2016

# FINANCING FOR DEVELOPMENT: THE ADDIS ABABA ACTION AGENDA

*A note for facilitating the efforts of civil society organisations in India towards engaging with the discourse on financing for development*

## The Context

Three international historic and transformative agreements came into existence in 2015. These include the Addis Ababa Action Agenda (AAAA) on Financing for Development, the Agenda 2030 for Sustainable Development, and the Paris Agreement on Climate Change. The Post-2015 Development Agenda, which succeeded the United Nations' Millennium Development Goals (MDGs) in the form of Sustainable Development Goals (SDGs), promises to go beyond poverty reduction and covers the issues related to social, economic, and environmental sustainability. Further, it incorporates issues such as social inclusion, infrastructure development and climate change mitigation and adaptation. To implement SDGs, appropriate sources of finance would need to be secured; towards this, official Development Assistance (ODA) and domestic resource mobilisation both are seen as critical to finance SDGs properly in developing countries, especially with a focus on addressing inequality and social injustice. In this era of 'common but differentiated responsibility' across countries, the Third International Conference on Financing for Development (FfD3) was expected to provide all countries with a platform for discussing possible solutions to daunting issues like growing economic inequality, climate change and means of implementation of transformational agenda of SDGs.

High-level political representatives, including Heads of States and Governments, Ministers of Finance, Foreign Affairs and Development Cooperation, as well as non-governmental organisations and business sector entities gathered for FfD3 held in July of 2015. The eight plenary sessions, six multi-stakeholder round tables, two hundred side events and bilateral meetings[1] at this high level Conference focused on global partnership, dimensions of sustainable development policy coherence and an enabling environment at all levels for sustainable development. One of biggest agenda on the table in Addis was tax justice and Domestic Resource Mobilisation (DRM), and the Conference was expected to create the space for establishing a global intergovernmental tax body under the auspices of the United Nations and move towards a more just global tax regime. Notably, an important agenda item included 'consistency between macroeconomic policy and stability on one hand and sustainable development on the other'[2].

## Challenges in Mobilising Domestic Resources

The FfD3 process outlined DRM as one of the most important sources of financing SDGs in developing and Least Developed Countries (LDCs). Earlier, the Doha Conference in 2008 confirmed the need to enhance tax collection for financing sustainable development. Yet, many developing countries are not able to mobilise adequate domestic revenues,

[1] Conference Agenda and Programme, United Nations, 2015 (www.un.org/esa/ffd/ffd3/conference.html)
[2] Ensuring Policy Coherence and an Enabling Environment at all Levels for Sustainable-Background note by the Secretariat, United Nations, 2015 (http://www.un.org/esa/ffd/ffd3/wp-content/uploads/sites/2/2015/07/FfD-3_BN_Policy-coherence_05.07.15pdf)

which in turn hampers the government's ability to invest in development. The tax-GDP ratio in developing countries remains very low when compared to OECD countries, with most low income countries having a tax-GDP ratio of even less than 15 per cent.[3] In the case of India, the tax-GDP ratio falls much below the average for BRICS (Brazil, Russia, China, India, South Africa), at about 26.9 per cent (for 2012)[4]; India's total tax revenue and total public spending as percentage of GDP stood at 17.9 per cent and 27 per cent respectively (for 2013-14). In the Asia Pacific region, though some countries have tax-GDP ratios of around 25 per cent, the average for developing Asia is only about 16.9 per cent, which constrains adequate provisioning of public goods regarding education, health, social protection, and livelihood.[5]

A major obstacle to government's ability to raise revenues is caused by prevalence of narrow tax base and wide ranging tax concessions provided to private sector companies in a number of developing countries, including in India. In recent years, fiscal challenges such as tax dodging by Multinational Corporations (MNCs), lack of transparency and limitations of international tax rules are being faced by many developing countries. The existence of a wide network of secrecy jurisdictions and tax havens, along with an industry of tax lawyers have been aiding capital flight out of developing countries, resulting in loss of public revenue in these countries– thus adding to the challenge of raising adequate public resources for development. To strengthen the progressivity of the tax system in developing countries such experiences of different contexts need to be discussed to help understand the challenges and highlight lessons for improving the tax base.

**Box 1: Evolution of the Financing for Development Process**

In March 2002, the United Nations held the First International Conference on Financing for Development in Monterrey, Mexico, marking a turning point for a global partnership for sustainable development. The resulting Monterrey Consensus "resolved to address the challenges of financing for development" and "to eradicate poverty, achieve sustained economic growth and promote sustainable development." A Follow-up International Conference on Financing for Development was held in Doha, Qatar from November 29 to December 2, 2008. The challenge for the Doha agenda was to solidify the objectives of the Monterrey Consensus into more concrete commitments. The Third International Conference on Financing for Development (FfD3) held from July 13 to 16, 2015 at Addis Ababa sought to [a] assess the progress made in the implementation of the Monterrey Consensus and the Doha Declaration; [b] address new and emerging issues; and [c] reinvigorate and strengthen the financing for development follow-up process.1

## Draft outcome Document before FfFD3

The draft version of the outcome document dated May 6, 2015 offered considerable hope in the form of possible solutions to some of the issues that developing and low income countries are facing. It "commit[s] to enhance revenue administration through modernized, progressive tax systems, improved tax policy capacity and more efficient tax collection, as well as improve the fairness, transparency and effectiveness of our

[3] Revenue Mobilization in Developing Countries ,Prepared by the Fiscal Affairs Department, March 8, 2011, International Monetary Fund (https://www.imf.org/external/np/pp/eng/2011/030811.pdf)
[4] Bold Stroke and Fine Print-Analysis of Union Budget, Centre for Budget and Governance Accountability, 2015 (http://www.cbgaindia.org/publication/of-bold-strokes-and-fine-prints-an-analysis-of-union-budget-2015-16/)
[5] Data from IMF GFS for 2011, International Monetary Fund(https://www.imf.org/external/pubs/ft/gfs/manual/compil.pdf) , See also Economic and Social Survey of Asia and the Pacific 2014, chapter 4, forthcoming, United Nations Economic and Social Commission for Asia and the Pacific (www.unescap.org/resources/economic-and-social-survey-asia-and-pacific-2014).

tax systems, including through broadening the tax base."[6]. It also agreed to implement nationally appropriate social protection systems, along with specific commitments to ensure an end to hunger, increased investment in health, improved agriculture to ensure food security and delivery of quality education to all children as part of ensuring long-term sustainability of development.

To reform the global financial institutional architecture and to promote a level playing field for developing countries, the draft outcome did uphold its decision to upgrade the United Nations Committee of Experts on International Cooperation in Tax Matters to an intergovernmental committee. The Committee was expected to complement the work of other ongoing initiatives and advance the participation of developing countries in international economic decision-making and norm setting for international tax cooperation. There was a reaffirmed commitment to track illicit financial flows, while keeping in mind that the most vulnerable countries would need assistance to do so. It also encouraged countries which are significantly reliant on natural resources, to implement transparency measures such as the Extractive Industries Transparency Initiative standards. The draft outcome recognised the need for international tax cooperation to increase transparency, through measures including Country-by-Country Reporting (CBCR) by multinational enterprises, public beneficial ownership registries, and automatic exchange of tax information between countries. Additionally, there was a commitment to design capital market regulation that promotes alignment with long-term performance and sustainability, and reduces excessive market volatility. The draft outcome of FfD3 agreed to create strong regulatory frameworks to ensure that MNCs integrate environmental, social and governance issues into their reporting.

The draft outcome took cognisance of the fact that gender inequality is one of the major impediments to sustainable development throughout the world, and put forward systematic pathways by which gender equality, empowerment of women and women's full participation in the economic sphere can be achieved. Further, the draft outcome acknowledged the differentiated needs of LDCs, Land Locked Developing Countries (LLDCs), and Small Island Developing Countries (SIDS), conflict and post-conflict societies as well as the African continent. There was a marked emphasis on the need to have developed countries recommit 0.7 per cent of their GNI towards ODA, in order to complement and reinforce the effectiveness of domestic resources for sustainable development.

While the draft document did address critical gaps, there were a few glaring omissions as well. For instance, there was no mention of the need on the part of developing countries to probe the justification for wide-ranging tax incentives being given to the private sector in the hope of attracting investment. The measure of 'public' CBCR by MNCs also did not find mention in the discussion on reforms in international taxation. The following section tries to assess the progressive features of the draft outcome which got diluted in the negotiations between different groups in the run up to the summit at Addis Ababa.

[6] Revised Draft of the Outcome Document, United Nations, 2015 (http://www.un.org/pga/wpcontent/uploads/sites/3/2015/05/070515_financing-for-development-Inf-Consultations.pdf)

## The Addis Ababa Action Agenda

The agreement reached at the FfD3, called the "Addis Ababa Action Agenda" (AAAA) outlines a roadmap for implementing the global sustainable development agenda. While the agreement is rated as comprehensive and forward looking by many, the civil society organisations (CSOs) found it to be disappointing. They noted that the conference "lost the opportunity to tackle the structural injustices in the current global economic system and ensure that development finance is people-centered and protects the environment". Before the conference, there was a growing concern about the ability of many developing countries and LDCs to implement the Post-2015 Development Agenda due to unjust global taxation policies, and many LDCs had hoped concrete policy measures would be put in place for financing sustainable development.

**Box 2: Key Points of the Addis Ababa Action Agenda**

To achieve the goals, countries also agreed to new initiatives, including:

Foreign aid—Countries recommitted to the target of 0.7 per cent of GNI for official development assistance, and 0.15 to 0.20 per cent for LDCs.

A package of measures for the poorest countries—Developed countries commit to reverse the decline in aid to the poorest countries, with the European Union committing to increase its aid to LDCs to 0.2 per cent of gross national income by 2030. They also agree to adopt or strengthen LDCs investment promotion regimes, including with financial and technical support. Governments also aim to operationalize the technology bank for this group of countries by 2017.

Technology—Countries agreed to establish a Technology Facilitation Mechanism (TFM) at the Sustainable Development Summit in September to boost collaboration among governments, civil society, private sector, the scientific community, United Nations entities and other stakeholders to support the sustainable development goals.

Infrastructure—Countries agreed to establish a Global Infrastructure Forum to identify and address infrastructure gaps, highlight opportunities for investment and cooperation, and work to ensure that projects are environmentally, socially and economically sustainable.

Social protection—Countries adopted a new social compact in favour of the poor and vulnerable groups, through the provision of social protection systems and measures for all, including social protection floors.

Health—Countries agreed to consider taxing harmful substances to deter consumption and to increase domestic resources. They agreed that taxes on tobacco reduce consumption and could represent an untapped revenue stream for many countries.

Micro, small and medium-sized enterprises—Countries committed to promote affordable and stable access to credit for smaller enterprises. They also pledged to develop and operationalize a global strategy for youth employment and implement the International Labour Organization Global Jobs Pact by 2020.

Taxation—The Agenda calls for strengthening support for the work of the UN Committee of Experts on International Cooperation in Tax Matters to improve its effectiveness and operational capacity, and the engagement with the Economic and Social Council. It emphasizes the importance of inclusive cooperation and dialogue among national tax authorities.

Climate Change—The Action Agenda calls on developed countries to implement their commitment to a goal of jointly mobilizing USD100 billion per year by 2020 from a wide variety of sources to address the needs of developing countries. Countries also committed to phase out inefficient fossil fuel subsidies that lead to wasteful consumption.

Source: Media News and Press Release, United Nations, 2015 (www.un.org/esa/ffd/ffd3/press-release/countries-reach-historic-agreement.html)

Due to the extreme pressure put by many developed countries to drop the agenda of reforming global tax policies advocated by developing countries, the negotiations were flawed. Thus, the AAAA represents a step backward from the draft outcome document, and maintains status quo regarding the pre-existing commitments made in Monterrey and Doha conferences. The agenda refrains from addressing the urgent need to reform the international tax system to curtail the massive illicit flows from several developing countries. On illicit financial flows, the language used around CBCR remains weak. The Public Beneficial Ownership was done away with to replace with Beneficial Ownership for competent authorities, and the language on Automatic Exchange of Information was significantly changed. The AAAA promotes private finance as a 'solution' to finance development, and considers tax incentives as useful, even while developing countries and LDCs are losing significant amount of revenue through tax incentives provided to MNCs. The biggest glaring omission remains the refusal to upgrade the UN Committee of Experts to a democratic intergovernmental tax body.

However, there has been some momentum in two areas. A promise was made for establishment of a TFM in the conference, a longstanding demand needed for development of poor countries. It also agreed to strengthen the follow up process of FfD3 that will now include an annual meeting of "up to five days".

**Box 3: Declaration in Addis Ababa by CSO forum on FfD3**

Addis Ababa CSO FfD3 forum declaration raised some concerns:

- Gender equality considered more as smart economics than strengthening women's and girls' entitlement to social and economic rights
- Misplaced optimism towards private finance to deliver sustainable development
- International tax policy remains the domain of powerful
- No concrete commitments to ensure tax justice and equity
- No critical assessment of trade regimes, including investment treaties
- Recent UN normative developments on debt ignored
- Limited progress on technology facilitation
- UN mandate to address tax justice issues stands weakened
- No strong commitments made in terms of transparency and accountability in internal tax system

Source: Addis Ababa CSO FfD3 forum declaration, United Nations, 2015 (www.un.org/esa/ffd/ffd3/documents.html)

The concerns on the AAAA highlighted by CSOs, academia and research organisations cover a range of issues. First is heavy reliance on the private sector and Corporate Social Responsibility (CSR) in the absence of concrete accountability mechanisms in place and without a strong development role of the State. Second, the conference was not successful in scaling up existing resources and committing new financial resources apart from excessive focus on increasing role of the DRM. Further, there is a lack of adequate commitment on expansion of ODA. In the given situation, FfD3 should have made the case for revisiting the rules of international tax cooperation that are creating problems for developing countries to mobilise adequate resources from domestic sources. However, the FfD3 did not offer anything to democratise the international space for norm-setting on tax cooperation, currently captured by a group of rich countries and the OECD. One of the most discussed issues in this process was Base Erosion and Profit Shifting (BEPS). AAAA asked the world to take into account the BEPS initiative designed by OECD, and noted that the developing countries may implement the measures on BEPS taken by OECD.

Third, the AAAA failed to establish an intergovernmental, transparent, accountable, adequately resourced tax committee that would serve to be an equally representative body consisting of developed, developing and least developed countries, to deliberate on matters such as curbing illicit financial flows, tackling corporate tax dodging, etc. The AAAA did not agree to upgradation of the Committee of Experts to an intergovernmental tax body. Also, AAAA did not accept the proposal to introduce Public CBCR for MNCs. Further, the proposal for having Public Beneficial Ownership registries was diluted in AAAA. Due to this, it is difficult for citizens and governments to understand how much MNCs pay in taxes or where they make their profits.

**Box 4: Illicit financial flows from India**

The study report titled "Illicit Financial Flow from developing Countries: 2004-2013" by Global Financial Integrity found that $510 billion of black money flowed out of India from 2004-2013. It is an average annual outflow of $51 billion or Rs 3.3 lakh crore. The GFI study did not include in the estimation the amount from misinvoicing from trade in services, cash transactions and hawala transactions. The report says that trade misinvoicing of goods accounted for 83.4 percent of the $510 billon of illicit financial flows. As per Ministry of Finance estimates, India received $392.2 billon as FDI from 2002 to 2015 but it lost more than that through illicit financial flows.

Source: Illicit Financial Flows from Developing Countries: 2004-2013, Global Financial Integrity, 2015 (www.gfintegrity.org/wp-content/uploads/2015/12/IFF-Update_2015-Final.pdf)

Fourth, with regard to gender equality, the AAAA did not adequately focus on economic empowerment of women and girls. It says "A commitment to respect all human rights, including the right to development, and that member states will ensure gender equality and women's and girls' empowerment", it lacks an integrated, consistent and explicit human rights based approach. The rights of women and girls cannot be achieved without tackling the structural barriers which have created gender inequality. Issues like women's income and work, unpaid labour and unpaid care, disproportionate burden on women because of regressive tax policies need to be given greater focus to address the basic problems of gender inequality (Paragraph 21, 39).

Fifth, the AAAA has not made any progress to find a "lasting solution to the debt problem of developing countries." It has not provided support to the work going on in the UN on debt crises prevention and resolution. Furthermore, the Addis Ababa conference provided the appropriate opportunity to adopt the UNCTAD Principles on Responsible Sovereign Lending and Borrowing. These represent a mere restatement of already existing best practices and international law on the matter whose adoption has no cost but could have led to saving billions in unwarranted debt contracts and payments (Paragraph,97).

Sixth, the AAAA failed to reiterate the applicability of the principle of Common But Differentiated Responsibilities (CBDR) on the Financing for Development. This principle is crucial for the political legitimacy and genuine impact of the FfD3 agenda. The appropriate application of CBDR can also serve to reinforce all countries' abilities to fulfil the commitments in areas of human rights, labour and environment.

## Conclusion

It was expected that the FfD3 would provide all countries with a platform to discuss possible solutions to challenging issues like growing economic inequality, climate change and means of implementing transformational agenda of SDGs. Also, it was expected to create an opportunity to establish a global, intergovernmental UN tax body. While the AAAA claims to leave no one behind, it "lost the opportunity to tackle the structural injustices in the current global economic system and ensure that development finance is people-centered and protects the environment".

The AAAA does not offer the hoped-for strong financial means of implementation for commitments made in New York and Paris. In reality, the developed countries have made strong efforts to push back the developing countries from achieving the ambitious outcome. The Action Agenda represents a step backwards from the draft outcome document that came out before the conference. It upholds status quo in relation to the pre-existing commitments made in Monterrey and Doha conferences. The concern was raised that language used in AAAA around CBCR was made more straitjacketed. The Public Beneficial Ownership was done away with and replaced with Beneficial Ownership for competent authorities only. The language on Automatic Exchange of Information has changed significantly as well. The biggest glaring omission was the refusal to upgrade the UN Committee of Experts to a democratic intergovernmental tax body. It is indeed unfortunate that the main demand made by the developing countries, G77+China and CSOs for setting up an intergovernmental tax commission was not accepted. In short, although the outcome document saw commitment in a few areas, it falls short in many other areas.1

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