Comment

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Tax evasion keeps the developing world poor

Hilary Benn has called for a the west to create an African NHS, but, says Alex Cobham, the real challenge is how to harness the tax systems to fund it

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Hilary Benn, the secretary of state for international development, last Thursday called for rich countries to assist poorer ones in setting up and maintaining systems of universal healthcare, to back 10-year plans for education and to help create lifelong social security systems.

Few people would argue that these are bad ideas - but the method of funding is critical to the prospects for success. It is not a question of funding a welfare state for Africa, but rather of assessing how a welfare state can be funded in Africa.

A welfare state cannot be a gift of charity, a permanent addition to aid budgets which are already well short of the level required to meet the Millennium Development Goals (MDGs) in 2015.

Nor can the funding for a welfare state hang in the balance each year or five, as electorates and politicians in donor countries reassess their own fiscal priorities - not if health and education outcomes are to be obtained, and social security systems attain their goal of meeting minimal guarantees for vulnerable populations.

Loading these worthy goals onto an already overburdened aid agenda risks further undermining effectiveness. The limited response to the great push last summer to Make Poverty History has shown the limits to further expansion of aid budgets - highlighting the scarcity of donor resources, and the need to find alternative, sustainable finance for development.

My research shows that a conservative estimate of the revenues foregone by poorer countries due to tax avoidance and tax evasion is $385bn (£221bn) each year. Even meeting the unlikely UN goal of aid budgets equal to 0.7% of rich countries' gross national income would yield a total less than a third of that figure.

There are two main channels of lost revenues, and these lead to two distinct policy priorities for donors such as the UK's Department for International Development (DfID).

First, the inability of tax systems in rich countries to keep track of the income of high net-wealth individuals and the profits of multinational companies means that both of these groups are able to shift their tax liabilities to low-tax or no-tax jurisdictions. While this means that they avoid paying their share of state spending in rich countries, the impact is much more pernicious in the poorest countries where tax systems are weaker and other sources of revenue more limited.

The UK Treasury under Gordon Brown has taken important steps to address some of the domestic consequences of tax avoidance, but recent work carried out for the Tax Justice Network identifies a tax "gap" in the accounts of FTSE 100 companies suggesting significant work remains even at this most visible level.

For developing countries, what is important is the availability of tax-relevant information collected by rich countries and secretive tax havens jurisdictions that serve them. This means requiring information exchange as standard, to allow poor countries to identify the true profit streams of companies operating within their borders. It also means stripping tax havens of their ability to provide shelter for tax evaders - starting with the UK's own Crown Dependencies.

DfID can push for the UK to take a lead in this area, bringing other rich countries with it; the bonus being that such measures are likely to pay for themselves for rich countries too, not only freeing up resources for the poorest.

The second area in which DfID can make a useful contribution is through its influence on the wider development agenda. Tax has been neglected for too long, with two unfortunate effects.

Where it has been left to rich country experts and treated as a game of "catch-up" with the moving target of systems in rich countries, policies have often - inevitably - been inappropriate. Switching to VAT-type taxes has often undermined the possibility for redistribution, while encouraging the existence of large informal sectors - further weakening the prospects for future revenue mobilisation.

The other effect has been that tax policies are subordinated to other policies such as trade liberalisation. Complete trade liberalisation now in the poorest group of low-income countries, for example, would cost them revenues equivalent to the total removal of all aid. The IMF calculates that these countries have recovered less than a third of the revenues already lost to liberalisation; yet still the Doha talks do not include revenue guarantees nor other protections for these countries with the greatest need for revenues. Instead, they are in effect encouraged further into aid dependence.

The UK as a major donor and the DfID as a recognised leader in development policy have the opportunity to put tax firmly on the development agenda. Addressing taxation ultimately offers the only possibility for sustainable revenue mobilisation; and in the shorter term the sums involved may make it the best hope for filling the gap that has undermined the MDGs and other development aims.

By taking measures to make sure international tax structures are capable of meeting the challenges of globalisation, and recognising the importance of sustainable domestic revenue mobilisation for long-term development needs, DfID can take a step towards the welfare state in Africa that Hilary Benn has called for.