

Fórum das Políticas Públicas 2017

Os Desafios das Políticas Fiscais

Equidade, competitividade, sustentabilidade e concorrência fiscal

Painel: Os desafios das políticas fiscais

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Good morning everyone.

Let me start first by apologizing for not presenting in Portuguese. I have now had my Portuguese lesson you will now have your English lesson for the morning. But I hope despite the fact that I'm not speaking in Portuguese that my comments will be useful to you.

Let me also thank the organizers and particularly the President here for having said so many kind things about the OECD. It is true that we are a different type of organization in that we are not a think tank like some others. We don't just sit and think deep thoughts and come up with optimal solutions.

We work with experts from all of our member countries and from a growing number of countries that are not members of the OECD but are increasingly joining our work, and that really I think is the strength of the OECD. The committee approach where we get the experts, the people from the ministries of finance, from the tax administrations to bring their practical experience to the work, the policy design that we undertake at the OECD, that is quite important.

That is why I was particularly pleased to hear this morning that the objective of this event is to really bring the academic and the political together. So that you get the benefits and the strength of expertise of academic thinking, research and analysis but also the political dimension, which is so important to actually achieving and implementing objectives in whatever policy area.

Now we are here today to talk about taxation and I was very pleased to see the themes of this conference because the issues of fairness, competitiveness, sustainability and tax competition are all issues that we are focusing on at OECD.

We are also focusing on the design of tax policy: how to make tax policy more redistributive, fairer so that it produces inclusive growth. In fact in two weeks time we will be having a ministerial meeting at the OECD where we will be discussing these issues. Because we have seen, I think all of us have seen the backlash against globalization, the frustration, the lack of trust in governments right now that is so high. And how do we reset that picture so that we can restore trust, restore the balance, address the issue of inequality and improve the lives of people. Our saying, our motto at the OECD is "better policies for better lives". I think to me that is quite important because that is at the end of the day what we are trying to achieve not the most perfect policy but policies that will actually impact and improve people's lives.

So if I start, and I will because I can't cover in the time that I have all of the areas of work that we undertake in fiscal policy, I thought I would focus on some of our more recent and high profile work which focuses very much on the issue of fairness. That is our work in international

taxation in both improving the transparency and cooperation among countries and also to deal with tax evasion and then also to deal with what is normally considered legal but not necessarily desirable: aggressive tax planning by multinational companies which I think you all know, it has been very much in the news.

So if we go back to the start of our big launch of this work. We have always been working on tackling tax evasion and our work to improve exchange of information between countries has always been part of it. But it never really attracted that much significance within individual countries. Why? Because when they were negotiating tax treaties, they were far more focused on working to remove double taxation so as to facilitate cross border trade and investment. The issue of cooperation to tackle tax evasion was sort of a side issue. It was there but it was a side issue despite the good work in progress we made and there were some countries that did focus on that quite a bit. The Nordics in particular developed a very strong and integrated approach to tackling tax evasion and were very effective and I think you probably all know they had some of the highest rates of tax compliance in OECD countries.

But then when we had the economic crisis the financial crisis of 2008 where all countries were suffering where citizens were disillusioned to say the least, the tolerance for tax evasion was down to zero and governments had to act. In addition, at the same time, we had leaks. We started with the Lichtenstein scandal where someone who had worked at a bank in Liechtenstein had stolen data and then exposed the fact that thousands and thousands of citizens from around the world were escaping tax. Now we all sort of knew that people were hiding their money off shore but there was never the proof and of course it was always very difficult to prove this to those countries that had secrecy because they would say "well we are just facilitating private wealth management". And so apart from anecdotal cases here and there it was very hard to prove. With this kinds of leaks they could no longer say that "oh this is just wealth planning", it was very clear that what was happening was illegal and on a very broad scale.

So with the combination of the crisis and these leaks, that's where the political momentum developed and we were able to get the G20 support. Very strong support to tackling issues like bank secrecy, bearer shares, the lack of transparency of companies and ensuring that companies and individuals were required to keep books and records so the tax administrations could do their job of following the financial trail to tackle tax evasion. That alone was not enough because we as we all know this is now a borderless world. There are no longer exchange controls, people can bank all over the world at the click of a button.

But tax administrations for their enforcement purposes are bound by national boundaries, they cannot cross the border into Switzerland to go chase a tax evader, that would be illegal and they would be arrested. So what is needed is cooperation in the form of exchange of information. In 2009 what we did was we established standards on all of this various aspects of transparency. We had an existing multi-lateral convention for exchange of information for cooperation. It dated back to 1996, we did it with the Council of Europe, but despite being a very advanced instrument, maybe it was way ahead of its time, not many countries ended up signing it. I think we had about 12, there was just not a lot of uptake.

Once these scandals broke with the financial crisis we decided to update this instrument and also open it up to the rest of the world because tax evasion is a global issue and all countries

are affected and if all countries are not involved in tackling the issue through cooperation then what happens? You simply shift the tax evading activities to another location so it is essential in our project to ensure that we got all financial centers involved and committed to implement transparency, get rid of bank secrecy and sign up to exchange of information. We have established a global forum on transparency for this and initially it consisted of OECD countries and the financial centers that we wanted to have committed to this process. The G20 countries also came along and then, interestingly, developing countries said "we want to be there too because we are harmed and we can benefit from your standards, the perks of your process that you are setting up, to ensure all countries implement this". Frankly, a lot of these measures that were designed to facilitate cross border cooperation between tax authorities also help strengthen the tax administration powers for national tax purposes.

I think when we started this work even Portugal didn't have full access to bank information and that has changed over time to come up to the standards. So many countries benefited from this in improving their own domestic powers to tackle these issues while at the same time through cooperation we are helping other countries to tackle the issues.

So today, what we have is a global forum of over 140 countries and jurisdictions including all financial centers around the world. They are all being evaluated through a peer review process by the countries themselves. We at the OECD facilitate it but it's the countries that review the legal frameworks that have been put in place as well as the administrative cooperation in practice. So not just the theory, not just the laws on the book but also that they are actually applying these laws as they are intended to be applied and in the time frames that are required by our standards. Otherwise, these standards would simply just be written in books and papers but would not have the impact that we were expecting.

So we started off with this approach. The exchange of information that we were asking for countries was exchange on request meaning when a tax administration was carrying out an audit of a particular taxpayer and they saw a trail leading to a bank account in some sunny jurisdiction, they could ask that jurisdiction for information. We were criticized by a lot of people saying "well that's not enough because you have to first have started the audit, found the bank account in order to get it" but it was a big step for a lot of countries. Think about Switzerland and Luxemburg, this was a huge step from going where they were before, which was pretty complete bank secrecy for tax purposes, to now opening up the door.

Now since that time in 2014 we have improved the standard by adding another standard which is automatic exchange of banking information so what this means is that countries now have to collect all of the information on foreign residents who have bank accounts in their country and submit that to their counterpart on an annual basis. This is going to start in September of this year.

We have 100 countries and jurisdictions that have committed to doing this starting either this year or next year but it is going to start happening. Now you may ask why 100 when you have 140 in your global forum, well the reason is that many of the 140 are developing countries that do not have the technology or the capacity to implement this. They are not at present a risk to other countries although many of them, in order to receive the information, do want to move in this direction. We are helping them to get up to the capacity to have the procedures and legal frameworks in place, in particular to protect the confidentiality of this information. Because of course people are concerned their financial information may be leaked and that

would be very detrimental to individuals whose information is leaked and so maintaining and insuring the confidentiality of this information is quite critical.

Now you may be saying “ok well is this working? Is this having an impact?”. Well we have no direct measure, but the indirect measure that we do have is that many countries in anticipation of the introduction of automatic exchange of banking information have established what we call “voluntary disclosure programs”, others may have called them amnesties... A program where tax payers have a limited period of time to come in, change their evil ways, declare everything they have abroad and then fix their situation *vis-à-vis* their tax administration going forward because they have disclosed everything and they have become compliant. Now as a result of this program in a large number of countries around the world almost 800 billion euros of additional tax revenue has been identified. That to us suggests that our efforts are having an impact. We cannot measure the deterrent effect of having exchange of information in place and having automatic exchange of banking information in place. That would be a great thing if those of you in academia could figure out a way to measure deterrent effect. It is quite difficult.

That is a large part of what we are trying to do: show to taxpayers that there is a much greater risk now of getting caught than there was before. And so that has been attributable to this changes as well as to the fact that we now have 109, soon to be 111, countries and jurisdictions that have signed our multi-lateral convention on mutual administrative assistance in tax matters. That is a big leap from the 12 countries we had before.

So that's what we've been doing to try and strengthen cooperation and transparency, to tackle tax evasion and tax fraud. Now there is also the very big issue of tax avoidance, which is largely legal, by multinationals taking advantage of things like differences in the way, certain types of payments are characterized in different countries or exploiting transfer pricing rules or taking advantage of tax treaties to gain benefits that weren't intended for residents of third countries. Somehow they have taken the treaty provisions and exploited them to gain benefits that they should not be getting. I think many of you have seen in headlines: Google, Amazon, Apple, Starbucks. All of these companies have been in the headlines for their tax planning and for their ability to get their effective tax rates down to less than one per cent in the case of Apple but others also in single digits.

If you think about it, after the economic crisis what happened? Many governments decided to lower corporate tax rates to try and boost investment and encourage corporate activity and job creation but at the same time in order to deal with their deficits they raised the IT rates, they raised property tax rates and these are things that hit individuals. So you have these individuals facing higher taxes, they are seeing wealthy people evading taxes by parking their income offshore and at the same time they are seeing these massive companies, very profitable companies paying less than once per cent in some cases. And so as a result of all of that and the fact that that came out in the news, I think that is an important component to your debate as well not just academic work, political component but also the role of civil society in helping shape tax policy that has really changed the last few years.

So as a result of these disclosures and developments the G20 again came to the OECD and asked us to do an analysis of this issue of base erosion and profit shifting by multinationals, which is now known as the BEPS project by the acronym in English. And so we did an analysis, we identified what were the causes or the ways that companies could exploit the existing

international tax rules. We came up with a 15 point action plan and then with that action plan we developed measures to address each of those issues and we presented that to the G20 in 2015.

Now these measures, and I won't go into all 15, I don't think we have time, they can basically be characterized as trying to insure greater coherence in the tax laws, to strengthen the connection between the place where tax is imposed and the place where value is created and substantial activities occur and then to increase transparency. If I give just a few examples for each of these, I think you will get the idea.

One of the issues in the area of coherence of the tax laws, which is also a competitiveness issue, is the issue of interest deductions in the tax system. Because shifting interest deductions to places where you have higher tax and putting the income in the place with the lower tax is a way to erode the tax base and probably one of the easiest ways you can do it.

Now some countries have tried to limit the amount of interest deductions that companies can take but that creates a competitiveness risk because let us say Portugal imposes a limit but Spain does not. Well, companies may decide to locate in Spain rather than in Portugal because they get a bigger interest deduction. So we came up with a system to establish a range, and this was really the first time that we have tried to come up with kind of rules to the game for domestic tax purposes. Previously countries said: "oh we are all sovereign in our tax policies, we are going to do whatever we want". Now countries have realized that there is an impact and so they have agreed to try and stay within that range so that there is less of this competitive issue and more importantly so there is less of an abuse of interest deductions to erode tax bases and shift profits.

Another example is the issue of what we call hybrid mismatch arrangements or hybrid transactions or entities where you can have say, a payment that in one country is treated as a tax exempt dividend and in other country it is treated as a deductible interest expense. So there you get two tax benefits for a single payment. Normally in a single country context you would not do that, you would give an expense to one company and your country but where it is paid they would have to include an income but because countries define different payments in different ways you get this mismatch. So we've created, I would say, some rather complicated rules to neutralize this effect so as to discourage this kind of arrangements. We were told by the private sector that these hybrids are basically now dead as a result of that.

So that has been I think a big innovation in terms of our work in the international sphere to coordinate on the domestic side to insure greater coherence, without harmonization but just greater coherence in how the different laws interact.

Then on substance, we did two main things: one is to strengthen our transfer pricing rules to make the connection between where profits are taxed and where the economic activity that generates those profits is located. And we did that to our transfer pricing guidelines. Then we also strengthened our modal tax treaty which was the core instrument, the first tax instrument of OECD. It is over 50 years old. And we have now established anti abuse provisions so that companies that weren't intended to be beneficiaries of those tax treaties cannot exploit them.

One of the innovations in this area that we have undertaken is that we have created a multi-lateral legal instrument to modify the network of over 3000 bilateral tax treaties that exist today. Why? Because we recognize that we can come up with all of these solutions to BEPS but it may take decades for countries to renegotiate all of these bilateral tax treaties.

And on June 7th we expect to have over 60 countries signing this rather innovative multi-lateral instrument and we hope that will help shape a future approach, a more efficient approach that will facilitate the updating of treaties in a more rapid fashion.

In terms of transparency, we have required the exchange of tax rulings; you saw the Lux Leaks where it became very clear that through rulings, private rulings, secret rulings, countries were giving away their tax base. And so now those rulings (and the EU has similar rule) those rulings are required to be exchanged with the other affected countries. Already we have identified 900 rulings that are subject to this and 600 have already been exchanged. That was quite important.

The other big change in the transparency front was in the area of transfer pricing where countries and tax administrations are trying to determine what is the market price that should have been charged between related parts of a single enterprise, the different parts of a multinational company, and we have what we called the arms length principle for that. But the challenge for tax administrations has been that they haven't had the complete picture of a multinationals operations.

So we established documentation requirements known as country by country reporting, plus a master file and a local file that will provide tax authorities with the complete picture but also all tax authorities will have the same information. Because you can imagine the companies may give one tax authority certain information and another one different information depending on what is the most beneficial information for them in that particular country.

Those are the kind of things that we have done to increase transparency, coherence and substance.

This has been a major undertaking. Again, we recognize that we can't just have OECD and G20 countries implementing this because the problem will just move elsewhere. And so we have created an inclusive framework on BEPS which allows all countries and jurisdictions that commit to the principles and the standards in BEPS to join and work with OECD and G20 countries to implement the standards, further develop them and insure their effective and consistent implementation. So that has been a major part of this work.

All of this has been a very big undertaking and I think it has been quite unsettling to multinational companies. They've been very concerned that all of these new rules create a great deal of uncertainty so it's part of our BEPS package that we also included a measure to insure that disputes and double taxation would be effectively resolved because, again, what we want to do at the OECD is to eliminate barriers to cross border trade and investment so that the economy can continue to grow but at the same time we need to insure that tax laws are complied with wherever companies operate and individuals invest their capital. That has been a key part of the BEPS project.

More recently, we launched a tax certainty project to strengthen the efforts of countries on both the policy side and the tax administration side to improve the tax policy environment for companies and individuals that are in fact trying to comply.

Maybe I will stop there, I know that it is an awful lot of information. But that has been a key component of our work on international taxation and I would say that one of the big side effects/benefits of all of this activity is that countries are collaborating now more than ever before and in all sorts of ways, including in acquiring common IT platforms to do the exchange of information. This is a first. I think this shows how countries realize that by working together they can be much more effective.

So I'll stop there. Thank you very much for your attention.