World Bank and IMF: Where do they stand on progressive and responsible taxation?

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The IMF and the World Bank, including the IFC, are increasingly engaged with the challenge of addressing how tax avoidance and evasion affect developing countries. However, their approach needs to go much further to address the role played by multinational enterprises and tax havens in exacerbating inequality and undermining countries' domestic revenues.

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The World Bank and the IMF have finally begun to connect the dots between tax havens, tax losses by activities of multinational enterprises (MNEs), and growing inequality, including gender inequality. They loudly trumpeted a new UN, OECD, IMF and World Bank "Platform for Collaboration on Tax", the week after the Bank & Fund spring meetings in April, announcing it as civil society gathered to influence the UN's Financing for Development (FFD) follow-up negotiations in New York.

Tax avoidance and evasion are not new issues to the IMF. As early as 2001, the former head of the IMF's Fiscal Affairs Department (FAD) described MNEs' tax practices as "fiscal termites", though no concrete steps were taken at the time to identify the scale of the losses or to address them. It took a financial crisis before the G20 requested the OECD to focus on tax havens in 2009 by forming the Global Forum on Transparency and Exchange of Information for Tax Purposes (known as the OECD Global Forum), followed up by the OECD's G20-mandated Base Erosion and Profit Shifting (BEPS) project initiated in 2012 to address the issue of corporate tax losses. 2014 and 2015 studies by the IMF estimated tax losses in non-OECD countries due to MNE activities at between \$100 and \$300 billion annually, with "especially marked and important" losses for developing countries. The new joint Platform finally provides an explicit developing country angle for this work and intends to pick up the momentum from the July 2015 Addis Ababa FFD Conference that placed domestic resources such as tax revenues at the heart of fulfilling the Sustainable Development Goal (SDG) financing gap of \$2.5 trillion.

Has Bank and IFC lending become more tax responsible?

In 2011 the World Bank finally adopted a policy on the use of Offshore Financial Centres (OFCs), with the main objective that they "are not used for tax evasion". The policy suffers from the lack of a specific list of high-risk jurisdictions or practices. Instead it adopts a weak process of peer reviews and assessments by the OECD Global Forum. For example the British Virgin Islands, which has a "largely compliant" status according to the Global Forum, hosts over half of the offshore companies mentioned in the ‘Panama Papers’ scandal in 2016 that exposed wide-ranging tax secrecy. Using a broader definition of a ‘tax haven’ from the Tax Justice Network’s Financial Secrecy Index, a 2015 report by Oxfam highlighted that 25 per cent of the International Finance Corporation (IFC, the Bank’s private sector arm) investment projects in the sub-Saharan African region were agreed with companies incorporated in tax havens, such as Mauritius, the Netherlands or Jersey.

In a 2015 analysis the investment analyst MSCI found that 22 per cent of the companies analysed paid a tax rate substantially below the weighted average, concluding that these companies presented a significant risk to investors due to both reputational and tax litigation risks. Reputation risks are apparent in the case of the Minera Yanacocha S.R.L., one of the largest gold mines in Latin America, 51 per cent of which is owned by Newmont Mining Corporation, with Peruvian Buenaventura holding 44 per cent and the IFC 5 per cent. A 2015 report by Peru-based Latin American regional CSO network LATINDADD highlighted that the average annual tax levy on income from the operation of Yanacocha in the period 2006-2013 was $196 million on an average net income of $5.7 billion. LATINDADD concluded that, while they cannot accuse the company of illegal behaviour, the corporate tax payments remained small due to “inexplicable distortion between costs and prices”. The report indeed raised more questions than answers due to the lack of greater tax transparency.

Further reviews of the IFC’s portfolio reveals it invested in 2012 in Stora Enso, a Finnish forestry MNE, for projects in a number of countries, including China, and for provision of advisory risk services in Laos. Stora Enso was reported by investigative journalists in 2012 to have avoided taxes through its Dutch subsidiary office in Amsterdam, which had generated half of the group's profit with less than two per cent of the group's turnover in years 2005-2010. The journalists also found that most of the profits on the cellulose originating from Brazil remained in the Netherlands, where the average effective tax rate for 2005-2010 was 1.5 per cent due to an advantageous Advanced Pricing Agreement (APA) between Stora Enso Amsterdam and the Dutch tax authorities. The ruling is not on public record, but the latest agreement ran up to 2014. Again, the behaviour has not to date been found to be illegal in Brazil, the Netherlands or Finland, but it raises serious questions concerning profit shifting and its impact on the domestic revenues of developing countries.

The IMF: walking its own talk on tax?

NGOs have for many years highlighted that IMF tax advice has promoted regressive tax policies that only create more inequality by advising countries to lower their trade and corporate taxes, while increasing value-added taxes where the incidence is mostly on the poor. A shift in understanding on tax issues may be detectable at the IMF, in particular on the impact of tax avoidance on developing countries’ revenues and on questions of income and gender inequality. A 2014 policy paper stated that: “fiscal policy is the primary tool for governments to affect income distribution” and that “the Fund should be mindful of how macroeconomic policies (including fiscal policies) affect income distribution and their consistency with the distributional goals of country authorities.” Notably, the policy paper was not approved by the board, but rather discussed in an “informal session”. Therefore this paper, along with the Fund’s recent research, does not represent board-approved IMF policy. Nevertheless, gender inequality and women’s economic participation were included as ‘macro-critical’ subjects in a 2013 IMF Staff Discussion Note which emphasised the importance of understanding the impact of gender through the broader lens of income inequality – including tax policies.

Tanzania Revenue Authority, Photo: Christain Aid

But has this guidance been put in practice? Looking at a 2016 assessment of Thailand, the IMF recommended increasing VAT from 7 to 10 per cent once economic recovery was underway, while also in the same evaluation commenting that lowering corporate income tax is good for growth and competitiveness without reference to the evidence the IMF itself has developed which contradicts, or at least complicates, such a statement. Meanwhile, in Costa Rica's 2016 Article IV evaluation IMF staff welcomed a rise in marginal income taxes (albeit from a very low rate of 20 to 25 per cent), while also recommending increases in VAT, however, "with targeted support to offset the impact on lower-income households". Looking at existing capacity building and the diagnostics tools on offer, it appears that the IMF's focus is still largely on indirect taxes following this assessment.

Some welcome signs of a shift in policy might be evident in Cote d'Ivoire's 2016 Article IV evaluation where IMF staff recommended reducing tax incentives in an effort to raise more revenue, which was met with resistance by the Ivorian officials who "expressed concerns regarding the impact of cutting exemptions on Côte d'Ivoire's investment attractiveness." This statement raises questions over the continued use of the World Bank's Doing Business Report (DBR) to rank investment attractiveness of developing countries. The DBR's tax indicator still awards positive points for a lower total tax rate for companies, and thus explicitly rewards the lowering of corporate taxes, while the IMF's research on spillover effects cited above found that tax competition remains a key challenge for developing countries.

The emphasis in tax policy advice also needs to consider spending, not just revenues, especially in addressing gender inequalities. The 2015 Article IV IMF evaluation of Chile congratulated the country for its reforms to "improve (female) labour force participation - and in turn equity - by extending the length of maternity leave, employment subsidies for low income women and youth, and employment support and training services, albeit not used up extensively". However, the IMF's advice was more generic on boosting female labour market participation without an explicit policy recommendation for extending maternity leave. It seems that IMF staff lack experience in gender or inequality analysis of fiscal policies' impact, and this brings into question how and whether the IMF's new thinking and evidence are being put into practice. Experience from budget monitoring work by the International Budget Project members in South Africa has shown that only by conducting such gender analysis can fiscal policies address a specific gender bias.

Ensuring policies are implemented

Looking ahead there is considerable potential for the Fund and World Bank Group to address some of their problematic tax policies. It is essential that the Bank revisits its OFC policy and establishes a broader tax policy for its lending operations that enables it to draw red lines in terms of high risk jurisdictions especially in offshore financial centres, while also allowing it to engage on a continuous basis, especially for the IFC's private sector investments. A 2015 joint report by international NGOs ActionAid, Christian Aid and Oxfam titled *Getting to good*, addressing tax responsibility of companies, highlighted indicators for good behaviour across eight areas that should be utilised by the IFC: tax planning practices; public transparency and reporting; non-public disclosure; relationships with tax authorities; tax function management and governance; impact evaluation of tax policy and practice; tax lobbying; and tax incentives. The report placed tax in a framework of corporate responsibility, and allows for stakeholders to identify key areas of tax risk and impact on wider society.

The Bank should put progressive tax policies that reduce inequality, and in particular gender inequality, at the heart of its offer of technical assistance under the International Development Association (IDA, the Bank's low-income country arm) 18th replenishment round. IDA 18 has a priority area on tax, governance and public finance management. Technical assistance should prioiritise support to the identification of key gaps in legislation including gender bias in tax and expenditure legislation, policies and capacity including strengthening tax audit and litigation, negotiation of both double tax treaties and bilateral Advanced Pricing Agreements to better protect revenue, and rationalisation of tax incentives in terms of cost and benefit. Additionally, the Bank should change the Doing Business indicator on total tax contribution towards a tax transparency indicator of companies' behaviour that promotes rule of law rather than low taxes.

The Platform for Collaboration on Tax ... should be … a space to bring the concerns of developing countries on to the table

In terms of the Fund, it has made welcome steps in identifying both the issue of tax havens and tax losses by MNEs, but has further work to do in terms of linking up gender and equality impact issues to its tax policy analysis. The Fund still has gaps in its work on illicit financing that currently only touches on the criminal and corrupt aspects of the problem, ignoring commercial transactions of facilitating corruption such as tax evasion and trade mispricing. The Fund should consider these wider issues in its research and policy advice work. Independent estimates by Global Financial Integrity consider that $1.1 trillion of illicit financial flows leave developing countries every year. Fairness and tackling illicit financial flows should be at the heart of the Fund's upcoming work "strengthening the capacity of national tax administrations and the deepening of its work on international tax issues of relevance for developing countries" in 25 countries to be identified over the course of 2016. It will be interesting to see if this emphasis shifts in the Fund's Tax Administration Diagnostics Tool (TADAT), launched in 2013. The key task becomes putting the IMF's often ground-breaking research into practice, and to develop diagnostic tools for developing countries on corporate tax capacity. In addition to the tools it has already developed to assess international spillovers the IMF should be focused on how they too can be applied to and used actively by developing countries.

It is these and other issues that brought the Platform for Collaboration on Tax into existence and it should be utilised as a space not only to promote the agenda of the OECD countries, as occurred too much under the OECD-led BEPS process, but to bring the concerns of developing countries on to the table to be addressed directly.

A fully referenced version of this article is available on the Bretton Woods Project website at: tinyurl.com/IFIsTaxPlatform

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