AFRICA’S TAXING PROBLEM

23 October 2013 by Vincent Huck

As tax planning practices of multinationals are under great public scrutiny and pressure mounts to close tax loopholes, there is an entire continent suffering from haemorrhaging tax revenues due to faulty tax practices and rules opened to abuse. Vincent Huck reports.

In the wake of the 2008 financial crisis the rising demand from the public for more transparency and accountability on the part of businesses has put tax evasion, tax avoidance and tax planning under the spotlight.

If up to now the international community seemed reluctant to address the issue, 2013 saw a number of important developments that intensified the debate. In June, the G8 under the UK presidency, called for greater transparency with regards to tax authorities in order to tackle tax evasion. In July, the Organisation for Economic Co-operation and Development released its Action Plan on Base Erosion and Profit Shifting. And in September, the G20 carried on the discussion on reforming tax internationally.

Tax evasion, avoidance and planning, as well as transfer pricing are global issues which affect every country, rich or poor, but the consequences on developing countries are greater. For Africa in particular the scale of harmful tax practices affects the capacity of the continent to develop.

Africa’s losses

Earlier this year, the African Progress Panel (APP) released a report on equity in extractives, which reveals Africa loses $38.4bn a year in trade mispricing, while receiving $29.5bn in aid. The report also states Africa loses another $25bn annually in other illicit outflows, such as funds illegally earned, transferred or utilised.

Tax Justice Network (TJN) Africa director Alvin Mosioma explains: “African countries face a number of challenges in their efforts to raise revenues from tax due to both domestic issues and to the international context.”

At the domestic level, Mosioma says the main challenge is the weak capacity of the revenue authorities. “It is firstly a lack of financial resources, as many of the companies operating in Africa have revenues that surpass the GDPs of the countries they operate in,” he says. “But most importantly the revenue authorities also suffer from understaffing.”

APP head of communications Edward Harris agrees: “Nigeria for example has 5,000 tax and custom officials for a population of 140 million. In comparison the Netherlands counts 30,000 tax and custom officials for a population of 10 million.”

Bribes and intimidation

This lack of resources undermines the capacity of revenue officials to perform their job and, according to TJN research, makes them increasingly receptive to bribes and easily intimidated by any type of lobby. “Moreover, as a consequence revenue officials often end up leaving the public sector and working for private companies or even accounting firms,” Mosioma says.

He describes the situation as a vicious circle from which it’s difficult to escape. “It is basically a need of capacity building,” he says. “It could come internally, as a percentage of the revenues collected by the authorities are kept for their own administrative work. The more they are able to collect, the more they are able to keep. This could be an incentive to empower revenue authorities.”

Other resources can come from external initiatives. For example a part of the financial aid from the West is directed to the empowerment of tax administration. But some initiatives also exist at the continental level, such as the African Tax Administration Forum, of which Mosioma says “there are ongoing processes that will be key to enhancing the capacity of revenue authorities at a regional level.”

Away from domestic issues African counties are also affected by tax issues at an international level such as the secrecy of tax havens and the issues around transfer pricing, tax evasion, tax avoidance and tax planning.

Harris explains: “The issue is the way the international system works, allowing for easy flows of large amount of money between different countries. You can work and make profit in a country, but the international financial system allows you to shift your profits to a much lower tax jurisdiction. It might be legal, but it’s unfair.”
Accounting firms’ role
For Mosioma accounting firms are at the heart of the problem, because they advice multinationals and approve their accounts. "Who designs tax minimising and tax planning tools? The accounting firms and especially the Big Four," he says.

Grant Thornton UK tax director Mike Warburton says accountants are in a difficult situation stuck between their duty to the public and their duty to their clients. "It’s their jobs to make sure their clients are compliant with the law,” he says. "But it’s also their obligation to help their clients save tax if requested.”

Harris believes it’s necessary to draw a line between what is strictly legal and what is ethical. "Tax avoidance can be legal in the strict sense of the word, but the scale of it is so big that it has gone out of control and it is completely unethical,” he says.

Mosioma questions where this duty to the public is and asks if it's just a myth. "Do they want their clients to continue investing in a country where the laws are disrespected, where governments are not able to support education, where human resources are made available for them to exploit," he asks.

"All these issues are tackled with tax. So if it’s their obligation to undermine tax for their clients, where does the public interest stand in a logic of profit maximisation?”

Harris and Mosioma agree accounting firms and accounting bodies have a role to play in tackling the issue. Mosioma believes accounting firms can be part of the solution by providing advice to multinationals which in the long term will serve the public. He also believes, to a certain extent, accounting firms and accountants can provide expertise to government, such as the OECD Tax Inspectors Without Borders project.

Harris also sees another opportunity for firms and accountants. "By proving their integrity and professional morals, they are going to be part of the equation of shifting a global mindset away from tax avoidance,” he says. “We need to shift the way we think about tax and accounting. The global tax system isn't fit for purpose and hasn't caught up with the rapidly changing world. It needs reforming.”

Reform on the way
Some, like OECD Centre for Tax Policy and Administration director Pascal Saint-Amans, argue that reform is on its way. In July the OECD released an action plan on BEPS which sets out 15 actions for study over the next two years. Most of these will result either in changes to OECD guidance, for example on transfer pricing, or to the OECD Model Tax Convention and recommendations to support domestic governments. An instrument is also proposed to enable amendment of tax treaties without the need for renegotiation.

"On the one hand it's positive. It has taken so much effort to reach this moment where the OECD and the international bodies recognise the importance of this issue," Mosioma comments. "However we are concerned that it's just a declaration of good intention and nothing happens after that. These declarations by the G8, G20 and the OECD have to be acted upon and should not remain political rhetoric.”

Mazars partner and tax advisor Erik Stroeve believes these are good developments. He says more reporting is obviously more time consuming and may be burdensome for multinationals, but it would make their dealings more transparent if they answer questions such as: where are their tax structures and how can they justify these tax structures?

Stroeve says: "In many cases it's not about avoidance, and the tax planning is often not really aggressive tax planning. Ultimately it can be explained from a business and commercial perspective.”

Double taxation
For Stroeve the main objective of tax planning is to avoid double taxation. "Of course in some instances companies are looking at making a competitive benefit which requires tax planning,” he says. "But because of shrinking budgets more countries are trying to get more money through the door and, more often than not, one euro is taxed on both sides. So it's about paying your fair share, but not paying it twice.”

However, Mosioma argues that avoidance of double taxation only leads to double non-taxation, and bilateral treaties on double taxation isn’t the way forward. "If a country like Kenya signs 100 bilateral agreements how will it have the capacity to enforce each one of them?” he asks. "The right direction is towards multilateral tax agreements at the international level.”

They might not agree on the nature of the regulatory changes, but all the stakeholders involved in the debate: firms, international organisations, NGOs and governments agree that a change in regulation is needed. “The rules of the game are more important than relying on the voluntary mechanism of the players,” Mosioma says.
And here lies another problem: at present there is no international authority whose sole purpose is to administrate tax on the global scale. The UN and the OECD are perceived to be in different camps, with the OECD believed to be the "rich countries' club" defending the interest of the US and Europe, while the UN is seen as the advocate of developing countries. But the creation of an international body solely devoted to tax issues might be a solution, as Mosioma says: "The World Trade Organisation exists, so why not the World Tax Authority?"

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**Tax Inspectors Without Borders**

The Organisation for Economic Co-operation and Development (OECD) is expected to start a new programme called Tax Inspectors Without Borders (TIWB) in the spring of 2014.

TIWB will complement the assistance given by international organisations and non-governmental organisations to tax administration in developing countries.

OECD Centre for Tax Policy and Administration director Pascal Saint-Amans explains: "In addition to all the assistance that's going on and which is good, we felt that there was a need for a short-term, more targeted type of initiative. "That's why we came up with the idea of Tax Inspectors Without Borders in 2012."

TIWB will essentially be a roster of tax experts, some of whom will be working for accountancy firms, nominated by OECD countries, at the disposal of developing countries for short missions.

"For example, an African country has planned a three-month audit on a multinational working in the mining industry and they know the main issue they will face is related to transfer pricing," Saint-Amans says.

"If they don't have a transfer pricing expert they can get one that matches their needs from the roster to come and assist for the period of the audit, as part of the team and under the supervision of the local team manager. "Ideally by working with the local team, under the supervision of the local manager, the tax expert would transfer his knowledge to his colleagues."

For Saint-Amans the benefits are multiple: "We're transferring knowledge through hands-on experience so developing countries may learn more.

"It clearly addresses their needs as they are the ones who express what they are looking for. "And it's cost-effective because they are targeted assignments."

Saint-Amans says ultimately TIWB should be run by a foundation, but in the short and medium term it will remain in the OECD and the funding will come from development agencies.