying international auditing standards.
3. Payments and revenues are reconciled by a credible, independent administrator, applying international auditing standards and with publication of the administrator’s opinion regarding that reconciliation including discrepancies, should any be identified.
4. This approach is extended to all companies including state-owned enterprises.
5. Civil society is actively engaged as a participant in the design, monitoring and evaluation of this process and contributes towards public debate.

A public, financially sustainable work plan for all the above is developed by the host government, with assistance from the international financial institutions where required, including measurable targets, a timetable for implementation, and an assessment of potential capacity constraints.

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The EITI is based on “the principle and practice of accountability by government to all citizens for the stewardship of revenue streams and public expenditure”. It is necessary to put in place a sensible assessment of the role of transparency/disclosure in driving development as it relates to international business taxation. Any standards must have a clear development objective, and should work towards one common global standard. The various initiatives for extractive industries should be tested and evaluated before consideration of whether any wider steps are appropriate. Transparency should be considered in the context of how it may contribute more to the integrity, efficiency and effectiveness of tax collection on the part of revenue authorities.

Turning to the Issues Identified

How can DFID better support developing countries to improve revenue collection?

Tax policy must be adapted to the practical challenges of tax collection and administration. These challenges are best understood by Tax Administrations and the two best forms of support which can be provided are a) sharing the experience of HMRC and b) facilitating south-south cooperation between developing country tax administrations. DFID should be the enabler for this programme but HMRC should have the lead role in this programme given its expertise. As stated above, a greater percentage of the Aid budget (and not the HMRC budget) should be spent on this area. Private companies are willing to engage with tax administrations to promote practical improvements in tax collection.

How can DFID support developing countries to use the revenue base responsibly in order to improve service delivery and development outcomes?

The key challenge to the use of the revenue base is transparency in how government revenues are spent. A sub set of this is, of course, the eradication of corruption and in particular the diversion of government revenues for personal gain. The EITI provides for the disclosure of how government revenues are spent and this model of disclosure should be encouraged on a wider basis. Should the UK (and other donors) make aid dependent on the disclosure of how government revenues are spent based on an international standard? Should the UK (and other donors) make aid dependent on countries signing up to the EITI within a specified timeframe?

Tax evasion and Avoidance in Developing countries by private individuals and companies

As I have stated above, the key enabler for a robust tax system in developing countries is a focus on the capacity building for tax administration and collection. The robustness of the tax system can be judged by how effective it is in taxing the country’s elite, the informal economy and companies. The taxation of all of these sectors are important in establishing that the tax system is robust and fair. Capacity building must include training and paying the personnel well and having the right hardware and software to support a modern tax administration.

How effective international efforts to promote tax disclosure and transparency are likely to be?

I have described the EITI in some detail as this is the only operating system of disclosure of taxes. Both the SEC in the US and the European Commission have current proposals for transparency requirements. Business believes that the EITI should be used as the model for disclosure and that more countries should be encouraged to participate. The debate has moved on in the EU and US to whether mandatory rules for disclosure of payments to governments are necessary. A global standard could have advantages in creating a level playing field for the extractive industries. So where such rules are envisaged, we believe governments should work together to adopt a consistent comparable approach, which establishes disclosure requirements and thresholds that are proportionate.

Transparency should be judged in the context of how it may contribute more to the integrity, efficiency and effectiveness of tax collection on the part of revenue authorities. The priority objective should be capacity building for tax administrations and while transparency is important is should be an enabler supporting this objective not an aim in itself.

Capital flight and its implications for developing countries

Capital flight is largely associated with local elites in developing countries. The primary weapons in addressing capital flight are robust exchange of information treaties and procedures between developing countries and low tax jurisdictions. The OECD is working on this through a global forum. This is the right mechanism and future work should focus on increasing the coverage and operational effectiveness of the exchange of information.

Zambia and the Mining Industry

As I have stated above, I have no direct experience of either Zambia or the mining Industry in Zambia. It is worth understanding the history of the industry and what follows quotes from an EITI report.

"From the late 1960s to the early-1990s mining in Zambia was dominated by the State owned Zambia Consolidated Copper Mines (ZCCM). ZCCM was established not only to ensure that the people of Zambia
were the primary drivers of the main revenue earning industry in the country, but also to act as a parastatal organization which provided services significantly beyond that typically delivered by a major mining enterprise. At its height ZCCM provided—in addition to its core operations—hospitals, schools, housing, utilities (electricity and water), and funding for youth groups and sports teams. It was far more than just a company—it was the heart of the social and economic development of the Copperbelt Region.

Copper production has varied immensely over time—from a high of 750,000 tonnes of copper in 1973 to a low of 227,000 tonnes in 2000.

In 2010 a total of 720,000 tonnes of copper was produced. The international price of copper has fluctuated significantly over this period of time.

Under-investment and low copper prices eventually lead to a massive decline in production by the mid 1990s. ZCCM became a loss making enterprise. Against this backdrop, as well as programs of broader economic reform and privatization, ZCCM was broken up and privatized in the late-1990s and early-2000s. At the time copper prices were extremely low, and the mines themselves in need of significant new investment. In order to attract investors the Government of Zambia (GRZ) negotiated a series of mine development agreements with what were (for investors) comparatively attractive levels of taxation, royalties, and conditions for depreciation of capital investment. The GRZ has maintained stakes in virtually all of the mines through ownership of 87% of the shares of ZCCM’s successor company—ZCCM Investment Holdings (ZCCM-IH), which is publicly listed in both Lusaka and London.

The ownership and levels of production of the mines currently producing in Zambia is

- Chambishi Metals: 10% ZCCM-IH
- Chibuluma Mines: 15% ZCCM-IH
- Kansanshi Mines: 20% ZCCM-IH
- Konkola Copper Mines: 49% ZCCM-IH
- Luanshya Copper Mines: 10% ZCCM-IH
- Mopani Copper Mines: 10% ZCCM-IH
- NFC Africa Mining: 15% ZCCM-IH

New foreign investors have shown significantly less interest in taking responsibility for the non-core-business services which ZCCM provided to the population. At the same time the GRZ has in some cases not been able to adequately fill the gap in the provision of social services left by the break-up of ZCCM.

Following significant investment in mines by new owners, as well as a more than quadrupling of copper prices, the Zambian mining industry is now—in terms of both the amount and value of production—booming.

In terms of transparency, ZCCM-IH stated that as a company quoted on the Lusaka and London stock exchanges, it is required to produced annual audited financial statements which are disclosed to numerous institutions (the Companies Registry, the Auditor General, the Securities and Exchange Commission, etc), and thus access to this data was more a question of making the information held by these institutions more accessible, rather than a need to actually disclose the data. Other companies were barred by confidentiality clauses in their development agreements from disclosing the level of payments made to government. Many companies noted that their contracts were with the government, and thus they would only disclose information to the government—not to the general public. Some companies noted that as joint stock companies they would need permission from all of their board members (which in virtually all cases includes the Zambian Government in the form of ZCCM-IH and MMMD) to disclose this kind of information.

The result is increasing pressure on both companies and government to renegotiate the terms under which companies operate so that the people of Zambia are able to benefit from the boom."

Capacity building in tax policy, administration and compliance would be the key priority in addressing these issues.

**Recommendations for Action**

**Aid Funding:** The key priority is to build the capacity of tax administrations in Developing Countries. A higher target percentage of Aid should be spent on developing the capacity of tax administration revenue institutions in Developing Countries by all Aid donors (including the UK government and the EC).

**How to facilitate:** Tax policy must be adapted to the practical challenges of tax collection and administration. These challenges are best understood by Tax Administrations and the two best forms of support which can be provided are a) sharing the experience of HMRC and b) facilitating south-south cooperation between developing country tax administrations. DFID should be the enabler for this programme but HMRC should have the lead role given its expertise. A greater percentage of the Aid budget (and not the HMRC budget) should be spent on this area.
UK government support for EITI: The EITI provides a framework for shared transparency by Governments and Companies which is in place. The UK should support this initiative by:

(a) Participating as a country.
(b) Considering making aid conditional on countries participating in EITI.

Reducing capital flight: The UK should provide active support to the expansion of exchange of information treaties and processes between Developing and low tax jurisdictions to reduce capital flight opportunities.

February 2012

Written evidence submitted by Dr Odd-Helge Fjeldstad, Dr Wilson Prichard and Professor Mick Moore of the International Centre for Tax and Development

1. The International Centre for Taxation and Development (ICTD) is a research consortium set up by DFID for a five year period of research and based at the Institute of Development Studies (IDS). The ICTD is also supported by the Norwegian agency NORAD. The consortium combines technical expertise with concern for aid effectiveness and political economy. It recognises that weak tax systems in low-income and fragile countries are not only the result of poor policy, weak administration or the wrong technical instruments, but of poor governance—weak accountability, corruption, limited responsiveness to extreme inequalities and the needs of the population, and challenged legitimacy of the state. The ICTD’s purpose is to build a stronger evidence base for those seeking to build more effective and legitimate institutions that deliver improved outcomes for poor people.

2. Dr Odd-Helge Fjeldstad is based at the Chr Michelsen Institute, Bergen, Norway, and is Research Director of the International Centre for Tax and Development (ICTD). He has considerable research and consultancy experience on taxation in sub-Saharan Africa, but has been doing intensive research and advisory work for Norad in Mozambique, Tanzania, and Zambia over the past two years. During 2008–09, he served as member of the Norwegian Government’s “Expert Commission of Inquiry into Capital Flight from Developing Countries”. Dr Wilson Prichard is based at the University of Toronto and is also Research Director of ICTD. Professor Mick Moore is CEO of ICTD, a Professorial Fellow at the Institute of Development Studies and former Director of the Centre for the Future State.

3. The British aid programme has in the past played an important role in tax reform in developing countries, especially in sub-Saharan Africa. In the 1990s, ODA/DFID, typically working jointly with the IMF and the World Bank, was responsible for considerable tax reform in Africa. In particular, it supported the creation of Autonomous Revenue Authorities. In recent years, the interest of DFID in taxation issues—and its professional capacity in taxation—declined appreciably. It is only very recently that it has begun again to re-build interest and capacity. Over this period, the global agenda and situation have changed, implying a need to develop a renewed focus on strategic areas of opportunity.

4. An effective British engagement in this field will be inter-departmental, involving in particular the Treasury and HMRC, as well as DFID. Compared to previous decades, global issues and international cooperation should feature more prominently in any future British programme. It is partly for that reason, and to add weight, that the Treasury and HMRC should be fully engaged.

5. In setting priorities, the starting point must be an understanding of the vastly changed context in which tax reform is being pursued, and donor support is being provided. There is now a much wider appreciation of the importance of taxation in development, and many more agencies and governments are active in the field. Unfortunately, this is now associated with frequently unhealthy competition among different aid and development agencies. One can see this at the global level, where there is competition between organisations like the IMF and the OECD for overall leadership in the tax and development field. At the level of individual developing countries, an unhealthy competition for individual aid donors to fund tax agencies, often on a small scale, is growing. This poses serious problems of duplication, wasted effort and fragmentation, with the latter potentially undermining reform efforts by diverting local resources, reducing local ownership and undermining the coherence of reform programs. It is therefore very important that the re-engagement of the British aid programme with taxation issues is planned strategically to minimise the danger that it will exacerbate these existing problems. Rather, one would hope that we will be able to contribute to the resolution of these problems.

6. DFID, Treasury and HMRC should seek to contribute to the resolution of these problems, by seeking to encourage coordination and cooperation and by contributing to identifying strategic opportunities for supporting reform efforts. An important implication of such an approach is that re-engagement should not simply be about earmarking additional resources. The financial requirements for reforming tax agencies are relatively modest. Money should certainly be available when there are serious commitments to reform. But giving more money may not be very helpful unless it is embedded in a broader strategy to strengthen overall donor support in this area.

7. In light of the expansion of donor activity in this area, an important part of DFID, Treasury and HMRC efforts should lie in seeking to support reform in strategic, and comparatively neglected, areas. The relative emphasis in tax administration reform should now shift both upwards, to the international level, and downwards to the sub national level, while increasingly taking account of political economy barriers and the need to
develop local leadership of reform efforts. Considerable progress has been made in national level reforms, and many remaining barriers are related to the need to build political support for reform. There is a set of national level reforms that (a) have to some extent been adopted in developing countries, (b) are widely accepted as being generally appropriate to the conditions of developing countries, and (c) have been widely propagated and are relatively well understood by potential tax reform leaders within developing countries. While there remains significant scope for progress in these areas, continuing challenges are frequently rooted in politics, rather than in the absence of local understanding or funding. DFID, Treasury and HMRC efforts should correspondingly focus particularly on supporting and encouraging local efforts to overcome these barriers, while offering specific support where opportunities for progress emerge.

8. An important opportunity for building political support for reform lies in putting more emphasis on the “demand side”, ie in building broader citizen engagement around taxation. Public debates on taxation in Africa are mainly limited to taxation of multinational companies. While this is important, a broader engagement about the whole tax system is missing. This is also reflected in Parliamentary debates on taxation. In some countries DFID supports some civil society organisations engaged on tax issues. DFID also provides some technical assistance to building tax capacity/knowledge in the business community, especially small and medium enterprises. There are opportunities to expand this type of engagement.

9. In contrast with important progress at the national level, sub-national taxation has been relatively neglected and requires further attention, as the IMF acknowledged in its March 2011 revised policy statement on revenue issues in developing countries. Despite significant moves towards decentralisation across the developing world, fiscal decentralisation has been limited and not very successful. This effectively reduces the decision-making power and autonomy of local governments. It also potentially undermines many of the expected governance benefits of decentralisation, which are significantly premised on fostering bargaining around revenue and budgeting between citizens and government. Tax reform at the sub-national level has been held back by a combination of political constraints, capacity constraints and poor coordination between national and sub-national authorities. However, there is emerging evidence that even relatively small investments can yield significant revenue gains, with potential governance benefits as well.

10. Equally importantly, it is now widely accepted that there is considerable scope to address the international dimensions of weak tax systems in developing countries. There are opportunities to increase international cooperation among tax agencies and to change the accounting rules for transnational business, in order to reduce the degree of tax evasion that takes place to the cost of developing countries. This is particularly evident in resource rich countries in Africa. Challenges with respect to extractive industries have been exposed. The problems are also serious in renewable sectors such as fisheries, forestry and wildlife, though these have received little attention.

11. Alongside specific reform priorities, there remains a substantial need to build specialised expertise in national tax administrations. The basics are often in place, but expertise to do in depth tax audits in complex sectors such as extractive industries, banking/financial sector, tourism and telecoms is often absent. One consequence is that African tax administrations are often easy matches for multinational companies that can afford to engage the best and most skilled tax lawyers and accountants.

12. Finally, some of the larger emerging economies are beginning to play a significant role in international negotiations and discussions over taxation issues. This includes in particular South Africa and, more recently, India. In addition, regional organisations of tax professionals are increasingly prominent at the global level. CIAT (Inter American Centre of Tax Administration), the long established Latin American regional organisation for tax specialists, increasingly operates globally. Africa has a new organisation, the African Tax Administration Forum, funded in part by DFID, which represents Anglophone, Francophone, and Arabic speaking Africa. It is important that these organisations and countries from “the South” are accepted as full partners in any new British initiatives in the field.

6 February 2012

Written evidence submitted by the Department for International Development

INTRODUCTION

1. The tax system is at the heart of an effective state. Domestic tax revenues provide sustainable funding for essential public services and transfer payments. Funding requirements for reducing poverty and improving physical and social infrastructure are substantial. But how taxes are raised, not just how much is raised or how it is spent matters greatly for reducing poverty, promoting growth, and improving governance. Taxes shape economic growth by altering the incentives for work, investment, saving and innovation. Taxation is a core part of state-building and the most visible sign of the social contract or “fiscal compact” between citizens and the state. Fair and transparent tax collection promotes social cohesion and shapes government legitimacy by promoting accountability of governments to tax-paying citizens, and by stimulating effective state administration and good public financial management.

2. Good tax systems strive to be economically efficient (raising revenue while creating optimal incentives in favour of “goods” such as work and investment and against “bads” such as pollution); effective (capable of...
delivering the desired objectives at minimum administrative and compliance cost); and equitable (offering fair treatment of taxpayers and promoting social cohesion). These objectives may not always align (for example consumption taxes may be economically efficient but regressive in their incidence). Tax revenue can be increased by broadening the tax base, increasing taxable activities (ie economic growth), improving compliance (ie improving enrolment and collection as well as reducing evasion and avoidance), or raising rates; although high rates can also dampen growth and reduce the incentives for compliance.

3. In many developing countries tax collection is low as a percentage of GDP, as a percentage of tax owed and in terms of participation rates. The tax base is often overly narrow, for example many developing countries have large informal economies, and property taxes are rare. Tax administrations may be ineffective, coercive or susceptible to corruption, while governments may undermine their own tax base with inappropriate exemptions and concessions. Oversight by parliaments, national audit bodies and other institutions may be weak or absent. Taxpayers may have limited rights of redress or the courts may be incapable of fair and effective dispute resolution. “Tax morale” may be low: if citizens think taxation is excessive or revenue will be lost to corruption they will be less likely to pay; small firms could move into or remain in the informal sector, which carries its own costs. Poorly designed policies and systems may deter investment, innovation and employment and impede the economic growth that is ultimately the most important driver of sustainable revenue flows.

4. The extraction of natural resources poses specific challenges for taxation and public financial management. These challenges can be particularly serious for countries which are poor despite abundant natural resources. Countries with natural resource wealth are likely to need to promote investment in what is a highly capital-intensive sector but at the same to be able to capture the economic rents generated, which, when managed properly, has the potential to transform the public finances, the economy and the lives of the poor. In extreme cases, however, where the revenues from natural resources are particularly large and badly managed, the fiscal compact between government and citizens can be undermined to the extent that a “rentier state” develops (for example Libya under Gaddafi). In such cases, political elites, having captured the resource rents, neglect the wider tax system and consolidate power through patronage and repression. Citizens come to see the state as at best a source of meagre handouts rather than a provider of public services funded by taxation.

5. Sustainable economic growth driving rising tax revenues is the eventual exit strategy from aid dependency for developing countries. Tax is central to the “Monterrey Consensus” agreed in 2002 and reaffirmed in 2008, by which developing countries committed themselves to deliver “effective, efficient, transparent and accountable” taxation systems, in return for increased international development assistance. Most recently, the Busan High Level Forum (2011) reiterated the commitment to domestic resource mobilisation, and revenue falls within one of the five Peace-building and State-building Goals of the New Deal for Engagement in Fragile States, endorsed in Busan. The G20 Development Working Group, and the Organisation for Economic Cooperation and Development (OECD), in particular through the Task Force on Tax and Development, have also held extensive discussions recently on taxation and domestic resource mobilisation in developing countries.

Question 1: How DFID can better support developing countries to improve revenue collection

6. DFID helps to improve revenue collection in developing countries through demand-led assistance projects at the country level, which may focus specifically on strengthening the revenue collection function, or may have broader objectives. Country level work is complemented by engagement in international processes and support for international organisations and for research.

7. Between 2006–07 and 2010–11, DFID spent approximately £ 97 million on helping to improve revenue collection. Annex A provides information on this spending. Annex B gives an overview of DFID’s main current or recent tax related projects, which range from large complex programmes down to very short, targeted interventions.

8. For example, in Burundi, through a regional programme, DFID helped to establish an independent Revenue Authority in July 2010, at a time when the country’s tax and customs services (then under the Ministry of Finance) topped the list of East Africa’s most corrupt organisations in Transparency International’s East African Bribery Index. The programme set out to transform the culture of tax collection. From January to June 2011, revenue collection was 37.4% above the level for the same period the previous year. From July to September 2011 the outturn revenue exceeded the forecast by 14 percent (or £7 million).

9. DFID support to the Rwanda Revenue Authority helped to provide the laws and regulations under which the authority was established, the office building and the management systems. The 10 year period of support saw a six-fold increase in the taxes collected and in 2010, the management procedures of the authority were awarded ISO 9001 2008 accreditation—the first Rwandan institution to attain this standard. The Authority reached a point where it was collecting the full £24 million value of DFID’s support programme every three weeks. Its effectiveness has been a major factor in Rwanda’s impressive development performance in recent years.

89 See for example Part 2 of 2010 OECD African Economic Outlook, entitled “Public Resource Mobilisation and Aid in Africa”.
10. DFID has provided support for tax reform in Afghanistan, where domestic revenue collection reached a high of 11.2% of GDP in 2010–11. DFID is continuing to provide technical assistance to assist the Afghanistan Revenue Department to increase revenue collection from 2011 to 2015.

11. In Ethiopia, DFID, alongside other donors, supports the Public Sector Capacity Building Programme which includes capacity building support to the tax system. An objective is to increase tax revenue by 87% from 43.3 billion birr in 2010 to 81.1 billion birr in 2013.90

12. In Nigeria, DFID is supporting the “Growth and Employment in States” (GEMS) project which runs from 2010 to 2015. This focuses on the value chain and business environment, as well as land reform and investment policy, and includes an estimated £9 million related to taxation.

13. In Zambia, DFID has extended its support to the multi-donor Public Expenditure Management and Financial Accountability program, providing an additional £2.2 million from 2011 to 2013. The programme extension includes a component to strengthen tax administration at the Zambia Revenue Authority, with the objective of reversing the recent decline in the non-mining tax to GDP ratio.

14. Projects reflect individual country circumstances, including the extent to which needs may already be met by other donors and international organisations. Coordination of donor support is important. Country ownership and political support are critical to success. Support for revenue collection may be part of broader public finance management or public sector capacity building programmes. DFID often works in partnership with international organisations and other donors, as is the case, for example, in Mozambique and Tanzania, or coordinates with their efforts. For example in Bangladesh the DFID funded Tax Administration Compliance and Taxpayer Services programme is being implemented at the same time as a major reform of tax policy supported by the International Monetary Fund (IMF), which includes an overhaul and updating of income tax and VAT legislation.

15. HM Revenue and Customs (HMRC) also supports projects to enhance the capacity of tax administrations in developing countries, delivering assistance on a bilateral basis and through multilateral forums, either working with DFID or independently. Bilateral initiatives include a long-term partnership with the Ethiopian Revenue and Customs Authority. Under this twinning programme, HMRC provides technical assistance, aligned to the strategic needs of the Ethiopian Government, on both customs and tax. HMRC also has an ongoing senior-level relationship with Rwanda Revenue Authority; the Permanent Secretary mentors the Commissioner General and HMRC is delivering targeted technical assistance to support Rwanda’s modernisation programme. Each year, HMRC hosts and runs two flagship training courses on behalf of the Commonwealth Association of Tax Administrators. The courses are designed to develop management capability and technical skills and are attended by senior managers and tax inspectors, primarily from developing countries in the Commonwealth. To promote the sharing of best practice and encourage skills transfer HMRC regularly welcomes visiting delegations from developing countries and also supports inward and outward secondments of specialist staff.

16. The recently established Investment Facility to Utilise UK Specialist Expertise (iFUSE) facility is a further route through which HMRC expertise can be provided to partner countries for short technical assistance projects. iFUSE became operational in January 2012. It is a platform which will facilitate the provision of support by experienced policy practitioners from UK Government Departments to their counterparts in developing countries.

17. The IMF is an important provider of technical assistance on revenue. HMRC supports the IMF’s outreach work with developing countries through the delivery of targeted technical assistance. DFID contributes funding to three of the IMF regional technical assistance centres. These centres provide technical assistance on tax as well as other financial and economic management issues to countries in the regions which they cover.

18. The Investment Climate Facility for Africa,91 which the UK funds alongside a number of other donors, is an important source of technical assistance, with tax and customs reform established as one of its main priorities. DFID is also providing support to the World Bank Group’s Foreign Investment Advisory Service (FIAS), which works to strengthen the business environment in developing countries. This involves helping developing countries to remove tax barriers to growth and investment and to widen the tax base through greater inclusion. During 2008 to 2011, FIAS has made a contribution to 49 reforms of business taxation systems in countries around the world (of which 34 where in Sub-Saharan Africa).

19. UK support in the area of taxation and domestic revenue mobilisation is not confined to capacity-building at the country level. An important part of our approach is improving the enabling environment for developing countries in the area of taxation, including through international initiatives, networking and research. In this way, the UK can exert influence and achieve impact beyond what could be achieved by working at the country level alone. The UK has actively participated in discussions on taxation and domestic resource mobilisation in an increasing number of international forums, including the G20, which are key in areas where progress is determined at an international level.

90 Ethiopia’s high inflation rate will considerably erode the actual value of this increase.
91 http://www.icfafrica.org/
20. The UK has been involved with the African Tax Administrators’ Forum (ATAF)\(^{92}\) since its inception and DFID is one of its largest single donors. ATAF is becoming increasingly effective on behalf of its member tax authorities, representing them on the international stage, engaging with donors, coordinating technical assistance and fostering peer-to-peer learning between members. HMRC has also supported ATAF through in-depth assistance in the field of transfer pricing to member countries.

21. DFID has funded the International Tax Dialogue\(^{93}\), a forum for tax and development specialists, in particular to work with ATAF on a project comparing key aspects of revenue administrations in 15 revenue authorities in Sub-Saharan Africa.

22. UK has also been involved in the OECD Tax and Development Task Force\(^{94}\) since its inception. DFID part-funds the Task Force in which it is an active participant alongside HM Treasury and HMRC. The Task Force is an unusual forum in that it is composed of representatives of donor countries, developing countries, business and Non-Governmental Organisations (NGOs) who together discuss ways to make progress on a range of important tax-related issues: the four pillars of its work are tax and state-building, tax transparency and exchange of tax information, transfer pricing and corporate reporting. Most recently the Task Force has agreed to look at how best to promote transparency around the granting and management of tax incentives, such as tax holidays, which can undermine the revenue base. This is a key emerging issue for developing countries.

23. HMRC is an active participant in the OECD work-streams and outreach training programmes, which support developing countries. HMRC is leading a project involving Uganda, Nigeria and South Africa on improving the efficiency of transfer pricing audits.

24. The G20 is the most recent forum to become involved in tax and development issues. There are two strands to this—firstly around tax transparency and exchange of information, where the UK has consistently sought to keep the interests of developing countries in focus in the remit given by the G20 to the Global Forum on Transparency and Exchange of Information. Secondly and more recently, domestic resource mobilisation was included as part of the G20 Development Action Plan. This work was itself in two parts, the first on general capacity building issues and the second on tax transparency and exchange of information, both of which are reflected in the commitments made in the Cannes G20 summit communiqué and the separate report to the summit from the Development Working Group. DFID was involved in both parts of this work through the Development Working Group and, in the latter through participation in the Advisory Panel to the Global Forum on Tax Transparency. DFID was the only development ministry on the Panel.

25. DFID has a strong commitment to commissioning world class research and ensuring that it is readily available to those who can use it. DFID also aims to use the best evidence, from any source, in its own decisions, and to evaluate programmes in order to learn lessons. DFID is providing £3.5 million funding for a five-year research programme consortium; The International Centre for Taxation and Development. This programme was commissioned to provide evidence on how best to strengthen taxation reform in developing countries. Previous DFID-funded, and other, research showed that better evidence was required to find the best ways to promote the effective, efficient and equitable tax systems needed to deliver development in developing—particularly low-income and fragile—states. Research outputs have the potential to exert significant influence on tax reform undertaken by developing country governments as well as on capacity building and technical assistance projects undertaken by DFID and other development agencies.

26. Ultimately, tax revenue is heavily dependent on the economy. Economic growth is a major factor in increasing tax revenue. The UK supports countries to achieve sustainable and inclusive economic growth through its bilateral country programmes, regional programmes, and by influencing both the multilateral organisations which it supports and the wider international community. This work includes helping to improve countries’ economic policies, improving countries’ openness to trade, promoting private sector development, improving the business environment, improving access to financial services, enhancing infrastructure, helping value and manage natural assets, reducing inequality of economic opportunity and supporting low carbon and climate resilient investment. For example DFID funds the International Growth Centre which provides independent growth policy advice to senior policy makers in developing countries.

**Question 2: How DFID can support developing countries to use the revenue base responsibly in order to improve service delivery and development outcomes**

27. Governments use their revenues to deliver services and development outcomes through their Public Financial Management (PFM) systems—the systems through which revenue is raised and funds are allocated and spent. These systems, which should ensure fiscal discipline, strategic allocation of resources and value for money in service delivery, are weak in many developing countries. Improving them can lead to better service delivery and development outcomes.

28. Aid is only a part of total government spending in DFID partner countries, and in some of these countries only a small part. Spending aid well is important, but improving PFM can lead to better use of all funds, not just aid. DFID expects its partner governments to be committed to improving PFM.

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\(^{92}\) http://www.ataftax.net/

\(^{93}\) http://www.itdweb.org/Pages/Home.aspx

\(^{94}\) http://www.oecd.org/document/0,3746,en_2649_34565_45958051_1_1_1_1,00.html
29. DFID helps to improve PFM in developing countries by providing technical assistance to partner countries, through dialogue and through international initiatives. DFID is helping to improve PFM systems in many of its partner countries. For example: DFID funded the UK National Audit Office (NAO) to assist the State Audit of Vietnam to turn its Strategic Plan into a more detailed Development Action Plan. The Plan was approved and implementation started in early 2011. With the United Nations Development Programme (UNDP) and the European Union (EU), DFID is supporting the Supreme Audit Institution of the Democratic Republic of Congo. In 2010, audit reports for 2005, 2006 and 2007 were produced. Anti-corruption Non-Government Organisations (NGOs) have started to use audit reports and demand more control over public spending. From 2007 to 2009, DFID supported the Ghanaian Public Accounts Committee (PAC), including through training the media and providing finance for public sittings. Broadcasting hearings on radio and TV got people talking about corruption and the standard of questions and answers improved.

30. The coalition government has given particular emphasis to achieving results and value for money and to improving transparency and accountability. This is reflected in changes in our approach to budget support. The commitments we expect of our partner governments now include improving accountability to their citizens. Where we provide budget support, we expect this commitment to include a credible programme to improve the Supreme Audit Institution and related parliamentary oversight.

31. Ensuring people have access to information on government spending and are able to make their voices heard can be a powerful way of improving resource use. In Uganda, communities using scorecards to feedback on their experience of health services had 33% fewer child deaths. In India, social audits and public meetings have driven down corruption in the rural employment guarantee scheme. DFID is committed to expanding people’s choice and helping to empower them to hold their governments to account. DFID will help citizens monitor government services using citizen report cards in Mozambique and Rwanda. In Bosnia, DFID supported civil society organisations to analyse the national budget and advocate for more transparent reporting. DFID is exploring how new technologies can help people monitor service provision and drive up performance through programmes in India and Tanzania.

32. DFID’s strengthened approach to budget support includes a commitment to spend, across budget support countries, an amount equivalent to 5% of budget support on strengthening domestic accountability institutions. We have increased citizen engagement in budget support dialogue in a number of our budget support countries. In Sierra Leone, DFID is supporting civil society to scrutinise the government budget and communicate and disseminate findings to the wider public.

33. DFID is also introducing innovations to the design of budget support programmes, to give more emphasis to results and reforms. Arrangements whereby a part of budget support funds is contingent on results achieved have been introduced or are planned for a number of countries, such as Uganda where this will apply to 30% of DFID budget support in 2012/3.

34. Our work at the country level is complemented by support for international initiatives. These include the Public Expenditure and Financial Accountability (PEFA) programme; a joint venture between three multilateral and four bilateral development agencies. A PFM performance measurement framework has been developed and has now been applied in over 120 countries. It provides an objective basis for assessing standards of PFM and, as countries carry out repeat assessments, for monitoring progress. Individual country assessments help to determine priorities for reform, whilst, collectively, the assessments provide an evidence base for research.

35. Supreme Audit Institutions (SAIs) help to hold governments to account for use of public funds. Where they are effective, their work is likely to deter fraud and corruption and may be a catalyst for system improvements. The International Organisation of Supreme Audit Institutions (INTOSAI) is an independent, worldwide body, to which the vast majority of SAIs belong. It provides a structure through which more can be achieved than just by working with individual SAIs. The World Bank and DFID are Chair and Vice Chair respectively for the donor group in a partnership with INTOSAI, established in 2009. Work is already underway on a databank of support to SAIs, a pooled funding mechanism and a tool for assessing SAI performance.

36. At the fourth High Level Forum on Aid Effectiveness in Busan in November 2011, the UK Government pushed for a stronger focus on results and transparency. This is reflected in the outcomes which include new shared principles on (a) the need to focus efforts internationally on achieving results, and (b) the importance of transparency as a basis for enhanced accountability—including an agreement to focus on establishing transparent public financial management and aid information management systems. This should help to ensure a focus on the effectiveness of institutions and policies that promote development, and not just on aid.

37. By working at the country and the international level, in partnership with others, DFID is helping to improve PFM, including the way funds are raised and spent. Evidence from PEFA assessments indicates a broadly positive trajectory of change.

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95 Bjorkmann and Svensson 2007
96 Singh and Vutukuru 2010
97 12 of DFID’s 27 priority countries have two or more comparable PEFA assessments, enabling changes in PFM performance to be tracked. For 11 of these countries more PEFA indicator scores improved than worsened between assessments and for 1 country, more worsened. Two countries have three comparable assessments. One showed continuous net improvement. The other showed improvement between the first two assessments and then worsened slightly.
Question 3: Tax evasion and avoidance in developing countries by private individuals and companies

38. Improving compliance requires not only tackling deliberate evasion and avoidance but also ensuring that taxpayers find the process straightforward and are convinced that their taxes are well spent (ie “tax morale” is high). Authorities need to help those willing to pay their taxes as well as making it difficult for those that want to escape their liabilities.

39. “Tax gaps”—the difference between the theoretical tax take given 100% compliance and the actual tax take—are notoriously difficult to estimate accurately. Where OECD countries have undertaken this exercise they have found it challenging despite the availability of some high-quality data. Estimates for developing countries of tax gaps and “illicit flows” (which include losses to evasion) have proved particularly controversial and face considerable data and methodological challenges. A report commissioned by DFID concluded that most such estimates are not reliable. Nevertheless, the fact remains that just as tax authorities will struggle where tax morale is low, those that lack capacity and technical skills, or which operate with legislation that is inadequate, will be especially vulnerable to evasion and avoidance.

40. Once tax policy has been determined, compliance is ultimately the core function of any revenue authority. Capacity building projects supported by DFID include a range of interventions that are directly or indirectly related to compliance, evasion and avoidance. For example, the large taxpayer units, which DFID funded projects have supported (in Bangladesh, Mozambique, Sierra Leone and Tanzania, for example) are designed to be centres of expertise for dealing with large organisations efficiently and effectively. In other cases DFID is supporting the improvement of tax legislation (for example Afghanistan) or strengthening audit (for example in Rwanda).

41. The taxation of companies and individuals with operations or assets in multiple jurisdictions poses particular challenges for revenue authorities. The network of tax authorities willing and able to exchange tax information to allow the proper assessment of tax liabilities was quite limited until relatively recently. The request by the G20 for the Global Forum on Tax Transparency and Exchange of Information for Tax Purposes to redouble its efforts in this regard has seen a huge increase in the number of tax information exchange agreements, although as yet relatively few involve developing countries.

42. The UK has consistently sought to keep the interests of developing countries in focus through the G20-Global Forum process and encourages developing countries to consider joining the Global Forum. DFID, HM Treasury and HMRC have been directly involved in promoting tax information exchange in three further, important ways. First, as discussed under question 1, DFID was part of the Advisory Panel to the Global Forum which took forward work on Part II of the Domestic Resource Mobilisation pillar of the Seoul Development Action Plan. The report prepared by the Panel was adopted by the Global Forum and was the key input to the Development Working Group discussions on this topic and the commitments made by the G20 in this area are now being taken forward by the Global Forum, including, for example, establishing a platform to coordinate technical assistance on exchange of information.

43. Secondly, DFID has recently provided funding for the Global Forum secretariat to provide technical assistance to the revenue authorities of Kenya and Ghana to enable them to participate fully in international tax information exchange. The UK is the first donor to support a specific technical assistance project in this field, the aim being that it should act as a “pathfinder” for developing countries and donors alike.

44. Thirdly, in addition to bilateral tax information exchange treaties, the Convention on Mutual Administrative Assistance in Tax Matters now offers a means for multilateral information exchange (ie by becoming a party to the Convention, a country has a treaty basis for information exchange with all other parties) as well as other forms of cooperation. One of the Government’s first acts on coming into office was to sign up to a new Protocol that brought the Convention into line with international tax information exchange standards and opened it up beyond OECD and Council of Europe countries to a potentially worldwide membership. The Coordinating Body of signatories to the Convention, which oversees invitations to join, has, with encouragement from the UK, stated that it would welcome expressions of interest from developing countries. The UK also pressed for all G20 members who had not already done so to sign up to the Convention, which they did at the Cannes G20 Summit.

45. Transfer pricing has become the focus of considerable attention in recent years in the context of the taxation of multinational enterprises. Incorrect transfer pricing can shift profits from high-tax to low-tax jurisdictions and abuse of transfer pricing is regarded by some as being the single largest contributor to cross-border tax evasion. Transfer pricing is, however, often a matter of judgement, with alternative views of the correct price of individual transactions.

98 In this discussion evasion is taken to refer to deliberate, illegal non-compliance (and so would include non-payment of taxes because it is assumed they will be embezzled or misused as well as practices more commonly thought of as evasion) whereas avoidance involves the exploitation of unintended loopholes in regulations. Incorrect transfer pricing is the mispricing of intra-group transactions.
100 http://www.oecd.org/dataoecd/52/35/48981620.pdf
101 Action 2: Support work to prevent erosion of domestic tax revenues. We ask the Global Forum to enhance its work to counter the erosion of developing countries’ tax bases and, in particular, to highlight in its report the relationship between the work on non-cooperative jurisdictions and development.”
46. The term “transfer pricing abuse” is often used incorrectly to encompass all manner of international tax avoidance structures or devices. It is important to realise that improving the ability of revenue authorities to deal with transfer pricing will not address all problems of losses through such structures. Measures to address developing country needs related to transfer pricing should be planned as part of the countries’ wider capacity building and reform efforts, including more general anti-avoidance work. Appropriate prioritisation and sequencing is required to ensure that work on essential but less high-profile issues is not displaced.

47. Within DFID programs, work on transfer pricing and related compliance functions may be part of Large Taxpayer Unit projects, as for example is the case in Bangladesh. In addition, the OECD Tax and Development "ix Force (see response to Question 1) has taken transfer pricing, and in particular the needs of developing countries wishing to improve their capabilities in this area, as one of its four workstreams. From this has come a recent project by the OECD to provide technical assistance on transfer pricing to Kenya and Ghana (separate from but designed to work in conjunction with the Exchange of Information project that DFID is supporting directly for Kenya and Ghana). In addition, a number of instances of technical assistance provided by HMRC have related to transfer pricing. Transfer pricing is also the subject of a small but increasing flow of requests to AFRITACs and FIAS also provides technical assistance in this area.

Question 4: How effective international efforts to promote tax disclosure and transparency are likely to be

48. The work of the Global Forum on Tax Transparency and Exchange of Information at the behest of the G20 has proved very effective at promoting revenue authority to revenue authority disclosure of tax information. The Government believes that this approach, when coupled with appropriate domestic powers to request information, is the most efficient and effective means of enabling tax authorities to obtain the information they need to ensure they can collect the revenue they are owed.

49. The number of Global Forum member countries and the network of tax information exchange agreements has been increasing rapidly and this looks set to continue. An important catalyst in this was the listing process, which the UK supported and which was encouraged by the G20 as part of its work on "non-cooperative jurisdictions”. This publicly identified jurisdictions that did not meet the international standard. It was undoubtedly the driving force for a significant change of stance from a number of important financial centres, which engaged with the Global Forum for the first time and agreed to adopt international standards on exchange of information. Although the standard set for reaching the “white-list” was relatively modest, the Global Forum is now carrying out an extensive programme of rigorous peer reviews of countries’ implementation and effective operation of tax information exchange. All review reports are available online102 and remedial action has by and large been promptly taken in response to deficiencies identified.

50. Critics of the current system, which is largely based on information exchange on demand via bilateral treaties, argue that multilateral instruments are superior and that automatic exchange of all tax information between all jurisdictions should be the ultimate goal. As noted above, the Convention on Mutual Administrative Assistance in Tax Matters now offers multilateral information exchange for the first time. As regards automatic information exchange, the EU Savings Directive requires automatic exchange of information between tax authorities in participating countries on bank account interest. The Convention however also provides a treaty basis for bilateral automatic exchange of information between signatories should both parties agree to this.

51. Companies and individuals have an important role to play, as was recognised in the report to the Cannes G20 summit by the Development Working Group, which urged multinational companies to “improve transparency and full compliance with applicable tax laws”. The UK was also involved in the 2011 updating of the OECD Guidelines for Multinational Enterprises, which state that “It is important that enterprises contribute to the public finances of host countries by making timely payment of their tax liabilities. In particular, enterprises should comply with both the letter and spirit of the tax laws and regulations of the countries in which they operate.” This approach was inspired by HMRC’s Banking Code of Conduct for Tax.

52. The model underlying the work of the Global Forum is essentially intergovernmental in nature offering peer-to-peer exchange of information—it between tax authorities. It enables them to obtain detailed and otherwise confidential information about persons of interest—if authority A makes a request to authority B, authority A can in effect benefit from all of the powers of information request and inquiry that authority B has at its disposal, but it must in turn respect confidentiality: this information is not released into the public domain.

53. A well-established model including public disclosure of tax payments (as well as other extractives revenue streams, such as royalty payments) is the EITI, the Extractive Industries Transparency Initiative. The EITI aims to promote accountability for natural resource revenues rather than compliance with tax laws per se. The vast “rents” that are generated in the extractive industries (essentially the difference between the market price for a scarce commodity such as oil and the cost of production) and which largely flow to the government (assuming suitable arrangements are in place) have been seen all too frequently to have a corrosive effect on governance and to feed corruption. Under EITI, extractive industry companies disclose the revenue payments that they make to government in an implementing country, and government discloses the amounts that it has received from companies and there is a reconciliation process to highlight any discrepancies.

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102 http://www.oecd.org/document/23/0,3746,en_21571361_43854757_46969623_1_1_1_1,00.html
54. The results of EITI include building trust and dialogue between different stakeholders, improving financial reporting, empowering civil society to hold governments to account and improving the operating environment for private investors.103 An independent evaluation of the EITI in 2011104 found that it had rapidly demonstrated tangible results in the form of financial reconciliation reports and viable tripartite governance institutions and had led to demand and delivery of transparency and information-based and participatory debate. It recommended that it should consider a Standard that covers a greater part of the value chain and develop further its national and global results framework. These issues are being addressed through the EITI Board’s Strategy Working Group.

55. DFID has provided initial funding to the Natural Resources Charter, which is a wider initiative that aims to improve the management of all parts of the natural resources value chain, from exploration through to the spending of revenues.

56. CoST, the Construction Sector Transparency Initiative, though in detail somewhat different from EITI is also based on the multi-stakeholder model. It is not concerned with the disclosure of tax or other revenues but rather is designed to promote transparency in all stages of the procurement and construction process so as to deliver better value for money, minimise cost overruns and tackle corruption. It is therefore an important initiative as regards ensuring taxpayers money is well-spent. The CoST pilot was funded by DFID and the UK is one of the countries implementing CoST.

57. In addition to its support for EITI, the UK government has expressed its support for regulations at the EU level for mandatory disclosure of payments to governments by extractive industry companies via changes to the Accounting and Transparency Directives. These proposals, currently under discussion in the European Council, seek to replicate, for application across all EU Member States in equal measure, similar measures to those in section 1504 of the Dodd-Frank Act in the US. They aim to complement and reinforce EITI and are, like EITI, aimed at promoting accountability for revenue. The UK government has sought to encourage resource-rich countries to implement EITI and other jurisdictions to introduce mandatory disclosure requirements for companies listed on their stock exchanges.

58. Country-by-country reporting, which is vigorously promoted by some NGOs in the UK and elsewhere, is different again. It is intended to apply to all multinational enterprises (not just those in the extractives sector) and would require a much wider array of data to be disclosed than simply the amounts of tax and related revenue streams, broken down by country of operation. The stated objective of this disclosure model is to allow outside parties to judge whether multinational enterprises are paying the right amount of tax in the countries where they operate—so it is aimed at tax compliance rather than focusing on accountability for revenue, as is the case for EITI and Dodd-Frank-style rules.

59. Country-by-country reporting has been discussed extensively in one of the subgroups of the OECD Tax and Development Task Force (ie in a group involving NGOs, business, donors and tax specialists) but the Task Force process has not yet concluded. More broadly, however, there is no international consensus as to whether country-by-reporting can achieve its stated aims and it is not currently a matter highlighted by developing countries themselves. Companies are also concerned about the potential compliance costs. Country-by-country reporting is also promoted as the reporting model that would be required if the current global tax system were replaced with a system of “global formulary apportionment”105 and can perhaps be more readily understood in that context.

Question 5: Capital Flight and its implications for developing countries

60. While there is no commonly agreed definition of capital flight in economic theory, work by the Overseas Development Institute, funded by DFID, defined capital flight as that part of outflow capital which is motivated by economic and political uncertainty. Alternatively, the OECD defines capital flight as “the transfer of assets denominated in a national currency into assets denominated in a foreign currency, either at home or abroad, in ways that are not part of normal transactions”.

61. Capital flight can be the result of inaccurate transfer pricing, resulting in the movement of funds intra-group across borders. Capital flight can also be the result of money laundering of the proceeds of illegal activities, including tax evasion, where this laundering process crosses borders (though it is debatable how much of the proceeds of, for example the illegal drug trade, would constitute part of the normal capital stock of a country). Capital flight can also be a “rational portfolio choice” as Paul Collier of Oxford University has described it, where holders of capital choose to move their funds elsewhere for fear of seeing them seized, devalued by currency fluctuations or inflation, or simply because of a lack of investment opportunities in the country.

62. Ways to reduce capital flight from developing countries can include reducing the scope for cross-border tax evasion; tackling criminal activities, and in particular taking action against money laundering; and improving the political and economic variables that constitute the investment climate.

103 EITI Impact in Africa report 2010.
105 Global formulary apportionment would allocate the taxable profits of a multinational group among the component enterprises in different countries on the basis of a predetermined formula, for example based on a combination of costs, assets, payroll, and sales.
63. Improving tax compliance and reducing tax evasion and avoidance are discussed in the responses to earlier questions. As regards tackling money laundering, DFID has supported a number of interventions in this area, for example providing funding to the Eastern and Southern African Anti-Money Laundering Group and the Inter-Government Action Group against Money Laundering in West Africa (Financial Action Task Force (FATF) style regional bodies) as well as specific country programmes in Nigeria and elsewhere. In terms of tax and money laundering specifically, the UK has also consistently advocated that FATF should, in its current review of its Recommendations, specify that tax offences should count as predicate crimes for money laundering (this would mean that moving the proceeds of tax evasion through the financial system would also count as money laundering, as it already does in the UK, which has an “all-crimes” definition of predicate offences). DFID seeks to trace and return the proceeds of corruption in partner countries that find their way to the UK (another form of capital flight); for example funding the Proceeds of Corruption Unit at the Metropolitan Police as well as a team at the Crown Prosecution Service. A total of over £170 million worth of asset have been restrained, recovered or returned and prosecutions obtained for money-laundering and other offences, most recently of the associates of James Ibori, former governor of Delta State in Nigeria.

*February 2012*
## Annex A

DFID ANALYSIS OF TAX RELATED PROJECT SPEND—FY2006/07 TO FY2010/11

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<td>£25,476</td>
<td>£5,000</td>
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<td>£725,559</td>
<td>£849,213</td>
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<td>107434</td>
<td>Reforms in Revenue Administration (RIRA)</td>
<td>DFID Bangladesh</td>
<td>01/04/2002</td>
<td>01/07/2008</td>
<td>£8,249,375</td>
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<td>£1,816,592</td>
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<td>£4,501,228</td>
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<td>Trademark East Africa—Burundi Programme</td>
<td>DFID Burundi</td>
<td>04/01/2010</td>
<td>31/03/2012</td>
<td>£6,525,000</td>
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<td>CARTAC Is Core Funding</td>
<td>DFID Caribbean</td>
<td>01/01/2011</td>
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<td>£4,500,000</td>
<td>35%</td>
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<td>Caribbean Regional Technical Assistance Centre</td>
<td>DFID Caribbean</td>
<td>01/09/2001</td>
<td>31/12/2007</td>
<td>£2,159,117</td>
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<td>Minerals Support Programme (contribution to World Bank PROMINES project)</td>
<td>DFID Democratic Republic of Congo</td>
<td>01/01/2007</td>
<td>01/09/2015</td>
<td>£27,500,000</td>
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<td>Civil Service Reform Programme</td>
<td>DFID Ethiopia</td>
<td>01/12/2006</td>
<td>30/04/2012</td>
<td>£5,000,000</td>
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<td>£22,608</td>
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<td>Support for Public Sector Capacity Building Programme</td>
<td>DFID Ethiopia</td>
<td>01/12/2004</td>
<td>31/12/2012</td>
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<td>Orissa Modernising Economy, Govt and Administration</td>
<td>DFID India</td>
<td>01/04/2009</td>
<td>31/12/2015</td>
<td>£19,300,000</td>
<td>12%</td>
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<td>DFID India</td>
<td>01/04/2010</td>
<td>31/03/2016</td>
<td>£61,000,000</td>
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<td>£2,181</td>
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<td>MP— Strengthening performance management in government</td>
<td>DFID India</td>
<td>01/04/2007</td>
<td>31/01/2016</td>
<td>£17,700,000</td>
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<td>Support for Governance reform in Bihar</td>
<td>DFID India</td>
<td>15/09/2008</td>
<td>15/09/2014</td>
<td>£18,000,000</td>
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<td>01/03/1999</td>
<td>31/12/2008</td>
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<td>DFID India</td>
<td>01/01/2003</td>
<td>10/06/2011</td>
<td>£36,000,000</td>
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<td>West Bengal : Kolkata Urban Services for the Poor</td>
<td>DFID India</td>
<td>01/04/2003</td>
<td>31/03/2015</td>
<td>£102,700,001</td>
<td>5%</td>
<td>£385,418</td>
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<td>West Bengal : Kolkata Environment Improvement Project</td>
<td>DFID India</td>
<td>01/04/2001</td>
<td>31/03/2009</td>
<td>£18,499,895</td>
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<td>£180,389</td>
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<td>Revenue Authority Support</td>
<td>DFID Kenya</td>
<td>01/01/2005</td>
<td>01/08/2006</td>
<td>£262,631</td>
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<td>DFID Kosovo</td>
<td>22/06/2011</td>
<td>01/10/2011</td>
<td>£161,056</td>
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<td>114099</td>
<td>Support to Central Revenue Authority—Technical Cooperation</td>
<td>DFID Mozambique</td>
<td>01/12/2007</td>
<td>30/06/2013</td>
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<td>100%</td>
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<td>£0</td>
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<td>£14,624</td>
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<td>£115,012</td>
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<td>Central Revenue Authority—Common Fund</td>
<td>DFID Mozambique</td>
<td>01/03/2007</td>
<td>30/06/2013</td>
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<td>104021</td>
<td>Integration of Reformed DGI into RA</td>
<td>DFID Mozambique</td>
<td>01/02/2004</td>
<td>31/10/2007</td>
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<td>Integration of Reformed Customs</td>
<td>DFID Mozambique</td>
<td>01/09/2003</td>
<td>30/04/2006</td>
<td>£42,165</td>
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<td>Integration of Reformed Direct Tax Department</td>
<td>DFID Mozambique</td>
<td>01/02/2004</td>
<td>31/10/2007</td>
<td>£1,716,535</td>
<td>100%</td>
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<td>Local Governance and Community Development Programme</td>
<td>DFID Nepal</td>
<td>01/07/2008</td>
<td>31/07/2012</td>
<td>£12,150,000</td>
<td>5%</td>
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<td>£227,658</td>
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<td>£38,429</td>
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<td>200341</td>
<td>Facility for Oil Sector Transparency (FORSTER)</td>
<td>DFID Nigeria</td>
<td>01/06/2009</td>
<td>30/06/2015</td>
<td>£9,500,000</td>
<td>10%</td>
<td>£0</td>
<td>£0</td>
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<td>£13,377</td>
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<td>Phase II Support to Nigerian Extractive Industries Transparency Initiative</td>
<td>DFID Nigeria</td>
<td>01/04/2007</td>
<td>30/11/2009</td>
<td>£79,962</td>
<td>10%</td>
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<td>£5,753</td>
<td>£10,718</td>
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<td>Project Description</td>
<td>Department</td>
<td>Start Date</td>
<td>End Date</td>
<td>Total Budget</td>
<td>% Estimated focus on tax</td>
<td>Tax Related Spend in FY 2006-07</td>
<td>Tax Related Spend in FY 2007-08</td>
<td>Tax Related Spend in FY 2008-09</td>
<td>Tax Related Spend in FY 2009-10</td>
<td>Tax Related Spend in FY 2010-11</td>
<td>Total Tax Related Spend (2006-07 to 2010-11)</td>
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<td>104190 Growth and Employment in States Programme (GEMS)</td>
<td>DFID Nigeria</td>
<td>10/09/2008</td>
<td>30/03/2017</td>
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<td>104188 Subnational Investment Climate Assessments</td>
<td>DFID Nigeria</td>
<td>01/07/2006</td>
<td>01/11/2011</td>
<td>£6,533,051</td>
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<td>£94,898</td>
<td>£979,958</td>
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<td>DFID Pakistan</td>
<td>01/01/2005</td>
<td>31/12/2011</td>
<td>£12,978,000</td>
<td>100%</td>
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<td>£2,480,000</td>
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<td>£3,420,000</td>
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<td>201819 Support to Rwanda Public Financial Management Reform- Basket Fund</td>
<td>DFID Rwanda</td>
<td>18/05/2010</td>
<td>31/12/2013</td>
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<td>28/02/2007</td>
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<td>22/11/2002</td>
<td>£5,416,857</td>
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<td>DFID South Sudan</td>
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<td>01/02/2012</td>
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<td>DFID Southern Africa</td>
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<td>105369 Tanzania Revenue Authority—Tax Modernisation Programme</td>
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<td>30/06/2013</td>
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<td>DFID Uganda</td>
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<td>02/03/2011</td>
<td>£9,280,748</td>
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<td>DFID Yemen</td>
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<td>08/06/2009</td>
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<td>201618 Strengthening Public Financial Management in Zambia</td>
<td>DFID Zambia</td>
<td>02/05/2011</td>
<td>31/03/2013</td>
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<td>DFID Zambia</td>
<td>01/10/2000</td>
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<td>05/06/2007</td>
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<td>Funding for the OECD</td>
<td>Governance and Social Development Group</td>
<td>24/06/2010</td>
<td>31/03/2015</td>
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**TOTALS**

| | | | | | £17,957,726 | £13,572,457 | £18,372,332 | £21,750,142 | £25,290,392 | £96,943,050 |

**Notes**

1. The projects contained in the above analysis are those which have incurred expenditure since the start of FY2006/07. Expenditure for the five financial years from FY2006/07 is showed. Expenditure after FY2010/11 is excluded.
2. Where projects have a partial focus on taxation an estimated percentage for “the project’s focus on taxation” is provided.
3. Identification of tax related projects involved accessing DFID’s internal systems and consulting with Country Offices, but as the range of such projects is very broad and there is no specific identification code for tax projects the list may not be complete.
Supplementary written evidence submitted by the Department for International Development

DFID TAX PROJECTS SUMMARY—FEBRUARY 2012

AFGHANISTAN

DFID Afghanistan is providing technical assistance over four financial years (2011–12 to 2014–15) to the Afghanistan Revenue Department (ARD) in the Ministry of Finance (MoF) of the Government of Afghanistan (GoA). This assistance is intended to help increase domestic revenue collection.

Key activities include modernising tax administration, eg computerised tax admin system; providing technical support to build capacity, including writing tax laws and assisting with institutional reform; and setting up a taxpayer awareness unit, which produces leaflets on obligations and how to pay and promotes this to large and medium taxpayers through ARD.

The purpose of the support is to assist the GoA in sustaining the impressive progress made in domestic revenue collection in recent years, in part achieved through a DFID-funded project (Strengthening Tax Administration, 2007–12). This support helped ARD establish a working base for tax administration reforms.

The current project is expected to play a key role in supporting the GoA in meeting its domestic revenue collection targets and is in line with the UK objective of ensuring a viable Afghan state that provides increasing levels of key basic services within the context of a stable and growing economy.

Domestic revenue collection has been increasing over recent years reaching a high of 11.2% of GDP in 2010–11, or about AFS 80.1 billion. Tax collection in 2010–11 grew by 20% and customs duties by 25% over 2009–10 levels.

BANGLADESH

DFID is supporting Bangladesh’s National Board of Revenue through a “Tax Administration—Capacity and Taxpayer Services” (TACTS) project, costing £7.1 million, between 2007 and 2015.

The government has ambitious targets to increase tax revenue. The project supports this, with objectives to improve the Government’s weak domestic revenue position, widen the tax base, promote transparency and trust in the revenue administration system and improve efficiency in tax administration.

The project aims to contribute to increasing the number of registered taxpayers from 2.2 million to 4 million. It will provide support to the large taxpayer unit (LTU) to increase efficiency, professionalism and effectiveness, leading to increased tax revenue. This includes provision of training on selected business sectors (eg banking, telecoms and insurance) as well as complex functions such as transfer pricing. There will also be mechanisms put in place to reduce LTU income tax arrears outstanding (eg revision of appeal process, strengthened appeals resolution process, strengthened income tax return audits). A Central Intelligence Cell will be strengthened to support investigation of non-compliance and tax evasion. Internal audit and legal competencies within the National Board of Revenue (NBR) will also be strengthened.

BURUNDI

DFID supports taxation and customs through Trademark East Africa (TMEA), a programme funded with other donors. In Burundi, this programme seeks to promote greater regional integration and trade competitiveness through a reduction in transport and related costs along the key corridors in Burundi. A study for a One-Stop Border Post at Kobero, the main border with Tanzania, has taken place and further preparatory work on a One-Stop Border Post with Rwanda is underway. TMEA also supports the Burundi Revenue Authority’s (OBR’s) operational departments (domestic taxes, customs and investigation) and support departments (human resources, finance, information technology, planning and research, communications and taxpayer services, legal affairs and risk management). Support will also seek to strengthen large taxpayer collection. In 2010, TMEA assisted OBR with the recruitment of its senior management team and heads of divisions; the first Commissioner General for the OBR has been in post since June 2010.

About £500,000 to support “fast track” activities to establish OBR was also provided from DFID’s Regional Integration in East Africa Project (REAP).

107 Office Burundais des Recettes.
108 TMEA helped OBR purchase the ASYCUDA World computer system for its customs operations and the SIGTAS system for its domestic tax operations. It is expected that computerising its border posts and putting in place effective controls on high value imports such as petrol and other excisable goods will bring significant improvements to Burundi’s revenue performance over the short term.
The OBR has successfully increased revenue collection. The Burundi Revenue Authority was set up in July 2010, at a time when the country’s tax and customs services topped the list of East Africa’s most corrupt organisations in Transparency International’s East African Bribery Index. The programme set out to transform the culture of tax collection. From January to June 2011, revenue collection was 37.4% above the level for the same period the previous year. From July to September 2011 the outturn revenue exceeded the forecast by 14% (or £7 million).

Democratic Republic of the Congo (DRC)

In DRC, DFID is contributing £27.5 million to a World Bank project (WB PROMINES) working on transparency in the mining sector—which could have a significant impact on revenue collection. A target is to increase the overall tax to GDP ratio and increase the proportion of tax directly attributable to the mining sector from 24% to 30%. The increased revenue is also expected to impact positively on growth and peace. Implementation of the Extractive Industries Transparency Initiative (EITI) in DRC is also supported through PROMINES.

Work on tax is also included in a new Public Financial Management and Accountability programme which is planned to start in 2012.

Ethiopia

In Ethiopia, DFID (alongside other donors) supports the Public Sector Capacity Building Programme which includes capacity building support to the tax system. An objective is to increase tax revenue by 87% from 43.3 billion birr in 2010 to 81.1 billion birr in 2013.109

The UK also provides technical assistance bilaterally to the Ethiopian Revenue and Customs Authority (ERCA) by providing targeted, demand-led technical assistance for civil service reform. This has supported, among other things, significant improvements in average customs clearance times based on a 2007 benchmark (low risk imports from seven days to 10 minutes, and exports from eight hours to 15 minutes).

Her Majesty’s Revenue and Customs (HMRC) is twinned with the ERCA and provides technical assistance aligned to the strategic needs of the Ethiopian government on both customs and tax. Areas covered include IT, customer services, enforcement and audit.

Ghana

DFID is funding technical support to Ghana to help with implementation of the Global Forum international standards of transparency and exchange of information for tax purposes.

DFID has also disbursed total of £6.5 million in sector budget support by 2011 on a Government-led project, Natural Resource and Environmental Governance (NREG). One of the intentions of the NREG programme is to improve mining sector revenue collection, management, and transparency, although the scope of the project is much broader. It also includes policy dialogue on EITI.

Technical assistance support continues and is intended to contribute to the design of a planned further phase of support for NREG. A project on oil & gas, mainly around governance and revenue management, is also planned.

India

DFID has a number of programmes with state governments which include within their scope assistance in improving revenues. These include:

- The Support Programme for Urban Reforms (SPUR) in Bihar, which aims to enhance the ability of selected Urban Local Bodies to provide urban services and attract private investment. This includes increasing local resource mobilisation improving the management of resources. The project is among the first in India to assist municipal revenue reforms, through taxpayer and property mapping, systems reform, use of IT and staff training.

- The Orissa Modernising Economy, Government and Administration (OMEGA) project, costing £19.3 million and operating from 2010 to 2015, which aims to enhance private sector investments in industries and infrastructure, to improve Government of Orissa’s capacity to mobilise revenue and manage expenditure and to improve delivery of selected poverty alleviation programmes.

109 Ethiopia’s high inflation rate will considerably erode the actual value of this increase.
The Bihar Governance and Administrative Reforms Programme (BGARP) which aims to improve the capability of the State Government of Bihar to deliver better quality services to all its citizens, through a number of measures, including technical analysis and capacity building of the Transport, Registration and Commercial Tax departments in the State Government.

KENYA

DFID is funding technical support to Kenya to help with implementation of the Global Forum international standards of transparency and exchange of information for tax purposes.

Kenya’s National Taxpayers Association (NTA) is funded through DFID’s Governance and Transparency Fund. The NTA works to ensure use of taxpayer’s money to deliver quality public services and transparent and citizen-responsive management of taxpayers’ money in devolved funds. It also raises awareness of taxpayers of their rights and responsibilities. This is achieved through establishing Citizen Action Groups. One particular success has been the use of the media to strengthen advocacy for the use of taxpayers’ money. NTA report that the use of media effectively “raises the stakes”, making it more difficult for public institutions to ignore issues and thus prompting quick and better responses from them.

MALAWI

DFID is planning (not yet approved) to contribute £7.5 million over five years to support the Government of Malawi’s PFM reform plan, which will include support on revenue.

MOZAMBIQUE

In Mozambique, DFID supports the recently created Central Revenue Authority through a multi-donor common fund within the national state budget, having provided £2.3 million to this fund between March 2007 and December 2011. This support helped establish the Mozambican Revenue Authority. It is now supporting the introduction of modern management practices and the achievement of the strategic objectives of the revenue authority in terms of improving the effectiveness and efficiency of tax collection. Aims include increasing revenue, strengthening the link between the taxpayer and the state, and improving public information and transparency to ensure resources are used well.

The Common Fund has contributed to a continuous increase in tax collection since 2007. Each year since the establishment of the Common Fund, actual tax revenues have exceeded the targets—in 2010, by 11% and in the first semester of 2011, by 3%.

One important factor in this success is that Mozambique now has over 1.5 million registered tax payers compared with 391,000 in 2006. There has also been significant investment in civic education and sensitisation around tax payments.

Part of DFID’s funding supports capacity building of the large tax payers unit to improve tax collection from large taxpayers. This includes training staff responsible for supporting large tax payers, and those auditing large taxpayers.

NIGERIA

DFID Nigeria has a “State Partnership for Accountability, Responsiveness and Capacity” programme, to improve financial management systems and enhance government use of public resources at state level. In some states, this programme supports tax collecting agencies, for example, with systems, procedures and controls in collecting land and employment taxes.

DFID Nigeria is providing £90 million in support to the “Growth and Employment in States” (GEMS) programme which includes work on tax. The programme supports the value chain and business environment, as well as land reform and investment policy. An estimated £9 million is expected to be tax related, focused at state level.

This project follows the Nigerian sub-national government Investment Climate Project (ICP) from 2007–11, which identified taxation as one of the key, feasible areas of reform. Support provided under the ICP included assistance with the development of state-level five-year tax board modernisation plans, training for 600 tax officials (the first training on tax many of them had ever been exposed to) and substantial support to the introduction of unique taxpayer identification numbers (UTIN) which has now reached the stage of formal testing.

The latest programme (GEMS) will use an innovative “market” approach to understand and address tax as it affects and is affected by market systems and political incentives, with a special focus on impact on the poor. It will have a strong focus on sustainability, looking at facilitating (rather than providing) pilot reforms, which it will seek to have replicated across the country through demand and demonstration effects.
The project will introduce a range of varied interventions in different states, including; mapping and documentation of existing tax processes, business processing re-engineering of tax processes, tax harmonisation and the removal of multiple and “nuisance” taxes, and support to target states’ existing, broader, reform plans.

DFID is also funding £11 million for the Enhancing Nigerian Advocacy for a Better Business Environment (ENABLE) programme. This programme, running until 2013, is to improve the environment for business advocacy in Nigeria. A small part of this programme worked to improve public-private dialogue in Lagos State on the issue of Multiple Taxation.

In 2011, DFID provided £89,000 to the International Monetary Fund to rewrite tax legislation in Nigeria.

HMRC has also provided assistance to Nigeria—two compliance caseworkers spent time in Nigeria helping the Federal Inland Revenue Service develop a compliance strategy, and senior level HMRC management sit on the board of the Nigerian tax administration in an advisory capacity.

**Occupied Palestinian Territories**

DFID supports a £5.5 million programme entitled “Palestinian Governance Facility”. The project started the inception phase in November 2011 and is due to finish in March 2015. The aim of the project is to improve the capacity of the Palestinian Authority to raise revenues from a strengthened tax base and reduce reliance on donor support. There is also an objective to plan, prioritise and manage expenditure, including donor funds.

**Overseas Territories**

DFID provided £1.4 million of PFM and tax reform-related technical assistance in 2011–12 to the Turks and Caicos Islands (TCI). This support has built an expenditure management system, reduced the backlog of accounts and submitted the end-of-year accounts for the first time in four years, helped to increase revenue collection by around one-third in a single year, and strengthened the revenue audit function to prepare for the switch to VAT in 2013. DFID technical assistance also produced a paper which is now being used as the basis to draft tax and PFM legislation.

In Anguilla, DFID funded £100,000 on PFM and tax-reform-related technical assistance between 2010 and 2011. This funded a PFM assessment followed by a revenue and expenditure analysis. Some of the report’s recommendations were incorporated into the Government of Anguilla’s 2011 Budget. DFID has subsequently provided specialists to help establish a Tax Reform Working Group, and to help the group deliver tax reform recommendations to the Anguillan Government. Some revenue-raising measures put forward by this group have been incorporated into the Government of Anguilla’s 2012 Budget.

In Montserrat, DFID recently provided £109,000 to support the Government of Montserrat’s customs and revenues services.

A tax adviser and tax auditor have also been funded for St Helena.

**Pakistan**

A Tax Administration Reform Project, costing £13 million over six years came to an end in December 2011. The objectives of the programme included improving organisational efficiency and effectiveness of revenue administration, promoting compliance through strengthened audit and enforcement capacity, improving trade facilitation through modern and internationally acceptable customs procedures, and improving the integrity and fairness of the revenue system.

**Rwanda**

The last phase of a 10 year programme of support for the Rwanda Revenue Authority (RRA) ended in June 2010. DFID support helped to provide the laws and regulations under which the authority was established, the office building and the management systems. The 10 year period of support saw a six-fold increase in the taxes collected and in 2010, the management procedures of the authority were awarded ISO 9001 2008 accreditation—the first Rwandan institution to attain this standard. The Authority reached a point where it was collecting the full £24 million value of DFID’s 10 year support programme every three weeks. Its effectiveness has been a major factor in Rwanda’s impressive development performance in recent years.

DFID Rwanda continues to support RRA indirectly through the Multi-Donor Basket Fund for Public Financial Management Reforms managed by the Rwanda Ministry of Finance, to which DFID is contributing £ 4.5 million for three years. This project includes a component to maximise revenue mobilisation. This will be achieved through improving risk-based audit, reducing cost of tax administration, improving service delivery, enhancing support to sub-national governments, broadening the tax base through enhanced voluntary tax compliance and strengthening organisational capacity.
UK support to the RRA has also continued through DFID’s regional integration support programme managed by Trademark East Africa (TMEA). £4.9 million of this programme is earmarked for the RRA to strengthen regional market integration—notably through the construction of “one-stop border posts” with Rwanda’s neighbours (Tanzania, Uganda, Burundi and the DRC).

Furthermore, there is an ongoing mentoring arrangement between the Commissioner General of the RRA and HMRC’s Permanent Secretary for Tax.

**Sierra Leone**

DFID has committed £16 million to support tax administration reform in Sierra Leone since 2004, with the current project due to end in 2012. The aim is to improve the National Revenue Authority (NRA)’s ability to administer taxes with an overall aim of boosting revenue collection as a percentage of GDP.

Post-war reconstruction and DFID support have helped to increase tax as a percentage of GDP from as low as 5% during the war to 11.6% in 2009 and 13.2% in 2010.

DFID is providing technical advisory support focused on improving governance of the NRA and compliance of taxpayers, including supporting the establishment of a Large Taxpayer Office (LTO), formed in January 2011. DFID is also managing a budget to procure essential items supporting the set up of the Large Taxpayer Office and upgrading the Customs and Excise Department with a modern risk-based computerised processing system.

So far, the programme has improved tax administration through the introduction of a General Sales Tax, introduction of Taxpayer Identification Numbers for all taxpayers, and implementation of a computerised risk-based customs control system at the country’s main port and airport.

The number of large taxpayers filing and paying on time has increased. The number of taxpayers audited during the year has also increased.

Operations within the NRA such as human resources, financial management and information and communications technology and data management systems are also being supported.

Finally, DFID is supporting the Government of Sierra Leone to improve revenue management in the mineral sector through support for setting up a new National Minerals Agency (NMA). The NMA will act as a regulator by managing and monitoring minerals licenses. DFID is also providing broader support on improving management of the sector—including transparency and accountability—through the World Bank’s Extractive Industries Technical Assistance Programme (EITAP).

**South Sudan**

DFID is contributing £4.8 million to “Capacity Building Trust Fund, Phase II” which started in February 2010 and is due to finish in February 2012. The aim is to improve the Government of South Sudan’s ability to allocate resources and deliver services. Important but under-resourced fiscal and PFM issues will be financed under Pillar 1 (Enhance fiscal responsibility) and Pillar 2 (Strengthen PFM systems) of the Juba Compact.

This fund also supported tax reform in Northern Bahr Ghazal State, including introduction of a new integrated tax management system (ITMS) in October 2011, which is expected to improve revenue collection by sealing revenue loopholes and easing the taxpayer registration exercise, as well as making improvements on the expenditure side. The project also included training for staff and supported tax awareness for the public.

DFID is also planning to help strengthen South Sudan’s customs systems.

**Tanzania**

DFID is contributing £8 million between 2009 and 2013 to the latest phase of a multi-donor funded Tax Modernisation Programme in Tanzania, which is helping to strengthen multiple departments within the Tanzanian Revenue Authority (TRA), including the Large Taxpayers Department. The project objective is to promote an effective and efficient tax administration which promotes voluntary tax compliance by providing high quality customer services with fairness and integrity through competent and motivated staff.

The programme has helped to fund new IT systems and related training to reduce the time taken by officials within the Customs and Excise Department to clear goods through customs. It has also funded investments by the TRA to improve taxpayer services and taxpayer education. The programme is also financing work by the Research and Policy Department within TRA to analyse the likely tax gap (between tax collected and tax payable) in key sectors, such as mining and telecoms.
Total revenue collection in 2010–11 was 19.5% up on 2009/10. Revenue as a percentage of GDP shows modest improvement over the same period: from 14.6% to 15.3%. Time taken to clear goods at sea ports and airports has also reduced. The average arrival to removal times for the quarter ended June 2011 was 12 days at Port (compared to 15 days in 2009) and five days at Airport (compared to seven days in 2009).

Uganda

The “Growth and Poverty Reduction Grant” (supported by £50 million of DFID funding) is a budget support programme which intended to help strengthen public institutions, including helping to increase tax revenue by improving tax collection, reducing the gap between approved budget allocations and the amount released to line ministries and reducing fiscal arrears.

DFID has had a longstanding programme of support to the Ugandan Revenue Authority (URA). Most recently this has helped URA management to plan and implement a modernisation plan. The plan identified a series of initiatives encompassing the improvement of business processes in customs, domestic taxation, corporate services, legal services; an increased application of information technology, expanded public and taxpayer education activities, higher standards of service quality and enhanced institutional integrity.

DFID is planning to provide £2 million of technical assistance and financial aid to the Uganda Revenue Authority (URA) to enable it to build its capacity for the taxation of oil. This funding will be used to purchase a new information technology system to manage oil taxation, and to pay for training for staff involved in oil taxation, to pay for technical advisers to provide mentoring and on-the-job training for cost recovery audits, and to help update the oil tax manuals. Together, URA staff and DFID advisers will revise business processes for oil taxation. Technical assistance will also be provided to help design and procure the new IT system.

HMRC hosted a short term secondment of officials from the Ugandan Revenue Authority earlier this year, focused on risk, intelligence and criminal investigation functions.

Zambia

DFID Zambia has extended its support to the multi-donor Public Expenditure Management and Financial Accountability programme, providing an additional £2.2 million from 2011 to 2013. This programme includes a component to strengthen tax administration at the Zambia Revenue Authority, with the objective of reversing the recent decline in the non-mining tax to GDP ratio.

DFID has also contributed £200,000 to a basket fund (with Norway and the EU) which is being used to strengthen the Mines Ministry. The Ministry has a crucial role to play in increasing mining tax revenue (eg promoting investment, checking the quantities and grades of mineral exports claimed by mines). Specific activities being supported are strengthening the cadaster (crucial for issuing exploration licenses), review of mining legislation, piloting physical audits of export consignments and supplementary funding of EITI.

Additional Work Relating to Tax

African Tax Administrators Forum

The African Tax Administration Forum (ATAF) is a platform to promote and facilitate mutual co-operation among 33 African Tax Administrations. It also enables these Administrations to contact tax experts in organisations like HMRC directly. DFID is providing funding of £500,000 and was amongst the first donors to support ATAF. The UK (HMRC) helped launch the Forum and has provided in depth outreach on transfer pricing to member countries.

Foreign Investment Advisory Service (FIAS)—World Bank Group

DFID is providing support to FIAS totalling £1.4 million over seven years (2008–2015). FIAS works to strengthen the investment climate of developing countries through improved policy making and reform. FIAS work involves helping developing countries remove tax barriers to growth and investment, widen the tax base through greater inclusion and facilitate greater productivity of the tax base.

FIAS has an objective to increase the number of enterprises complying with tax requirements by 10% within three years of FIAS supported tax reforms.

FIAS is also supporting a new initiative to improve tax transparency and promote international cooperation against tax evasion, whilst improving developing countries’ ability to administer and enforce their tax laws. Technical assistance in Africa and East Asia focuses on helping countries to develop transfer pricing legislation, administrative procedures, audit capacity, and appropriate accounting rules and ensure their legal and administrative frameworks meet international tax transparency standards.

During 2008–11, FIAS has made a contribution to 49 reforms of business taxation systems in countries around the world (of which 34 were in Sub-Saharan Africa).
International Development Committee: Evidence

International Centre for Tax and Development (ICTD)

DFID is funding £3.5 million until 2015 for a research programme, which will generate knowledge to help developing countries to mobilise domestic resources efficiently, effectively and equitably, and develop tax systems that promote pro-poor economic growth and good governance.

International Tax Dialogue

As part of its Tax Reform for Poverty Reduction Programme, DFID provided funding to the International Tax Dialogue, including specific funding to produce a study with the African Tax Administrators Forum on Domestic Resource Mobilisation in Sub-Saharan Africa.

IMF Regional Technical Assistance Centres

Through the International Monetary Fund (IMF)’s Regional Technical Assistance Centers, DFID is funding technical assistance including on revenue administration, as well as other areas of financial and economic management. Work in East Africa has now been extended to Southern Africa. DFID also funds an IMF Regional Technical Assistance Centre in the Caribbean.

East AFRITAC

The countries eligible for assistance are: Eritrea, Ethiopia, Kenya, Malawi, Rwanda, Tanzania and Uganda. DFID will provide £11 million over a five year period (2009–10 to 2013–14). The IMF reported that “significant results” were achieved on revenue administration in these countries.

South AFRITAC

The countries eligible for assistance are: Angola, Botswana, Comoros, Lesotho, Madagascar, Mauritius, Mozambique, Namibia, Seychelles, South Africa, Swaziland, Zambia and Zimbabwe. DFID will provide £7 million over a five year period (2010–11 to 2014–15).

CARTAC

CARTAC member countries are: Antigua and Barbuda, The Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Haiti, Jamaica, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Trinidad and Tobago, and Suriname. The following UK Territories are also members: Anguilla, Bermuda, British Virgin Islands, Cayman Islands, Montserrat, and the Turks and Caicos Islands. CARTAC focuses on revenue administration; public financial management; capital markets development; financial sector regulation and supervision; macroeconomic management; and macro-fiscal management and economic statistics. DFID is providing funding of £4.5 million over five years (2011–2016).

Investment Climate Facility for Africa

DFID was instrumental in the establishment of the Investment Climate Facility (ICF) for Africa and was a founding member and supporter of the initiative. DFID has committed £17 million of support to the ICF for its work across Africa to remove the barriers to doing business and make the continent a more attractive place for companies to invest and locate their operations. The ICF is a partnership between the private sector, donors and national governments. It is working in 29 countries in Africa and has 40 projects, several of which relate to tax.

There is further information at:

OECD Tax and Development Task Force

The UK supports the OECD tax and development task force and has committed £250,000 until March 2015.

The OECD Informal Task Force on Tax and Development is examining how capacity building in the tax administrations of developing countries can bring the greatest benefit. HMRC is leading a specific outreach project on improving the efficiency of transfer pricing audits, involving Uganda, Nigeria and South Africa.

Global Forum on Exchange of Information for Tax Purposes

DFID supports the Global Forum on Exchange of Information for Tax Purposes to ensure developing countries can benefit from the more transparent international tax environment. DFID is funding technical support to Ghana and Kenya to help them implement the Global Forum international standards of transparency and exchange of information for tax purposes, and participate fully in government to government international tax information exchange.
Further written evidence submitted by the Department for International Development
APPENDIX TO THE TRANSCRIPT OF THE ORAL EVIDENCE SESSION ON 15 MAY 2012

The following should be appended to the transcript of the evidence session in order to correct some errors in what was said and to provide clarification:

QUESTION 160
The ratio of tax to GDP which was mentioned in the reply should be a minimum level of 20% (not 19%).

QUESTION 164
In discussing the level of tax related spending, a figure of £159 million relating to the period 2001–06 was referred to. The period concerned was the five and a half years from January 2001 to June 2006. However, the £159 million figure quoted is not the estimated expenditure during this period. It is the estimated total tax related financial commitment for projects which were operational during the period and a few which, at the end of the period, were planned but not yet operational. The estimated tax related expenditure for the projects during the five and a half year period was £81 million.

QUESTION 173
The DFID contribution to helping the Burundi revenue authority (the OBR) was about £5 million (not about £30 million).

The £19 million project in Afghanistan is in its early stages, so it should be described as assistance we are providing, rather than have provided, and the increase in revenue referred to cannot be attributed to this project (although DFID did help with increasing revenue through an earlier project).

The project in Tanzania is on-going, so the £8 million should be described as funding we are contributing, rather than funding we have contributed. The project period is 2009 to 2013.

QUESTION 181
The example of preference for traditional courts over formal courts is a finding about attitudes in Liberia and an example of a challenge when promoting the spread of formal legal institutions. It is not the explanation for why informal businesses do not become formal or a finding about processes for resolving tax disputes.

QUESTION 189
The response should not be interpreted as DFID helping with transfer pricing wherever we are supporting the development of large taxpayer units. The situation should be described as follows: “We are supporting the development of large taxpayer units in some countries. In Bangladesh, this includes help on transfer pricing”.

QUESTION 190
The latter part of the response refers to efforts in the EU. To clarify, this is not about the EITI, but about EU proposals to introduce rules requiring extractives companies to report their payments to governments.

QUESTION 194
The last sentence of the response, about CDC not making new investments through harmful tax regimes should be qualified by the statement “where it has the discretion as originating or sole investor”, to be in line with the new CDC policy.

QUESTION 195
The statement about CDC having the power and discretion to apply that as a policy should be qualified by the statement “in many cases”, (because in some cases CDC may not be the originating or sole investor and may not have discretion).

To be clear, the last sentence of the response refers to international tax transparency and exchange of information standards. Therefore the sentence should say “Regimes that do not comply with the international tax transparency and exchange of information standards are defined by the OECD and Global Forum on Transparency and Exchange of Information for Tax Purposes”.

QUESTION 198
To improve clarity the initial part of the response should say: “Yes. That is what has been put out, that the previous shareholding structure of Actis meant the taxpayer and Government did not receive any direct financial return at all, and that is my understanding.”
The end of the last sentence, which refers to the Government’s rights should be expressed as “have therefore given the Government rights to receive not only a value for the sale of 40%, but also a share in the carried interest profits of certain of Actis’s funds”.

**Question 199**

In the last part of the response, the explanation of the situation under the new deal should be expressed as follows: “under the new deal, the Government now has the right to receive a cash payment of US$ 13 million and a share in the carried interest profits of certain of Actis’s funds, rather than, as before, effectively an entitlement to share in the profits of Actis only after the Executive of the partnership has been able to take out the revenues, which, as you reported from the 2007 accounts, is broadly what has happened, leaving none for the contributing members.”

19 June 2012

**Supplementary written evidence submitted by The Department for International Development (DFID)**

**Tackling the Illicit Flow of Assets into the UK**

As a leading global centre for financial and legal services, the UK is a significant target for attempts to launder criminal proceeds obtained through corruption overseas. This can take any number of forms including acquisition of property in the UK, payment of private school fees in the UK or bank transfers via the UK to other financial centres.

There is no consensus on the size of total illicit flows from developing countries into the UK but there is little doubt that stemming such flows and tackling the underlying problems is critical for developing countries both in economic terms and the governance impact associated with the elites that benefit.

**HMG Strategy on Tackling Corruption from Developing Countries**

There has been progress in tackling the problem of illicit flows from developing countries. Politically exposed persons (PEPs)—those in public positions and at risk of being corrupted—are the focus of a cross-Whitehall “Politically Exposed Persons Strategic Group”. This group brings together the key government ministries and agencies to co-ordinate UK strategy and action in relation to PEPs. The HMG strategy and the roles of the ministries and agencies are set out in a policy document “Combatting Money Laundering by Politically Exposed Persons” (attached as an Annex).

**DFID Support to UK Law Enforcement**

DFID has been providing support to UK law enforcement since 2006 to tackle money laundering from developing countries. Since 2006, the Department has supported two police units—the Metropolitan Police Service Proceeds of Corruption Unit and the City of London Police Overseas Anti-Corruption Unit. In 2011, the Department extended funding support to the Crown Prosecution Service Asset Recovery Team and plans are in progress to fund an enhanced intelligence cell in the Serious Organised Crime Agency. The total cost since 2006 has been in the region of £6million.

The following table showing figures from 2006 to June 2012, shows the current level of assets “restrained, recovered or returned”. Assets that are “restrained” means assets under a restraint order under the Proceeds of Crime Act; “recovered” assets means assets recovered or confiscated following a trial and a confiscation order; and assets “returned” means assets which have been returned to developing countries.

The figures in the table change regularly as more assets are restrained; or as the assets are re-valued at various points in the criminal process.

<table>
<thead>
<tr>
<th></th>
<th>Identified for restraint</th>
<th>Restraint</th>
<th>Confiscated/Forfeited</th>
<th>Returned/Recovered</th>
</tr>
</thead>
<tbody>
<tr>
<td>Met Police</td>
<td>63,013,000</td>
<td>11,508,000&lt;sup&gt;a,b&lt;/sup&gt;</td>
<td>1,295,000&lt;sup&gt;c&lt;/sup&gt;</td>
<td></td>
</tr>
<tr>
<td>City of London Police Overseas Anti-Corruption Unit</td>
<td>6,750,000</td>
<td>4,750,000&lt;sup&gt;d&lt;/sup&gt;</td>
<td>11,250,000&lt;sup&gt;b&lt;/sup&gt;</td>
<td></td>
</tr>
<tr>
<td>SOCA</td>
<td>6,750,000</td>
<td>4,750,000&lt;sup&gt;d&lt;/sup&gt;</td>
<td>19,000,000</td>
<td></td>
</tr>
<tr>
<td>Civil recovery</td>
<td>12,400,000&lt;sup&gt;f&lt;/sup&gt;</td>
<td>12,400,000&lt;sup&gt;f&lt;/sup&gt; (recovered)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>6,750,000</td>
<td>147,763,000</td>
<td>22,758,000</td>
<td>13,794,000</td>
</tr>
</tbody>
</table>
Notes

(a) Includes:
   — Forfeited funds of £1,115,000 ( £1,000,000 relates to the DSP Alamieyeseigha case—returned to Nigeria; and £115,000 relates to the Joshua Dariye case, also returned to Nigeria);
   — Funds under Confiscation Orders amounting to £10,393,000; of which the following has been collected: £180,000 related to Joyce Oyebanjo in the Dariye case (that was returned to Nigeria); £3,253,346 in confiscation cases relating to the James Ibori; and £543,000 that does not relate to PEP corruption.

(b) £11,250,000 from Macmillan’s Publishers civil disposal with SFO.

(c) Funds included in the Confiscated/Forfeited column that have been returned.

(d) Returned to Costa Rica.

(e) Returned to Uganda.

(f) Recovered UK property transferred to ownership of Nigerian Government.

Total of assets restrained, confiscated or forfeited
(Total of columns 2 and 3) £170,521,000
Total assets recovered or returned
(Column 4) £13,794,000

The cases that are completed and where money has been returned are:

Metropolitan Police Cases:
   — Alamieyeseigha case: £1,000,000 has been returned to Nigeria.
   — Joshua Dariye case: £115,000 has been returned to Nigeria;
   — Joyce Oyebanjo: £180,000 has been returned to Nigeria (Oyebanjo was an associate in the Dariye case).

City of London Police cases:
   — £35,000 has been returned in the Ugandan case of Chemical, Biological, Radiological, Nuclear (CBRN) Team Ltd. The defendants were Tumukunde (from Uganda) and Tobiasen (from UK, now deceased).
   — US$100,000 has been returned in the Costa Rica case, a joint case with the SFO against Pearson Webb Springbett International Ltd (PWS) The UK defendant was called Messent.

It should be noted that it is a long process to restrain and recover assets and so most of the biggest cases, including the cases of James Ibori and associates, are not yet complete. It is not possible to provide a breakdown of amounts relating to cases such as these, which are going through a judicial process.

June 2012

COMBATING MONEY LAUNDERING BY POLITICALLY EXPOSED PERSONS

HM GOVERNMENT’S PERSPECTIVE ON COMBATING MONEY LAUNDERING BY POLITICALLY EXPOSED PERSONS

This document outlines HM Government’s commitment to tackling money laundering by “politically exposed persons” (PEPs). PEPs include senior public officials, their families and close associates. The aim of the document is to highlight the importance of effective PEP controls, to set out Government’s objectives and to explain the role of key public sector organisations involved in combating money laundering by PEPs.

The content is relevant to UK Anti-Money Laundering (AML) supervisors; industry bodies; senior managers, money laundering reporting officers (MLROs) and staff in the regulated sector. Other organisations involved in anti-money laundering and asset recovery, within the UK and internationally, may also find this document informative.

The document is structured as follows:
1. Why are PEPs high risk customers?
2. What are the UK’s international obligations?
3. What are the obligations for regulated firms in the UK?
4. How is the Government helping to tackle money laundering by corrupt PEPs?
5. Appendix: members of the PEPs Strategic Group:
Glossary of Key Terms

AML  Anti-money laundering
CPS  Crown Prosecution Service
FATF  Financial Action Task Force
PEP  Politically exposed person
PoCU  Metropolitan Police Service Proceeds of Corruption Unit
SAR  Suspicious activity report
SOCA  Serious Organised Crime Agency

1. Why are PEPs high-risk customers?

Politically Exposed Persons (PEPs) hold prominent public functions. As a result of these positions PEPs are vulnerable to corruption, possessing the capacity to misuse their power, divert funds for their own benefit or take bribes. Although the majority of PEPs undertake legitimate business, a corrupt minority make this a high-risk category of customer for money laundering. In certain cases, business undertaken by corrupt PEPs will also be associated with organised crime or the drugs trade.

As a leading global centre for financial and legal services, the UK is a significant target for attempts to launder criminal proceeds obtained through corruption overseas. Previous cases have shown that UK financial institutions have been used as repositories for stolen funds from a number of countries across Asia, Africa and the Americas.

The UK has a robust legislative framework to deter, detect and disrupt money laundering and other financial crime. This includes regulations providing for enhanced due diligence procedures designed to mitigate exposure to the risk from corrupt foreign PEPs. It is important that the regulations, and the corresponding policies and procedures employed by firms, adapt to remain relevant to changing risks. There is a potentially significant risk for individual firms’ reputations, and more widely the UK marketplace, if risks from corrupt PEPs are not managed in an appropriately robust way.

Corruption by PEPs is not a “victimless” crime. Corruption undermines political systems leading to instability and potentially growth in organised crime, which can impact on all countries. In developing countries corruption hurts the poor disproportionately by diverting funds intended for development: limiting resources for health and education; discouraging foreign investment; distorting governance and accountability mechanisms; leaving the environment vulnerable to exploitation; undermining human rights.

No sector is immune from exploitation by corrupt PEPs and their associates seeking to steal and launder illicit funds. High risk sectors, products, transactions and countries of origin are likely to change in response to factors as effective deterrence & political shifts.

2. What are the UK’s international obligations to tackle PEPs money laundering?

The Government is at the forefront of international anti-corruption efforts and has a comprehensive anti-money laundering regime. The UK was a founding member of the Financial Action Task Force (FATF), the international body that develops global standards to combat money laundering. The UK also works with partners in the FATF and FATF-style regional bodies to encourage all countries to effectively implement the FATF standards. The UK was one of the first countries to have ratified the UN Convention Against Corruption, the first global anti-corruption treaty.

The FATF standards include special requirements for enhanced due diligence relating to PEPs, outlined in box 1 below. The legislative framework for money laundering in the UK is set by the Money Laundering Regulations 2007 (“the Regulations”) and the Proceeds of Crime Act 2002. The 2007 Regulations include specific provisions on foreign PEPs, based on the FATF recommendations and the Third EU Money Laundering Directive.

Note on FATF Recommendations

FATF’s 40 recommendations on money laundering include customer due diligence measures that financial institutions and designated non-financial businesses and professions should take when establishing a business relationship with a customer or carrying out transactions. Identifying and verifying the identity of the customer and the beneficial owner; obtaining information about the purpose and nature of the business relationship and ongoing monitoring are part of these customer due diligence measures.

The additional requirements for PEPs, within FATF Recommendation 6, are to:
(a) have appropriate risk management systems to determine whether a customer is a PEP.
(b) obtain senior management approval for establishing business relationships with PEPs.

Footnotes:
110 Politically Exposed Persons (PEPs) are defined within the Money Laundering Regulations 2007 as those individuals who hold (or have held within the preceding year) a prominent public functions for a state outside the UK, a Community institution or an international body. The definition encompasses immediate family members and known close associates.
111 FATF’s 40 AML recommendations can be downloaded from the FATF website: http://www.fatf-gafi.org/dataedcd/740/34849567.PDF
112 The Money Laundering Regulations 2007 came into effect on 15 December 2007. These Regulations implemented the requirements of the EU’s Third Money Laundering Directive in the UK.
(c) take reasonable measures to establish the source of wealth and source of funds.
(d) conduct enhanced ongoing monitoring of the business relationship.

3. What are the obligations for regulated firms in the UK?

The UK operates a risk-based approach to customer due diligence checks that requires enhanced procedures in high-risk situations, such as when customers are not physically present, or where the client is a foreign PEP. Every regulated business has a statutory AML supervisor under the 2007 Regulations. Several supervisors and industry groups have produced detailed guidance for firms setting out good practice and explaining how to apply risk-based approach in their sector.113 A simplified overview of PEPs-specific obligations is outlined in box 2 below.

Regulated firms are required to implement equivalent customer due diligence and record keeping measures across their entire group (ie in all branches and subsidiaries including those located abroad), unless local laws prohibit it. If this is the case they are required to inform their supervisor.

Regulated firms also have to comply with suspicious activity reporting requirements under the Proceeds of Crime Act 2002 and the 2007 Regulations. Businesses and their employees must disclose information to the Serious Organised Crime Agency (SOCA) via a suspicious activity report (SAR) when they have reasonable grounds to suspect that someone is engaged in money laundering or terrorist financing. SOCA advises firms to use the glossary of terms to highlight within the “reason for suspicion” if the suspicions relate to a proven or suspected PEP.114

Overview of requirements relating to PEPs AML

Senior managers and MLROs (“nominated officers”):
— Assess the firms risk from PEPs money laundering and ensure that the firm has appropriate risk-based procedures in place to identify PEPs.
— Ensure staff are aware of AML requirements through regular training, including PEPs AML (risk sensitive basis).
— Ensure that senior managers are required to approve new relationships with PEPs.
— MLROs to review internal SARs, including PEPs SARs, and submit to SOCA.

Staff managing client relationships:
— Be aware of the firm’s risk assessment and AML controls, including PEP provisions.
— Carry out enhanced due diligence on PEPs, on a risk sensitive basis.
— Gain approval from senior management for establishing a business relationship with a PEP.
— Take reasonable steps to establish the source of wealth and source of funds.
— Conduct enhanced ongoing monitoring.
— Submit PEPs SARs to the MLRO where there are reasonable grounds for suspicion.

What happens to SARs when they are submitted?

SARs are processed by SOCA’s Financial Intelligence Unit (FIU) and added to the Elmer database, which is accessible to law enforcement authorities.115 SARs which can be identified as relating to money laundering amongst PEPs are passed on to the Metropolitan Police Service Proceeds of Corruption Unit (PoCU) for further investigation. Where investigations lead to evidence capable of leading to prosecutions the PoCU will work closely with the Crown Prosecution Service (CPS), which has responsibility for prosecution and ultimately asset recovery through confiscation.116

Objectives

How is the Government helping to tackle money laundering by corrupt PEPs?

HM Government aims to make the UK a hostile environment for corrupt PEPs. Specific PEPs investigation capacity was established within the Metropolitan Police Service Proceeds of Corruption Unit in 2006. With the support of SOCA and the CPS, over £160 million of assets has been frozen and £20 million recovered.

114 SARs should be submitted online via the SOCA website: http://www.soca.gov.uk/financialIntel/suspectActivity.html. The glossary of terms can also be found online: http://www.soca.gov.uk/financialIntel/SARglossary.html.
115 Elmer is SOCA’s financial database, to which around 200,000 SARs are added each year. The database is available and searchable by police forces.
116 Other investigative agencies which can be involved in cases related to PEPs money laundering, depending on the source of intelligence and the type of predicate offence, include SOCA, Serious Fraud Office (SFO), City of London Police Overseas Anti-Corruption Unit (OACU), and Her Majesty’s Revenue and Customs (HMRC).
Ken Clarke, the Ministerial Anti-Corruption Champion, is the overall lead on government efforts to fight international corruption, of which the anti-money laundering regime is an integral component.

Government departments, public sector bodies and law enforcement agencies are working together to achieve the objectives 1–4 below:

**Objective 1: To Establish an Effective Deterrent Against Corrupt PEPs Money Laundering through Improved Intelligence Capability**

— Government is working to promote greater collaboration both across law enforcement agencies and between law enforcement and industry, to improve the sharing of information relating to the risk of corrupt PEPs. This information will be analysed in conjunction with SARs and international intelligence sources.

— Improved intelligence should strengthen knowledge of the sectors, products, services and countries at highest risk from attempts to launder proceeds of corruption by PEPs.

**Objective 2: To Optimise PEPs Suspicious Activity Reports (SARs)**

— SOCA is dedicated to continually improving the SARs regime. As part of this there is a focus to specifically optimise the quality of reporting on PEPs-related suspicion through improved feedback to reporting sectors. SARs which include a full explanation of the grounds for suspicion enable law enforcement to prioritise resources efficiently and to continue to build understanding of PEPs risks.

— It is widely recognised that identification of suspicious PEPs is a challenge for reporting entities. SOCA will work with supervisors and sector representatives in order to develop sector specific messages to facilitate identification, such as trends, warning signs and indicators.

The Government does not intend to compile a universal list of PEPs as a risk-based approach to identification offers a more targeted, effective and sustainable approach.

**Objective 3: To Maximise the Recovery of Stolen Assets in the UK**

— The Government is pursuing opportunities for increasing the Metropolitan Police’s investigation capacity and to enable the CPS to take further action against those who seek to hide the proceeds of corruption in the UK.

— The UK is leading a project within the FATF to identify the obstacles to cross-border confiscation and asset recovery. This is closely linked to the work being carried out through the World Bank’s Stolen Asset Recovery (STAR) initiative.\(^{117}\)

— The NPIA chairs the International Criminal Finances Working group to identify obstacles to cross border financial investigation and asset recovery. This identifies capacity building of AML regimes overseas as key to support international financial investigations. DFID is also supporting the International Centre for Asset Recovery to support developing countries develop capacity in this area.

**Objective 4: To Maintain an Effective and Proportionate Legal and Regulatory Environment**

— The Government continually seeks to improve the regime. In line with this, the UK is conducting a review of the effectiveness and impact of the Money Laundering Regulations 2007, which includes consideration of the risk-based approach and measures relating to PEPs.

— The Government also regularly engages with a range of partners and stakeholders on further enhancements to UK defences. For example, the Money Laundering Advisory Committee (MLAC), chaired by Home Office and HM Treasury, includes AML supervisors, industry representatives and law enforcement agencies. MLAC works to ensure that AML measures are effective and proportionate. The AML Supervisors’ Forum, comprising the 28 UK money laundering supervisors, also meets quarterly. This aims to spread best practice between supervisors, and to highlight general and industry specific risks and trends.

— Identifying innovative approaches including use of visa bans and civil action.

Government activities to achieve the objectives above are co-ordinated via the PEPs Strategic Group, a cross Whitehall stakeholder forum including law enforcement agencies and the FSA. The members of this group and their roles specifically relating to PEPs anti-money laundering are described in the Appendix.

**Roles and Responsibilities of Government Departments and Key Public Sector Bodies Relating to PEPs Anti-Money Laundering**

These organisations are members of the PEPs Strategic Group.

\(^{117}\) The Stolen Asset Recovery Initiative—known as StAR—is a joint initiative by the World Bank and United Nations Office on Drugs and Crime (UNODC). StAR’s objective is to reduce barriers to asset recovery and thereby encourage and facilitate more systematic and timely return of stolen assets.
(a) Key policy stakeholders

Her Majesty’s Treasury

HM Treasury oversees the UK’s anti-money laundering strategy and is responsible for implementing AML Regulations. Treasury and Home Office co-chair the Money Laundering Advisory Committee (MLAC), a high level strategic forum of Government, industry and law enforcement representatives. Treasury liaises directly with AML supervisors via its Supervisors’ Forum. Treasury also leads the UK delegation to meetings of the FATF and works within the FATF and FATF-style regional bodies to encourage all countries to effectively implement international standards on anti-money laundering.

www.hm-treasury.gov.uk

Department for International Development (DFID)

DFID manages Britain’s aid to poor countries to reduce global poverty. It works to maximise the impact of aid, including helping build effective and accountable states. As lead department for UNCAC, DFID is responsible for ensuring that the UK’s international commitments are fulfilled. DFID therefore acts as the Secretariat for the PEPs Strategic Group, and promotes co-ordinated action amongst its members.

www.dfid.gov.uk

Home Office

The Home Office is the lead department for primary legislation such as the Proceeds of Crime Act. Treasury and Home Office co-chair the Money Laundering Advisory Committee (MLAC), a high level strategic forum of Government, industry and law enforcement representatives.

www.homeoffice.gov.uk

(b) Key operational stakeholders

Serious Organised Crime Agency (SOCA), UK Financial Intelligence Unit (UK FIU)

SOCA is responsible for management of the SARs regime, including issuing feedback on SARs to reporting entities. The FIU gets over 200,000 SARs every year, which are processed and disseminated to other law enforcement agencies.

SOCA liaises with AML supervisors via the Supervisors’ Forum (chaired by HM Treasury). SOCA delivers direct feedback to reporting entities via the SARs annual report, intelligence alerts and mainstream communication under the “Payback” banner. The International and PEPs Unit within the FIU liaises with international FIUs via the Egmont Group.

SOCA also investigates some international asset recovery cases, depending on the source of intelligence and predicate offence. Most PEPs related investigations are led by the PoCU.

www.soca.gov.uk

Metropolitan Police Service, Proceeds of Corruption Unit (PoCU)

PoCU was established in 2006 to combat money laundering in the UK by PEPs and their associates. Investigations are driven by PEPs-related SARs from SOCA and other intelligence.

PoCU investigations have identified activity common to different cases including the use of regulated professions.

PoCU conducts parallel investigations with the jurisdiction where the offence(s) occurred and with other jurisdictions that may have been used to hide the origins of corrupt assets. This includes providing advice and support to “victim” jurisdictions.

PoCU is part of the International Corruption Group, part-funded by DFID, which also includes the City of London Overseas Anti-Corruption Unit (OACU). OACU focuses on foreign bribery by UK businesses and nationals.

www.met.police.uk

Crown Prosecution Service (CPS)

CPS is responsible for public prosecution of people charged with criminal offences in England and Wales. A team in the Central Confiscation Unit works on overseas corruption cases. International Policy Unit works on capacity building overseas.

www.cps.gov.uk
### Additional members of the PEPs Strategic Group

<table>
<thead>
<tr>
<th><strong>Department for Business, Innovation and Skills (BIS, formerly BERR), Anti-Corruption Unit</strong>&lt;br&gt;<strong><a href="http://www.berr.gov.uk">www.berr.gov.uk</a> (redirect)</strong></th>
<th>The Anti-Corruption Unit (ACU) provides guidance to UK business on bribery law and in managing the risks of international corruption, working with UKTI on country-specific issues. It promotes best practice standards for avoiding bribery and support Government procedures to safeguard public money from being tainted by contact with international corruption. Internationally, the ACU represents the UK at the OECD Working Group on Bribery and supports DFID in taking forward the UN Convention Against Corruption. BIS ACU also supports the Ministerial Anti-Corruption Champion to oversee all cross government anti-corruption initiatives.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Her Majesty's Revenue and Customs (HMRC)</strong>&lt;br&gt;<strong><a href="http://www.hmrc.gov.uk">www.hmrc.gov.uk</a></strong></td>
<td>HMRC has a dual role: (a) as supervisor under the MLR 2007: to register and maximise compliance for money service businesses, high value dealers and other defined businesses; (b) as a law enforcement agency to investigate and take action against businesses failing to comply with the regulations.</td>
</tr>
<tr>
<td><strong>City of London Overseas Anti-Corruption Unit (OACU)</strong>&lt;br&gt;<strong><a href="http://www.cityoflondon.police.uk">www.cityoflondon.police.uk</a></strong></td>
<td>OACU was established to investigate foreign bribery by UK businesses and nationals. Funded by DFID, OACU works closely with SFO and international counterparts.</td>
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<tr>
<td><strong>Serious Fraud Office (SFO)</strong>&lt;br&gt;<strong><a href="http://www.sfo.gov.uk/">http://www.sfo.gov.uk/</a></strong></td>
<td>SFO is the focal point for receiving any allegations of corruption offences by UK nationals or incorporated bodies overseas. It maintains a register for overseas corruption cases. Holds information on financial pathways used by PEPs/intermediaries. SFO undertakes the investigation and Prosecution of Corruption and is assisted by and works closely with LEA’s both in the UK and Overseas. It works with the ACPO lead force on Corruption, City of London OACU, other Police forces (including Ministry of Defence police), HMRC and other government departments in combating Corruption both overseas and domestically.</td>
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<tr>
<td><strong>Foreign and Commonwealth Office (FCO)</strong>&lt;br&gt;<strong><a href="http://www.fco.gov.uk/">http://www.fco.gov.uk/</a></strong></td>
<td>The FCO has a number of priorities of relevance for asset recovery work. These include ensuring the good governance of the UK’s Overseas Territories. The FCO can also provide local knowledge and contextual information on political situations within countries and regions.</td>
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<tr>
<td><strong>UK Central Authority (UKCA)</strong>&lt;br&gt;<strong><a href="http://police.homeoffice.gov.uk/operational-policing/mutual-legal-assistance/?version=1">http://police.homeoffice.gov.uk/operational-policing/mutual-legal-assistance/?version=1</a></strong></td>
<td>The UKCA leads on Mutual Legal Assistance (MLA) policy and legislation for the United Kingdom. It is also responsible for negotiation and implementation of treaties and other international agreements in the field of MLA. The UKCA is responsible for MLA casework in relation to England &amp; Wales and Northern Ireland. UKCA determines whether assistance requested by overseas authorities should be provided and whether it is appropriate for requests for assistance in restraint and confiscation cases should be forwarded overseas. Requests for assistance relating to Scotland are handled by the Crown Office.</td>
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<tr>
<td><strong>Financial Services Authority (FSA)</strong>&lt;br&gt;<strong><a href="http://www.fsa.gov.uk">www.fsa.gov.uk</a></strong></td>
<td>The Financial Services Authority (FSA) is the regulatory body for the financial sector in the UK. Its statutory objectives include to promote confidence in the UK financial system and to reduce the scope for regulated firms being used to further financial crime. It supervises firms for compliance with their legal and regulatory obligations, including those related to PEPs.</td>
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Supplementary written evidence submitted by The Department for International Development (DFID)

OFFICIAL DEVELOPMENT ASSISTANCE

Official Development Assistance (ODA) refers to flows of funds to countries and territories on the OECD Development Assistance Committee List of official development assistance recipients (available at www.oecd.org/dac/stats/daclist) and to multilateral development institutions, which are provided by official agencies (including state and local governments, or by their executive agencies) and each transaction of which is:

— administered with the promotion of the economic development and welfare of countries on the OECD Development Assistance Committee list of official development assistance recipients as its main objective; and

— concessional in character and conveys a grant element of at least 25% (calculated at a rate of discount of 10%).

ODA is based on flows of funds and flows can only be recorded once. If DFID provides funding to HMRC to deliver technical assistance to developing countries, DFID will assess whether the funding meets the ODA definition and, if so, will include the funds in its report of total ODA. It would not be recorded as ODA by HMRC.

If DFID were to provide funding to a partner government and that government were then to use those funds to engage HMRC to provide services, the provision of the services by HMRC would not count as ODA, but the original provision of the funds by DFID would count as ODA (if the ODA conditions were met).

If HMRC were to receive funding from other development agencies in order to provide services to developing countries, we would expect that the funding would be reported as ODA by those agencies (if it met the ODA criteria), but would not be reported as ODA by HMRC (to avoid double counting).

Where HMRC provides assistance to developing countries from its own resources, that could count as ODA if the criteria for ODA eligibility are met. However, most assistance provided by HMRC to help build capacity in developing countries is funded by others.

DFID prepares the statistics for UK ODA, including ODA provided through other government departments. Over the last three years, these statistics have not included any ODA provided by HMRC, although UK ODA includes an amount of Gift Aid which is deemed to be ODA eligible and Gift Aid is administered by HMRC.

June 2012

Written evidence submitted by Extractive Industries Transparency Initiative (EITI)

INTERNATIONAL SECRETARIAT OSLO

SUMMARY

3.5 billion people—half of the planet’s inhabitants/world’s population—live in countries whose economies are dominated by natural resources. The governments of most of these countries do not raise significant tax revenues directly from their own citizens. Partly because of this, these countries tend to be more repressive, corrupt and badly-managed. Ensuring the transparency of government revenues from natural resources is the first step in addressing this “resource curse”. The second step is creating a platform to monitor and discuss with citizens how the government manages the sector, including raising a debate about the role, level and use of tax and other government incomes from mining, oil, gas and other extractive industries.

The EITI is a global standard that establishes transparency and accountability in resource-rich countries:

— **Transparency**: through the reporting, verification and public disclosure of company payments and government receipts from oil, gas, mining and other natural resources;

— **Accountability**: through a multi-stakeholder group of government, companies and civil society and vibrant public dialogue.

35 countries on five continents—from Afghanistan to Zambia—are implementing this standard.

There is emerging anecdotal evidence that the EITI process increases income from the extractives sector. The data from EITI reports also create opportunities to compare tax levels and revenues for the sector across countries.

The UK government has pledged to “lead by example and contribute to advancing open government in other countries.” (Open Government Partnership Declaration, 2011). The Department for International Development (DFID) is helping promote better governance of resource-rich economies while also supporting the EITI internationally and in many resource-rich countries. However, the biggest impact would come if the UK government were to join fellow oil majors such as the US and Norway in implementing the EITI, thereby
keeping its pledge to “lead by example” while adding great weight to the EITI as a truly global standard for transparency and accountability of tax and revenue. Until that happens, the UK’s absence will remain conspicuous and inconsistent with its policy of open government.

**Brief Introduction to the EITI**

The EITI was launched by the UK government in 2002 to promote trust and to reduce corruption and poverty in resource-rich countries. It is a standard with two key elements:

1. **EITI report**—Governments disclose their revenues from oil, gas and mining. Meanwhile, oil, gas and mining companies disclose their payments to governments in bonuses, royalties, taxes and payments-in-kind. A third-party entity reconciles these two reporting streams, making efforts to clarify any discrepancies;

2. **Multi-stakeholder group**—oversees the process and builds a platform for the key stakeholders to discuss the information and management of the sector more widely. This group also ensures that the EITI is inclusive and collaborative in each country.

35 countries across all continents are implementing the standard. These include Afghanistan, Democratic Republic of Congo, Indonesia, Iraq, Nigeria, Tanzania, and Zambia—which span the range of natural resource-rich countries and include some of the largest oil and mineral producing countries in the world. Twenty-one of the implementing countries are African. In September 2011, President Obama committed the US to implement the EITI.

The EITI global standard is overseen by an international board on which the UK government serve. Companies like BP, Shell, Rio Tinto, AngloAmerican, institutional investors such as F&C Asset Management and Standard Life Investments and civil society organizations including the Publish What You Pay coalition and Global Witness also serve or have served on the Board, chaired by the Rt Hon Clare Short. A number of other British companies and institutional investors support the EITI.

The G8 has promoted the EITI for years and re-affirmed its support/backing in the 2011 Deauville Declaration, which called on “all countries” (ie emerging and developed economies) to join or support the EITI. The EITI has been endorsed by the G20 and the UN General Assembly. In October 2011, The Economist described the EITI as an “ingenious scheme... giving citizens a chance to see how much of (oil, gas and mining) payments actually end up in public coffers”.

In the UK, the EITI enjoys support across political parties, media groups, academics, faith groups, industry associations and NGOs. The UK government provides political, technical and financial support for EITI largely, but not exclusively, through DFID. The UK government is a founding member of the Open Government Partnership a multi-government initiative promoting “more transparent, effective and accountable governments—with institutions that empower citizens and are responsive to their aspirations”.

**Evidence**

Countries whose economies are dominated by resource extraction industries, tend to be more repressive, corrupt and badly-managed. This can be partly attributed to the replacement of tax from citizens with direct income from natural resource production. A multitude of academic studies and journalistic literature (eg, Collier, Sachs, Venables, etc) confirms that transparency of revenues to government is the first step in addressing the “resource curse”. Along with transparency must come accountability and a sound environment for debate about of the role, level and use of tax and other government incomes from the sector. As Clare Short said in a BBC World Debate filmed in Lusaka in August “All over the world there has been total secrecy about the contracts, about how much the production was, about how much they really pay to the government, how much the government receives. If there’s nothing to hide, let’s get all of this out in the open. Let the people know what it costs, how much is being produced, what proportion of profits are being paid in taxes.” (http://eiti.org/news-events/clare-short-bbc-world-debate-does-mining-benefit-africa).

The EITI’s two pillars seek to satisfy this necessary, but not sufficient, first step. There is emerging anecdotal evidence that the EITI process increases income from the extractives sector by building the capacity of tax collecting authorities, improving systems, and reducing opacity between line ministries and tax collecting authorities. Some EITI countries have seen a higher level of tax collection. For example, Ghana’s 2012 budget included increased corporate tax rates and changes to capital depreciation allowances, echoing recommendations in Ghana’s 2009 EITI report, which criticized low corporate tax payments and a high capital depreciation allowance of 80% for companies’ first year of operations. In 2010, the Zambian Government agreed a mining windfall tax with local operating mining companies using the EITI as a major forum for negotiation. After the first Nigeria EITI report, the Nigerian President, Umaru Musa Yar’Adua, said that the Nigerian EITI had “conducted studies that swelled government’s coffers by over $1 billion”. Its second report, showed financial discrepancies and outstanding payments totaling over US$5 billion for revenues generated by the sector in 2005 which, if the discrepancies alone were recovered could result in a far higher investment in the developmental sectors than the aid to that country.

The data from EITI reports also create opportunities to compare tax levels for the sector across countries. So Nigerian citizens can question why their government receives less for its oil than Norway despite similar
levels of production. The EITI publication *Extracting Data* brings together these cross-country comparisons: http://eiti.org/document/extracting-data.

Whilst the EITI does not directly address issues of tax evasion and avoidance in developing countries by private individuals and companies, it does reduce the space for opaque transactions. Nor does it directly tackle issues of capital flight, but it does create a more attractive investment climate as seen by correlations between EITI compliant countries and indices on corruption, doing business, and credit ratings. In 2010, Fitch upgraded Azerbaijan’s long-term foreign and local currency Issuer Default Ratings (IDRs) to “BBB-” from “BB+” following the declaration of Azerbaijan as EITI compliant. Liberia jumped Liberia 91 places on Transparency International’s Corruption Perceptions Index (CPI) two years after becoming EITI Compliant.

DFID is helping promote better governance of the extractive sector and is supporting the EITI internationally and in many developing countries. They are considering our recommendation that DFID support the establishment of a UN Panel of Experts or similar high-level body to increase the profile of better-managed natural resource sectors. At the country level, DFID’s technical assistance in countries like Nigeria and DRC have been critical TA for EITI implementation, and is support for implementation in Indonesia ensured that the EITI’s most populous country became an implementer in 2010. DFID’s work to support public financial management reforms across Africa and elsewhere, especially training tax and mining officials on reporting has been important in ensuring that EITI links well with wider governance reform processes.

However, there is more that can be done. It would amplify this policy if the UK were to implement the EITI itself. As well as serving domestic objectives for improving the management of UK public resources and revenues and building trust about the sector, this would help the UK promote extractive resources transparency as a global standard and allow developing countries an opportunity to compare and understand the UK tax regime in the extractive sector. Indeed, as the founder of the EITI and the Open Government Partnership, a major oil producer with many of the largest extractives companies listed on the FTSE, the UK government’s absence from the EITI is notable.

By implementing the EITI, the UK would help reinforce the EITI as the global standard for transparency in extractive industries. Countries like Angola, South Africa, Brazil, Sudan, Colombia, Uganda, Papua New Guinea, often question why they should implement the EITI if the UK is not willing to subscribe to the international standard *that it launched itself*. These are countries which do not respond to aid as a lever for better governance, yet are home to hundreds of millions of poor people and receive billions of pounds each year in resource revenues. They could benefit significantly from EITI implementation.

The US commitment to implement the EITI has highlighted the anomaly of the UK’s absence—with recent critical commentary in the *Daily Telegraph* and *Africa Confidential*. Canada and Australia are also under international and domestic pressure to implement the EITI.

Following the UK Government’s invitation for consultation on its open data initiative data.gov.uk, the EITI International Secretariat submitted a short paper urging the UK Government to follow the example of Norway, the United States and other countries, by committing to implement the EITI standard: http://eiti.org/news-events/international-secretariat-encourages-uk-implement-eiti-0.

The UK Government has committed “to being the most transparent government in the world”. A useful next step to fulfilling that commitment would be to implement its own transparency initiative.

*February 2012*

Written evidence submitted by the International Secretariat of the Tax Justice Network

**Scope of this Submission**

The terms of reference for the International Development Committee’s inquiry identify five key issues:

- How DFID can better support developing countries to improve revenue collection;
- How DFID can support developing countries to use the revenue base responsibly in order to improve service delivery and development outcomes;
- Tax evasion and avoidance in developing countries by private individuals and companies;
- How effective international efforts to promote tax disclosure and tax transparency are likely to be;
- Capital flight and its implications for developing countries.

This submission will focus on international efforts to curtail tax evasion through effective tax information exchange processes. It will argue that illicit financial flows from developing countries are motivated by varying factors, but tax evasion is almost always an outcome of such flows, and revenue losses to developing (and

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118 The Tax Justice Network is a global network of financial/legal specialists, development NGOs, faith movements, trade unions and others with a shared interest in tackling harmful tax practices and promoting just tax policies. The network has researchers and/or active partners in over 80 countries in six continents. The network has regional secretariats in Africa, Asia, Australia, Europe, and North and South America. Its international secretariat is located in London.
developed) countries run to many billions of pounds annually. The arising revenue losses are likely to exceed the value of aid flows by a significant margin.

The most effective means of deterring tax evasion involving offshore structures, typically located in secrecy jurisdictions, is through a system of multilateral automatic information exchange treaties. The European Union already has such a system in place (in the form of the 2005 Savings Tax Directive) and is pushing for various reforms to strengthen information exchange relating to legal entities such as trusts and offshore companies, and to broaden the types of income covered. TJN proposes that a variant of automatic tax information exchange can be adapted to meet the needs of developing countries with democratic and stable governments. Even a simplified approach to exchanging basic information would provide a “smoking gun” to trigger investigations.

Adopting effective tax information exchange processes would deter and significantly curtail tax evasion. DFID might usefully take a part in supporting pilot projects with selected developing country partners to adopt automatic information exchange and build capacity to effectively handle the arising data flows.

**Tax Evasion: Reaching Epidemic Levels**

For obvious reasons it is hard to produce reliable estimates of tax evasion, either nationally, regionally or globally. In November 2011 the Tax Justice Network published estimates based on shadow economy data produced by the World Bank giving a global tax evasion figure of US$1 trillion annually. Only a small handful of countries (accounting for less than 2% of global GDP) were not included in this estimate.

The scale of tax evasion varies from country to country and from region to region. Africa, for example, is estimated to lose tax revenues amounting to approximately US$779 billion annually, representing 98% of total healthcare expenditures for that continent. In the case of Latin America the figures were US$376 billion and 139% respectively. Analysed at country level it is clear that developing countries are significantly more vulnerable to tax evasion than the majority of developed countries (see table starting on p.17 of TJN’s report listed in footnote 101 below). At the most extreme is Bolivia, with a shadow economy estimated at 66% of total GDP, where tax losses due to evasion are over four times the annual healthcare budget.

Tax evasion arises at both the domestic level and from non-declaration of incomes and capital gains on assets held offshore. The ratios vary significantly from country to country, and the available data on cross-border financial and non-financial investments and banking assets are filled with gaps. Estimates for Latin America, for example, suggest that over one-half of all financial assets of high net-worth individuals on that continent are held offshore, almost entirely evading taxes. No comparable figure is available for Africa, but most specialists conclude that the figure is at least as high as that for Latin America, if not higher.

The scale of illicit outflows from developing countries has been estimated at between US$858 billion to US$1,060 billion a year. The large majority of these outflows are destined for banks and financial institutions located in developed countries. In May 2010, Global Financial Integrity, a Washington-based research advocacy group, used data from the Bank for International Settlement to estimate that developed country banks absorb between 56 to 76% (depending on source country) of cash flowing out of developing countries.

It is clearly not practicable to accurately estimate what proportion of the income from assets held offshore is not declared for tax purposes in the country of residence of the ultimate beneficial owner. Through extensive interviews with banking professionals and other wealth managers, TJN has estimated that the vast majority, exceeding 90%, of such income is undeclared. The scale of the problem is clearly immense. In 2005, TJN estimated the global volume of personal wealth of high net-worth individuals held offshore at US$11.500 billion (TIN, 2005) The Price of Offshore). The potential tax revenue losses arising from this offshore wealth holdings were conservatively estimated at that time at US$255 billion annually. We stress this is a conservative estimate for two reasons: first, it was not possible at that time to estimate offshore wealth holdings of African HNWIs, and therefore the entire continent was not included in our estimate. Second, the figure relates only to HNWIs (super rich individuals) and therefore excludes a wide category of other users of offshore (the proverbial Belgian dentists with deposits squirrelled away in Luxembourg). Since we published The Price of Offshore in 2005, new data has emerged concerning financial outflows from Africa. In April 2008 James Boyce and Léonce Ndikumana of the University of Massachusetts, Amherst, published fresh research which estimated that capital flight from 40 sub-Saharan African countries between 1970 to 2004 stood at US$8607 billion in 2004 dollars (including interest earnings), compared to a total of US$227 billion external debt owed by those countries in 2004. An even more recent update has estimated the accumulated capital losses of 37 Sub-Saharan countries between 1970 and 2008 at US$944 billion. This sum vastly exceeds the volume of aid flows over that period.

The Boyce/Ndikumana estimates reveal that Sub-Saharan Africa is a net creditor to the rest of the world in the sense that external assets, measured by the stock of capital flight, exceed external liabilities in the form of external debt. As Boyce and Ndikumana comment: “The difference is that while the assets are in private hands, the liabilities are the public debts of African governments.” They further note: “The real counterpart

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of many assets on the balance sheets of creditor banks is private deposits in many of the same banks by individuals belonging to Africa’s political and economic elites.”

Since we published The Price of Offshore the scale of the problem appears to have increased. Recent unpublished research suggest that the sums being shifted offshore have accelerated in the past few years, partly in response to financial crises in many countries. One US expert has suggested that the stock of private wealth now held offshore may well exceed $US 20,000 billion.122 TJN has commissioned further research from this expert and we hope to be able to publish a revised estimate in quarter 2, 2012. What is indisputable, however, is that the sums involved are huge, tax evasion on cross-border wealth holdings is endemic, and developing countries are losing tax revenues on a massive scale.

What can be done to curtail cross-border tax evasion?

In the absence of effective exchange of information between tax authorities, the cost of enforcing tax compliance on foreign source income is prohibitive, especially for a revenue authority in a poorer country with limited capacity to mount time-consuming and expensive external investigations. The risk to tax evaders of being detected can be reduced significantly by using complex multi-jurisdiction structures involving offshore companies, offshore trusts, offshore bank accounts and similar legal devices structured through secrecy jurisdictions that provide legalised secrecy arrangements combined with weak or non-existent financial disclosure requirements. Such structures are the norm for most HNWIs placing assets offshore and, in the absence of cross-border cooperation between national tax authorities, tax evaders can be confident that the risk of detection, successful investigation and subsequent prosecution is low to infinitesimal.

The antidote to this generalised view that tax evasion using offshore structures is a relatively risk-free crime lies with reinforcing national sovereignty on tax matters through enhanced international cooperation and greater transparency of ultimate beneficial ownership of offshore legal structures. This is not rocket science. Information exchange processes have been negotiated in some double taxation agreements between countries, and bilateral tax information exchange agreements exist between some developed countries and some offshore secrecy jurisdictions. Since 2005, member states of the European Union have had a multilateral agreement for automatic exchange of tax information (known as the Savings Tax Directive), which, although deficient in some technical respects, represents the appropriate standard to which other regions should aspire. The United States has enacted the Foreign Account Tax Compliance Act (FATCA) which requires foreign registered banks to automatically share information about US citizens operating offshore accounts.

The advantage that the European Union model holds over alternative systems of tax information exchange lies with the exchange happening on a multilateral and automatic basis. A resident of country A opens an account in country B and the bank branch where the account is opened automatically informs the tax authorities of country B who in turn automatically shares that information (using suitable encryption technology to protect confidentiality) with the tax authorities of country A. Extended to cover all types of income or capital gains, and to include legal as well as natural persons (e.g. companies, trusts and foundations), this approach has the great advantage of having a strong deterrent effect on tax evasion. It is also far cheaper than the alternative approach to tax information exchange which involves detection, investigation, and a formal request for cooperation from the courts of the treaty partner through what is known as the “on request” model for tax information exchange. This is the model currently promoted for over a decade by the Organisation for Economic Cooperation and Development and which is widely seen as cumbersome and inadequate.

To date no developing countries have provision with other countries for automatic exchange of tax information. The United Nations Committee of Experts on International Cooperation on Tax Matters has concluded that a multilateral tax treaty solution would be beneficial to developing countries and further proposed, in 2009, that automatic information exchange would be the preferred standard:

“… the extent of administrative burden could be reduced if information were provided automatically by financial institutions … Automatic provision of information could substantially benefit developing countries since it would provide them with information even in the absence of an investigation.”

This emphasis on using automatic information exchange as the effective international standard for curtailing tax evasion in developing countries was given further political momentum at the G-20 Summit in November 2011, when India’s Prime Minister Manmohan Singh said:

“The G20 countries should take the lead in agreeing to automatic exchange of tax related information with each other, irrespective of artificial distinctions such as past or present, for tax evasion or tax fraud, in the spirit of our London Summit that ‘the era of bank secrecy is over’.”123

TJN supports this position. We view automatic information exchange as the appropriate model for developing countries to adopt. We argue that automatic exchange has clear advantages over the “on request” approach mentioned above in so far as it has a stronger deterrent effect—and will therefore work faster to shape a culture of tax compliance—and it is vastly easier and cheaper to implement.

Developing countries have already demonstrated their capacity to handle online cross-border automatic information exchange for security purposes (the use of passport swipe technologies at border controls has

122 Jim Henry of Sag Harbor Consulting in a draft paper given at a research workshop at Essex University, 5th-6th July 2011
become a global norm), and there is no reason why tax authorities in developing countries should not be able to rapidly adopt technologies to make effective use of tax related information. Above all we would stress that the very threat of effective information exchange would go a long way to changing the attitudes of persistent abusers.

How would we go about the process of extending AIE to developing country partners? Larger and politically more powerful countries might initially be attracted to the unilateral AIE approach adopted by the United States through its Foreign Account Tax Compliance Act (FATCA).124 Alternately, such countries might want to work with regional partners to emulate the EU’s Savings Tax Directive (in its amended form once this has been adopted) and extend it to secrecy jurisdictions. Another alternative would be to participate in the 1988 joint Convention on Mutual Administrative Assistance in Tax Matters (OECD and Council of Europe), which since April 2010 has included a protocol that opens participation to non-OECD and non-European states.

Developing countries with limited tax administration resources would probably benefit from being able to use a more basic form of automatic information exchange involving exchange of limited information (eg citizen A, ordinarily resident at such-and-such address, has opened an offshore bank account at the following bank branch in jurisdiction X). Even this simple approach to tax information exchange would be sufficient to provide a “smoking gun” for investigations if and when it subsequently becomes apparent that tax evasion might be happening. For such countries it would be helpful to provide technical support with negotiating tax information exchange agreements with offshore jurisdictions and with developing capacity to effectively use such agreements to gather the evidence required for a successful prosecution.

Concerns about information leaks from revenue offices are sometimes exaggerated, but steps can be taken to provide secure channels for tax information exchange and restrict access to data records to protect confidentiality. In some circumstances it might be appropriate to not share information with countries where human rights are not observed or are violated.

**Concluding Remarks**

Effective tax information exchange could significantly reduce and deter tax evasion, and by curtailing illicit financial flows it could also achieve some of the macro-economic rebalancing required for the global economy. The current situation, in which the majority of developing countries are not party to effective tax information exchange processes, has trapped them into a vicious circle of capital flight, under-investment, economic volatility, and over-reliance on external debt. The other side of this particular coin is excessive inflows of hot money into speculative markets, harmful currency appreciation (as happened to the Swiss franc in 2011), falling aggregate demand and rising inequality.

Considerable progress has been made in the past five years towards creating information sharing processes between developed countries and cooperating secrecy jurisdictions. Developing countries generally suffer from larger illicit financial outflows and consequently higher levels of offshore tax evasion, but by and large have not benefited from the recent progress. Supporting such countries with creating effective information exchange processes would rapidly enhance tax compliance and reduce their revenue losses. Accompanied by other transparency-enhancing measures, eg requirements for disclosure of corporate ownership information, and a country-by-country financial reporting standard, effective tax information exchange would greatly assist many developing countries with building sustainable tax revenues.

30 January 2012

**Written evidence submitted by Glencore International Plc**

1. **Introduction**

   1.1 Glencore International plc, headquartered in Baar, Switzerland, is one of the world’s leading integrated producers and marketers of commodities. Glencore has worldwide activities in the production, sourcing, processing, refining, transporting, storage, financing and supply of metals and minerals, energy products and agricultural products.

   1.2. Glencore’s industrial operations directly or indirectly employ over 54,800 people in 30 countries. Over 2,700 people work in Glencore’s marketing operations in 50 offices in 40 countries. Glencore’s oil department employs around 400 people in London.

   1.3. Glencore’s customers around the world are active in a wide range of industries, such as automotive, oil, power generation, steel production and food processing. They rely upon Glencore’s established global network for the supply of metals and minerals, energy products and agricultural products. These commodities either originate from Glencore’s own production assets or are sourced from third parties. Glencore also provides financing, logistics and other supply chain services to producers and consumers of commodities.

   1.4. Glencore owns and operates mines and other industrial facilities throughout the world, including in developing countries across Africa, Asia and Latin America. As a result of these investments Glencore has

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gained significant knowledge and experience in building sustainable businesses in collaboration with local communities and national governments.

1.5. Glencore is listed on the London Stock Exchange and is a constituent of the FTSE 100, with a secondary listing on the Stock Exchange of Hong Kong.

2. Conducting Business in Developing Countries

2.1 As a leading natural resources company, and investor in the developing world, our presence and business activity serves to promote development. Our investments and the jobs, entrepreneurial opportunities and Government revenues they generate contribute to local, regional and national economic well-being and growth.

2.2 Working in the developing world entails particular challenges and responsibilities. Glencore puts sustainability at the top of its agenda and it is an integral part of everything we do.

2.3 For this reason, we have put a corporate sustainability framework in place to balance social, environmental, ethical and commercial interests at every level of our group. This framework is called Glencore Corporate Practice, or GCP. We have designed and implemented the GCP to meet internationally recognised, sector-specific, good practice standards.

2.4 The Committee is undertaking an inquiry into tax in developing countries and as part of that inquiry is using Zambia as a case study. One area of focus is whether large investors in countries such as Zambia are contributing sufficiently to Government revenues and to the development of society more broadly.

2.5 For Glencore, our main priorities in resource-holding countries are to invest for the long run, conduct our operations responsibly, provide good quality jobs and indirect economic opportunities, and generate taxes, royalties and other dues to Governments. In addition we make substantial voluntary contributions to improve the lives of the people in the communities where we operate. Our commitment to continual improvement of environmental protection and safety is also an integral part of our operations.

3. Glencore’s Operations in Zambia

3.1 Glencore owns 73.1% of Mopani Copper Mines plc. The other shareholders are First Quantum (16.9%) and the Zambian government (10%).

3.2 Mopani is an integrated copper and cobalt producer located in the Copperbelt Province of Zambia. Mopani’s operations consist of four underground mines, a concentrator and a cobalt plant at Nkana in the town of Kitwe and an underground mine, concentrator, smelter and refinery in the town of Mufulira.

3.3 Mining began at Nkana in 1931. The town of Kitwe started as a railway station to support the growing copper operations on the Copperbelt. Mining began at Mufulira in 1933 and the town grew around the mine.

3.4 Glencore acquired its shareholding in Mopani through a competitive tender as part of a general privatisation, supported by the World Bank, of copper mining assets in 2000. Following years of under-investment prior to privatisation, the business was in a parlous financial and physical condition and its 10,000 jobs were at risk. Safety performance was poor. In addition the Mufulira smelter had been emitting sulphur dioxide unconstrained since it was built in 1937.

3.5 Since privatisation the shareholders have and continue to make a very substantial contribution to local, regional and national economic well-being and growth.

3.6 The corporate shareholders have committed $2 billion in investment since privatisation to redevelop and expand Mopani’s operations. The Government is carried, which means it does not contribute to this investment whilst benefiting from the results. This investment has secured the long-term future of the business, increased employment and production, and improved safety. The shareholders will continue to invest at high levels going forward as the cost and challenges of mining at deep underground levels increases.

3.7 Some 16,300 people work at Mopani today (8,300 employees and 8,000 contractors). We estimate that each employee has an average of eight dependents. Over 6,000 new jobs have been created since privatisation, Mining is the highest paying sector in Zambia. The salary of the most junior employees is $508 per month (K2,620,000) compared to the national minimum wage of $81 per month (K419,000). Mopani believes it is the second highest payer of its most junior employees amongst the mining companies in Zambia.

3.8 Mopani spent $775 million on contractor and supplier companies in 2011. Of this, 82% of the total was spent in Zambia, 69% of the total in the Copperbelt and 61% of the total in Mufulira and Kitwe.

3.9 Production has increased from 135 thousand tonnes of copper and two thousand tonnes of cobalt in 2003 to 204 thousand tonnes of copper and nine thousand tonnes of cobalt in 2011.

3.10 Mopani has paid $425.1 million in taxes, royalties and other dues to Government since privatisation.

3.11 Taxes, royalties and other dues to Government as declared above include Pay As You Earn (PAYE), Mineral Royalties and Import Customs & Excise Duty. Mopani also pays Import VAT & Reverse VAT as well as property rates on a monthly basis.
3.12 In 2011, due to the increases in the number of employees, import duties on capital goods and mineral royalties, Mopani paid $104 million (K508 billion).

3.13 With the continued capital investment and the doubling of the royalty tax in the current year it is expected that this amount will be higher again in 2012 and into the future.

3.14 From April 2012, the royalty tax that companies extracting base metals, including copper, pay to the government doubled from 3% to 6%. The royalty is calculated using the London Metal Exchange copper and cobalt prices and is based on revenue rather than profits. There were a number of meetings held between the Government and the Zambian Chamber of Mines regarding the royalty increase when it was proposed. The industry expressed concerns it may discourage investment and reduce the overall Government take in the long-term, however the Government decided to implement the new rate.

3.15 The effective tax rate for Mopani in 2012 will be approximately 52%. This estimate takes account of the doubling of the royalty tax during the year and is based on budgeted sales.

3.16 The tax system in Zambia allows for a 100% tax deduction against corporate Income Tax in the year in which capital investment on mining and processing is spent. This results in no direct Income Tax being paid in the years in which large investments are made and creates tax losses/credits that are carried forward to be used against taxable income in future years.

3.17 Due to the high level of capital investment undertaken by Mopani at privatisation, and since, to continue the operations and address a number of legacy issues, Mopani currently has Income Tax losses/credits available for offset. The level of capital investment in the future will also affect the amount of Income Tax payable by Mopani in the coming years.

3.18 These capital allowances are similar to those included in the tax legislation of other African countries such as South Africa, the Democratic Republic of Congo and Namibia and other countries outside Africa including Australia, Japan and the United States. The tax allowances encourage capital investment thereby supporting economic development.

3.19 Due to the continuous investment required in keeping Mopani running as well as upgrading the mines and processing facilities, to date the corporate shareholders have not received any dividends as they continue to invest in Mopani’s long-term future. This investment includes addressing legacy issues such as the emission of sulphur dioxide at Mufulira.

3.20 Currently about half of all sulphur dioxide emissions are captured and this has been enabled by phased investments in a modern smelting technology that has provision for gas capture. The final phase of a $145 million project to capture 97% of emissions, a world-class performance, has been fast-tracked and will be complete by the end of 2013, some 18 months ahead of the deadline set by the Government at privatisation.

3.21 Exposure to elevated levels of sulphur dioxide can cause impairment of respiratory function and aggravation of existing cardiovascular disease and respiratory disease (especially bronchitis). Workers at the Mufulira smelter are provided respirators as part of their Personal Protective Equipment for this reason.

3.22 The Mufulira smelter is one of just three copper smelters in Zambia. It plays an important role in ensuring the economic viability of other operators’ mines by processing their concentrate into metal in return for a small tolling fee. About half of the smelter’s metal output is generated in this way.

4. Mopani’s Voluntary Contributions in Community Development

4.1 In addition to creating jobs and generating revenue for Government, Mopani makes further contributions voluntarily to improve living standards in the communities in which it operates.

4.2 These voluntary contributions are made based on local needs and in line with the priorities of the Government for the development of the country, which include health, education and infrastructure development.

4.3 Mopani’s voluntary contributions total over $140 million since privatisation and have averaged $15 million per annum on on-going projects in recent years. Spending in 2011 was substantially higher due to additional spending on sanitation and road projects.

4.4 Mopani operates two major hospitals (treating 120,000 patients per annum) and seven township clinics (130,000 patients treated per annum). Both hospitals have attained the highest ISO:9001 standard. Spending on health has increased by 300% from 2002 to 2011.

4.5 Over 14,000 people are on HIV/AIDS antiretrovirals and care funded by Mopani, 85% of them non-Mopani employees or their dependents.

4.6 A malaria reduction programme implemented since October 2000 has reduced incidence from the national average of 216 per 1,000 to fewer than 20 per 1,000 in Mopani’s catchment area. An average of $650,000 is spent annually on this programme which included indoor residual spraying of 30,000 households in 2011.
4.7 Mopani operates two primary schools and two secondary schools. Children are enrolled on merit and about half are from families in which no one works at Mopani. Some 2,000 children are currently enrolled with a further 700 on the waiting list. These schools are amongst the very best in the country and have achieved a 100% exam pass rate since Mopani has operated them.

4.8 During 2011 Mopani spent $4.5 million building 1,500 individual sanitation units in a residential area in Kitwe where households shared communal facilities which caused disease. A second phase of this project has begun. Mopani also began a $10.5 million project to repair two key roads in the Copperbelt which are arteries of economic growth. This project will be completed in 2012.

4.9 Mopani has also set up a cooperative farm for retired employees who wish to continue to be active economically. This cooperative farm now operates independently and Mopani is in discussions with the local authority to acquire land to build a second similar project to replicate its success.

4.10 Around 50% of Mufulira town’s total water requirements are met by Mopani, which supplies the water free of charge to the local utility. The proportion supplied by Mopani will significantly increase on commissioning of new water pipeline from the nearby Kafue river. This has been extended to Kankoyo township, where residents all have access to potable water, courtesy of a newly installed pipeline.

5. Draft Tax Audit

5.1 Mopani is audited every year by Deloitte and its accounts have always been given a clean bill of health. As a public company, Mopani’s accounts are lodged with Securities and Exchange Commission as well as the Companies Registry in Lusaka and are publicly available.

5.2 Mopani is convinced that the taxes, royalties and other dues to the Government have always been calculated and paid in the proper manner in line with the applicable legislation.

5.3 In February 2011 a draft provisional report prepared by advisers to the Zambia Revenue Authority was unofficially circulated in Zambia. The report was described as “confidential, preliminary and an incomplete draft” by the Zambia Revenue Authority.

5.4 The draft provisional report contained fundamental factual errors and both Mopani and Glencore have publicly refuted its ‘conclusions’ on numerous occasions.

5.5 The most fundamental flaw incorporated by the authors of the report was the inclusion of toll treated material in the volumes used to calculate Mopani’s average sales price. Ownership of the toll material does not transfer to Mopani which only receives a treatment and refining charge and returns the final product of copper cathode to the contracted third party.

5.6 In addition, the authors alleged that Mopani manipulated copper prices to engage in transfer pricing in favour of Glencore, when in reality all copper is sold on arms-length terms basis prevailing London Metal Exchange prices. The London Metal Exchange is a transparent forum for trade that provides worldwide reference pricing for metals. Mopani’s copper brand, MCM, is one of the most historic copper brands approved for delivery against the London Metal Exchange copper contract. Mopani also undertakes production hedging on the London Metal Exchange, a standard practise within the mining industry, and the results of these hedging activities were not taken into account by the authors during their desktop review.

5.7 The authors also alleged that gold and silver hedges were improperly recorded and used to impact taxable income. In fact any hedges recorded were entered into to offset physical price exposure and the net financial impact on Mopani’s taxable income was zero. They further alleged that operating costs rose for unexplained reasons without making any attempt to clarify these facts, for instance they used general inflation rates for their calculations despite mining cost inflation exceeding the general inflation rate and despite Mopani’s labour, and fuel costs having risen at substantially higher levels than inflation.

5.8 In response to a request from Glencore to review the draft provisional report, Deloitte described “fundamental flaws in terms of methodology and approach applied” and reiterated that “for each of the years subject to audit, Mopani’s statutory financial statements were audited by Deloitte Zambia and unqualified audit opinions were issued”. Deloitte’s full letter is posted on Glencore’s website.

5.9 Mopani has engaged in a detailed and constructive dialogue with the Zambia Revenue Authority on these matters. The Zambia Revenue Authority has completed its audits of all the years in question. Thus far they have found all the allegations to be unsubstantiated. We continue our dialogue with the Zambia Revenue Authority and expect the audits to be finalised and closed out shortly.

5.10 In 2005 the European Investment Bank signed a Finance Contract with Mopani for an amount of $50 million to partially fund the rehabilitation of the Mufulira smelter. The European Investment Bank has informed the European Anti-Fraud Office (OLAF) and launched its own investigation about the tax allegations made in Zambia against Mopani. Discussions continue with the European Investment Bank on this matter.

Mopani’s position with regards to the European Investment Bank process is entirely consistent with the position it has taken with the Zambia Revenue Authority.
6. The Relationship between Taxation and Development

6.1 Glencore fundamentally believes that inward investment has a positive impact in developing countries, creating employment and entrepreneurial opportunities which are the only route out of poverty. Feeding the mineral requirements of China, India and other fast-growing economies has the potential to create transformative economic growth in resource-holding countries in Africa and beyond.

6.2 In addition, in the natural resources industry, investment in developing countries has a positive impact globally. The world needs minerals to sustain and improve living standards worldwide. Demand is growing and supply is constrained. Some of the best remaining sources of supply lie in developing countries and failure to develop them will result in higher prices for everyone.

6.3 It is Glencore’s view that progress in building durable economic growth in less developed countries is more likely in open economies with taxation systems that are transparent, welcoming to foreign investors and accountable.

6.4 We agree that the link between taxation and development is fundamental and that the failure to collect tax in developing countries is a major issue of concern. Businesses such as ours, which are based on significant investment in fixed assets that will deliver returns only over decades, have no interest in taxation systems that are unfit for purpose, arbitrary or misdirected.

6.5 However, as a major investor in the developing world Glencore cannot and should not be expected to adopt aggressive political postures over the proper conduct of Government and its taxation policy.

6.6 Glencore does not make political contributions or seek to become involved in party politics in any way.

6.7 The issues of wealth distribution, public service provision and poverty reduction matter to Glencore, but go far beyond the subject of this Committee’s inquiry and indeed the capacity or proper remit of Glencore or any other corporate in any particular country. These matters are of concern to us all, but their resolution in individual countries, whether in Zambia or elsewhere, must be resolved by the legitimate governments of those countries and the properly constituted international agencies within whose remit these matters lie.

April 2012

Annex A

ADDENDUM TO GLENCORE SUBMISSION

The following information has been extracted from published sources, including Glencore’s Sustainability Report 2010 and Annual Report 2011.

1. Regional breakdown of taxes and royalties paid and relating to the Group’s industrial activities in 2010. (US$ millions)

<table>
<thead>
<tr>
<th></th>
<th>Africa</th>
<th>Americas</th>
<th>Asia</th>
<th>Europe</th>
<th>Oceanic</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>89</td>
<td>112</td>
<td>308</td>
<td>2</td>
<td>63</td>
<td>575</td>
</tr>
</tbody>
</table>

2. Changes in the revenue, output, earnings and capital expenditure of Mopani 2010–2011 (US$ millions; output in thousand metric tonnes).

<table>
<thead>
<tr>
<th></th>
<th>Revenue</th>
<th>EBIT</th>
<th>Capex</th>
<th>Copper production</th>
</tr>
</thead>
<tbody>
<tr>
<td>2011</td>
<td>1,155</td>
<td>207</td>
<td>163</td>
<td>204.4</td>
</tr>
<tr>
<td>2010</td>
<td>863</td>
<td>68</td>
<td>130</td>
<td>197.4</td>
</tr>
</tbody>
</table>


<table>
<thead>
<tr>
<th></th>
<th>Q1/10</th>
<th>Q2/10</th>
<th>Q3/10</th>
<th>Q4/10</th>
<th>Q1/11</th>
<th>Q2/11</th>
<th>Q3/11</th>
<th>Q4/11</th>
</tr>
</thead>
<tbody>
<tr>
<td>Own feed</td>
<td>18.6</td>
<td>12.9</td>
<td>31.2</td>
<td>31.7</td>
<td>24.5</td>
<td>25.1</td>
<td>24.0</td>
<td>27.8</td>
</tr>
<tr>
<td>3rd party</td>
<td>28.1</td>
<td>20.9</td>
<td>23.9</td>
<td>30.1</td>
<td>25.3</td>
<td>27.5</td>
<td>27.3</td>
<td>22.9</td>
</tr>
</tbody>
</table>

4. Royalty taxation as a percentage of Mopani’s overall tax burden.

<table>
<thead>
<tr>
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<th></th>
<th></th>
<th></th>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Total tax burden</td>
<td>23.0</td>
<td>40.9</td>
<td>47.4</td>
<td>64.8</td>
<td>61.1</td>
<td>71.6</td>
<td>104.0</td>
</tr>
<tr>
<td>Mineral Royalty Tax</td>
<td>1.9</td>
<td>3.0</td>
<td>4.3</td>
<td>17.8</td>
<td>20.0</td>
<td>28.1</td>
<td>23.2</td>
</tr>
<tr>
<td>Mineral Royalty Tax %</td>
<td>8.3%</td>
<td>7.3%</td>
<td>9.1%</td>
<td>27.5%</td>
<td>32.7%</td>
<td>39.3%</td>
<td>22.3%</td>
</tr>
<tr>
<td>Mineral Royalty rate</td>
<td>0.6%</td>
<td>0.6%</td>
<td>0.6%</td>
<td>3%</td>
<td>3%</td>
<td>3%</td>
<td>3%</td>
</tr>
</tbody>
</table>
5. Mopani’s pay stipulation to its contractors with regards to their staff

All contractors sign a contract with Mopani that includes a provision requiring them to pay their employee’s a minimum of 80% of Mopani’s minimum basic salary. Mopani believes it has the second highest minimum basic salary amongst the mining companies in Zambia.

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Written evidence submitted by HM Treasury

RESPONSE TO Q211—INFORMATION ON THE OECD TASK FORCE

As part of the OECD Global Forum on Development held 27–28 January 2010, the creation of the Task Force on Tax and Development was announced at a joint meeting between the Committee on Fiscal Affairs (OECD CFA) and Committee on Development Assistance (OECD DAC).

UK attendance at meetings in this area followed the normal pattern where political engagement by Ministers (to register an issue of the international agenda) gives way to engagement by officials (to work through the development of the new process and then to carry forward the detailed technical work).

The Right Honourable Stephen Timms MP from the previous Government attended this meeting as Financial Secretary to Her Majesty’s Treasury, to register this issue on the international agenda.

The first meeting of the actual Task Force took place on 11 May 2010 in Paris. Officials from the Department of International Development (DFID) and the Treasury attended the first one rather than a Minister.

The task force is essentially a technical discussion forum and not intended for ministerial level representation. Delegates from donor countries are usually officials from development, foreign, or finance ministries.

The UK position for taskforce meetings is prepared in close consultation between DFID, HMT and HMRC.

There have been two further taskforce meetings held 11–12 April 2011 in Paris, and most recently 9–10 May 2012 in Cape Town. An official from DFID has attended all three taskforce meetings.

The Task Force is co-chaired by South Africa and the Netherlands, and includes members from OECD and developing countries, international and regional organisations, NGOs and business.

The role of the Task Force is to support the Committees in delivering a programme to strengthen tax systems in developing countries. It identified four areas of work as key for developing countries efforts to mobilise domestic resources:

— state building, accountability and effective capacity development;
— more effective transfer pricing regimes in developing countries;
— increased transparency in the reporting of financial data by MNEs; and
— countering international tax evasion/avoidance and improving transparency and exchange of information.

The Taskforce has also held further sub-group meetings which took place during the following dates:

Transfer Pricing
15 December 2010
19 September 2011

Transparency in Financial Reporting
9 December 2010
29 March 2012

State building, Taxation and Aid
4 November 2011
7–8 February 2012

The DFID official attended both sub group meetings on Transparency in Financial Reporting.

We see the Taskforce as a valuable forum not only for the strength of the discussion but for the practical steps that it has taken to respond to the issues and needs identified by developing countries themselves, for example the recent technical assistance on transfer pricing to Kenya, Ghana, Vietnam, Rwanda and Colombia.

RESPONSE TO Q212—MEANING OF “PLAUSIBLE GROUNDS” WITH RESPECT TO THE UK-SWITZERLAND AGREEMENT

A powerful new provision in the UK-Switzerland agreement will allow HMRC to find out whether UK taxpayers have bank accounts in Switzerland. This provision is a substantial improvement on HMRC’s current ability to identify Swiss accounts.
Under this new provision, the UK will ask the Swiss authorities to determine whether a named individual has an account with a Swiss financial institution. The agreement specifies that the UK must have “plausible grounds” for making such a request. It goes on to define “plausible grounds” in Article 33 paragraph 3:

“Plausible grounds for the request exist where the competent authority of the United Kingdom has identified on a case-by-case basis a tax risk in relation to the United Kingdom taxpayer and sees plausible, non-arbitrary grounds for checking the tax position of a United Kingdom taxpayer. These grounds shall be based on an analysis of a range of information such as previous tax returns, level of income, third party information and knowledge of the persons who were involved in completing a tax return. So called “fishing expeditions” are excluded.”

In practice, this means that UK must confirm that a tax risk in relation to the individual in question has been identified through HMRC’s risk assessment procedures. It is not necessary for a link to Switzerland to be proved; nor must the “plausible grounds” be disclosed to the Swiss.

Response to Q226—Suspicious Banking Reports

In response to the Committee question about how many suspicious banking reports are received per year in respect of (a) UK citizens and (b) foreign nationals, I can confirm the Treasury does not keep this information.

All Suspicious Activity Reports (SARs) go directly to the Serious Organised Crime Agency (SOCA). However, it may be helpful to cite SOCA’s 2011 annual report which states it received a total of 247,601 SARs in the last year (October 2010 to September 2011) with approximately 78% coming from the banking sector.

23 May 2012