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Follow-up International Conference on Financing for Development to Review the Implementation of the Monterrey Consensus

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Multi-stakeholder round tables under the overall theme "Looking ahead: further cooperative actions in financing for development", focusing on the following six major thematic areas

Round table 1

Mobilizing domestic financial resources for development

Summary of discussion

1. Round table 1 was co-chaired by Emomali Rahmon, President of Tajikistan, and John Michuki, Minister for Finance of Kenya. Justin Yifu Lin, Chief Economist and Senior Vice-President of the World Bank, moderated the panel. Presentations were made by the following panellists: Azizul Islam, Minister for Finance of Bangladesh; Assane Diop, Executive Director, Social Protection Section, International Labour Organization; Angel Gurría, Secretary-General of the Organization for Economic Cooperation and Development; Michael Keating, Director of the Africa Progress Panel; Her Royal Highness Princess Máxima of the Netherlands, member of the United Nations Advisers Group on Inclusive Financial Sectors; and Vito Tanzi, former State Under-Secretary for Economy and Finance of Italy.

2. Mr. Lin introduced the topics under discussion. In particular, he stressed the importance of deriving investment from domestic rather than external sources as a foundation for long-term growth. He argued that now would be a good time for many countries to invest in development in order to prepare themselves for high economic growth in the future. He also noted that, if financial resources were derived from domestic sources, it would help countries to minimize currency mismatches and withstand the impact of financial crises.

3. Mr. Islam noted the importance of synergy between domestic resource mobilization, debt, trade and private capital flows. With regard to direct taxation in developing countries, he pointed out the lack of sufficient databases and information technology in tax administration. Given that the value-added taxes introduced in many developing countries did not sufficiently cover the shortfall of tax revenue caused by trade liberalization, donor countries should support national efforts in the area of tax collection. Because of insufficient physical infrastructure in developing countries, there was an urgent need for the international community to assist the

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least developed countries in that respect. Transnational corporations should not seek tax incentives that lasted long periods of time. Lowering the transaction cost for remittances was also identified as a useful measure.

4. Mr. Diop referred to the impact of the current financial crisis on financing for development, which would negatively affect employment and poverty-reduction prospects. It was estimated that 20 million jobs could be lost by 2009, which could significantly increase poverty levels. A multilateral framework was necessary to minimize such effects. It would be necessary to protect the most vulnerable segment of the population by providing basic social services. The need for decent work for all was emphasized.

5. Mr. Gurría stressed the importance of taxation for effective State-building. Since there was a direct link between the quality of Government expenditure and the readiness of citizens to meet their tax obligations, the importance of improving the relationship between Governments and taxpayers was emphasized. A clear understanding was needed that tax revenues would be spent in a transparent and efficient manner. However, tax collection was not necessarily confined within national borders. Tax havens undermined the tax base of both developed and developing countries by offering secrecy and a no-tax environment to evaders. There was a need to develop a renewed focus on enhancing domestic revenues through broadly based taxation, thus enabling greater predictability of revenues. Necessary measures would include creating effective tax systems, tackling the scourge of corruption, addressing tax havens and tax evasion, and helping to create an investment-friendly environment.

6. Mr. Keating focused on the impact of the global economic slowdown on Africa. In the light of declining commodity prices, the levels of trade and remittances from overseas had been decreasing. Given the critical lack of productive capacity and relatively high cost of electricity in developing countries, further investment in infrastructure was essential.

7. Princess Máxima addressed the issue of inclusive finance for development. She noted that much of the population in developing countries had no access to formal financial services, such as banking and insurance. As a result, the poor faced high transaction costs and high risk in the informal financial sector for sending and receiving remittances. In order to enhance domestic resource mobilization it was important to educate people how to save.

8. Mr. Tanzi referred to his 27 years of experience at the International Monetary Fund in providing advice to developing countries. He emphasized the need for effective tax policies that were fair, neutral, simple and broad-based. It was equally important that tax administration should be easy to comply with if sustainable development was to be achieved. Debt financing of budget deficits — the most common way to finance Government expenditure — was not sustainable in the long term. Lowering taxes usually resulted in higher tax revenue. In developing countries, however, owing to the existence of large informal sectors and the difficulty of enforcing tax collection, lowering tax rates did not guarantee increased tax revenues nor did providing tax incentives to transnational corporations.

9. The presentations by the panellists were followed by an interactive discussion among participants, including representatives of Governments, institutional stakeholders, civil society and the business sector.

10. The following key points were made in the presentations and discussions:

- Taxes represent the most important resource for investment, which in turn is essential for effective State-building. Effective tax policies that are fair, neutral, simple and broad-based, together with a tax administration that is easy to comply with, are essential for sustainable development. There is a need to avoid the politicization of tax compliance and collection.

- In order to support capacity-building in tax policy and administration in developing countries, it is essential to provide technical assistance in those fields, in particular to establish bilateral tax treaties and the exchange of information. Upgrading the technical skills of tax officers and the use of information technology in tax administration are prerequisites for enhancing tax revenue.

- Given that developing countries are not fully integrated into international forums on tax matters, the United Nations Committee of Experts on International Cooperation in Tax Matters could play an important role for such countries. To further promote such international cooperation, several participants supported the upgrading of the Committee to a Commission.

- Capital flight — derived mostly from illicit financing flows, tax evasion and avoidance, transfer-mispricing by transnational corporations and corruption — imposes large costs on development. It denies developing countries the precious financial resources essential for development. Capital flight is estimated at between $500 and $800 billion per year, an amount greater than total official development assistance to all developing countries. In order to prevent such capital flight, it is necessary to strengthen the exchange of information among tax authorities on a regular basis.

- Corruption is an issue for both developed and developing countries. In order to reduce corruption in the area of natural resources, the Extractive Industries Transparency Initiative should be recognized as an important instrument for preventing corruption. The United Nations Convention against Corruption and the Stolen Asset Recovery Initiative should be strengthened, extended and adopted by more countries.

- The taxation of natural resources and fees on public services could supplement existing tax revenues in developing countries. In the light of the high volatility of the prices of natural resources, the taxation of natural resources should be designed so that tax rates can be increased when the price is high and a price support mechanism can be triggered when the price is low. Commodity price fluctuations call for prudent management of fiscal revenues to ensure a source of permanent stable revenue for commodity-dependent developing countries. When public services are provided without any fee, consumers tend to overuse such services. Thus, imposing a modest fee on public services is an ideal way to support the efficient management of Government expenditure.

- It is estimated that approximately 20 per cent of the population in developing countries (2 billion people) do not have access to formal financial services, such as banking (savings and loans) and insurance. As a result, the poor face both high transaction costs and high risk in the informal financial sector for sending and receiving remittances.

- In order to enhance incentives for savings, it is necessary to ensure that real interest rates are positive rather than negative. Financial depression should be avoided.
- Taking into consideration the recent bankruptcy of some major financial institutions, there is an urgent need to establish a guideline or regulation for transparent loan terms and consumer-protection mechanisms for microcredit.
- Given the critical lack of productive capacity and relatively high cost of electricity in developing countries, further investment in infrastructure, including energy, agriculture and human development (especially education), is essential.