

CHAPTER 3

HOW TO EFFECTIVELY PROMOTE TAX GOOD GOVERNANCE IN THIRD COUNTRIES: A MISSING TOUCH-STONE ON THE EU AGENDA

*Alicja Majdanska**

Abstract

The current international development agenda presents inter-agency cooperation as one of the relevant tools that may be necessary to achieve sustainable development. This chapter places inter-agency cooperation in the context of the concept of good governance and, in particular, tax good governance. It suggests that inter-agency cooperation is an inherent element of this. Based on this assumption, the case of the good tax governance agenda of the European Union is discussed. It is recommended that inter-agency cooperation should be included as one of the tools on the EU development agenda addressing third countries. Many developing countries could benefit from the experience of EU member states in this area.

1 Introduction

In connection with the 2030 Agenda,¹ the European Union (EU) has committed itself to supporting developing countries in strengthening domestic resource mobilisation in these countries.² In light of this commitment, a new strategy ('Communication') was issued.³ This strategy addresses the way in which to fight aggressive tax avoidance. It also looks at the potential to support developing countries. According to the European Commission, Communication is a key measure for fighting aggressive tax avoidance and supporting developing countries.⁴ The

* The author would especially like to thank Jeffrey Owens for his constructive comments.

1 United Nations (2015) Resolution adopted by the General Assembly on 25 September 2015, 21 October 2015, A/RES/70/1.

2 European Commission (2015) 'Fact sheet, sustainable development goals and the Agenda 2030' 25 September 2015, http://europa.eu/rapid/press-release_MEMO-15-5709_en.htm (accessed 20 October 2016).

3 Communication from the Commission to the European Parliament and the Council on an External Strategy for Effective Taxation, COM/2016/024 final.

4 European Commission (2016) 'Fact sheet, the anti-tax avoidance package – Questions and answers (updated)' 21 June 2016, http://europa.eu/rapid/press-release_MEMO-16-2265_en.htm. (accessed 15 September 2016).

standards of tax good governance as defined by the European Commission are prominently featured in this Communication. These are the basis of the strategy applied by the EU with respect to third countries. They have been suggested as a primary tool for assessing the tax regimes of third countries. In addition, the European Commission has proposed to introduce them in bilateral trade agreements that are concluded by the EU and the member states. Finally, their implementation in third countries is expected to be supported with assistance from the EU.⁵

In an attempt to promote and enhance tax good governance among third countries, the European Commission has not recognised the role of inter-agency cooperation. This may be due to the fact that thus far the role of inter-agency cooperation in enhancing tax good governance also has not been discussed by academia or international bodies. Inter-agency cooperation has appeared on the agendas of many international bodies, including on those of the Organisation for Economic Co-operation and Development (OECD)⁶ and the Financial Action Task Force on Money Laundering (FATF),⁷ to name but a few. However, none of institutions mentioned drew a direct link between tax, good governance, inter-agency cooperation and illicit financial flows (IFFs). This chapter intends to bridge this gap.

The chapter begins with a brief introduction to the theory of good governance. It is followed by a brief account of how it occurred that taxation was recognised as a catalyst of good governance and that, as a result, tax good governance developed. Against the picture of tax good governance, the role of inter-agency cooperation is discussed. The attention then shifts to the role of the EU as promoter of good governance and tax good governance. The special focus is on Communication as the latest tax good governance agenda addressing third countries. Based on this analysis, the recommendations addressing the EU tax good governance agenda are formulated.

5 See sec 3 of this article.

6 Eg, in 2011, the OECD launched the 'Oslo Dialogue' which is designed to increase cooperation between authorities in numerous countries when approaching financial crimes, tax evasion and illicit flows. With this initiative, the whole government approach was developed. See also the report OECD *Effective inter-agency co-operation in fighting tax crimes and other financial crimes* (2013).

7 FATF 'International standards of combating money laundering and the financing of terrorism and proliferation: The FATF Recommendation' February 2012, <http://www.fatf-gafi.org/publications/fatfrecommendations/documents/fatf-recommendations.html> (accessed 20 October 2016).

2 Theory of tax good governance

2.1 Good governance

The concept of tax good governance was built on the theory of good governance. Thus, in search for the basis of the concept of tax good governance, it is necessary to first understand the concept of good governance.

Regarding the concept of good governance, it is difficult to agree on one operational definition, namely, its roots, or way of measurement.⁸ A review of the literature suggests that the sole term of governance is employed in a variety of meanings.⁹ For instance, in a number of studies by the OECD, 17 definitions of 'governance' were identified.¹⁰ A baseline consensus is that governance refers to¹¹

the development of governing styles in which boundaries between and within public and private sectors have become blurred. The essence of governance is its focus on governing mechanisms which do not rest on recourse to the authority and sanctions of government.

As some scholars have indicated, '[t]he governance concept points to the creation of a structure or an order which cannot be externally imposed but is the result of the interaction of a multiplicity of governing and each other influencing actors'.¹²

It is not surprising that the term 'good governance' is also ambiguous, and it is difficult to determine one precise definition. It appears that, according to different organisations and different actors, it may have various meanings.¹³ Some scholars, when searching for the roots of good governance, analyse the works of Aristotle and his theory of good governance as defined by the city's state of happiness achieved through the entire action of all the institutions that comprised the state mechanism.¹⁴

8 M Moore 'How does taxation affect the quality of governance?' (2007) 47 *Tax Notes International* 79-98.

9 G Stoker 'Governance as theory: Five propositions' (1998) 50 *International Social Science Journal* 17.

10 OECD *Donor approaches to governance assessments: 2009 Sourcebook* (2009).

11 Stoker (n 9 above) 17.

12 J Kooiman & M van Vliet 'Governance and public management' in K Eliassen & J Kooiman (eds) *Managing public organisations* (1993) 64.

13 RM Gisselquist 'Good governance as a concept, and why this matters for development policy' WIDER Working Paper 2012/030, Helsinki UNU-WIDER 1.

14 CA Dumitrescu 'The concept of good governance in Aristotle's view. Part II: The practical dimension' (2010) *Cogito – Multidisciplinary Research Journal* Issue 2, http://cogito.ucdc.ro/nr_3_en/1%20-%20THE%20CONCEPT%20OF%20GOOD%20GOVERNANCE%20IN%20_eng_.pdf. (accessed 13 September 2016).

Others refer to Plato for whom good governance is simply a right order.¹⁵

The theoretical basis for this chapter is a definition of good governance as refined in the development agenda. Taking into account that the aim is to examine Communication as the latest EU tax agenda with respect to third countries, for the purpose of this chapter, the meaning of the concept on the development agenda is relevant. In this context, it was decided to employ the definition as developed by the United Nations (UN) as this definition played the most important role in defining good governance. It also seems to capture the core elements common to most of the various approaches to the concept of good governance.¹⁶ In a publication by the UN,¹⁷ it was defined as being determined by eight characteristics, namely, being consensus oriented; participatory; following the rule of law; effective and efficient; accountable; transparent; responsive; and equitable and inclusive.

The first of the UN characteristics of good governance relies on being consensus-oriented, indicating that it should call for mediation of different interests in society. Good governance should aim at reaching a broad consensus in society regarding what is in the best interests of all community members.¹⁸ It should also be focused on providing sustainable development. Second, governance should be participatory. Participation in the context of good governance should be translated as providing the opportunity for participation of men and women either directly or through legitimate intermediate institutions or representatives. Third, the rule of law in this context refers to fair legal frameworks that are impartially enforced. It requires the full protection of human rights, particularly those of minorities. Fourth, good governance also requires effectiveness and efficiency. These features require the best use of the resources at their disposal. Fifth, good governance does not exist if governmental institutions as well as the private sector and civil society organisations are not accountable to the public and to their institutional stakeholders. Sixth, good governance requires transparency which means that the decisions taken and their enforcement are completed in a manner that is in

15 C-V Raiu 'An ontology of good governance. A political theory approach' (2015) 40 *Romanian Journal of Economics* 154-169, <http://EconPapers.repec.org/RePEc:ine:journl:v:40:y:2015:i:49:p:154-169> (accessed 13 September 2016).

16 There are different definitions of the term 'good governance' in the literature. Eg, Potter pointed that it encompasses a sphere of public sector management; accountability and legal framework for reforms; information and technology; legitimacy of government; and competence of governments to formulate appropriate policies, make timely decisions; execute them effectively and deliver social services to the people. D Potter 'Democratisation, good governance and development' in T Allen & A Thomas (eds) *Poverty and development into the 21st century* (2000) 379.

17 UNESCAP 'What is good governance?' <http://www.unescap.org/sites/default/files/good-governance.pdf> (accessed 14 September 2016).

18 This may be achieved through the introduction of mediation among different stakeholders. See eg K Qudrat-I Elahi 'UNDP on good governance' (2009) 36 *International Journal of Social Economics* 1167-1180, <https://doi.org/10.1108/03068290910996981> (accessed 14 September 2016).

accordance with rules and regulations. It also means that information is freely available and directly accessible to those who will be affected by such decisions and their enforcement. It requires that enough information is provided and that it is provided in easy-to-understand forms and media. Seventh, good governance should meet the standard of responsiveness which refers to institutions and processes that attempt to serve all stakeholders within a reasonable time frame. Finally, it should be based on the principle of equity and inclusiveness, which indicates that all members of society should feel included in the mainstream of society.¹⁹

All features collectively address actions primarily undertaken by government institutions. The important part of public institutions' agendas is the administration of the tax system. As was explained in the literature, '[t]he state's capacity to raise taxes is closely linked to its ability to deliver sound policies and there is much to suggest that tax raising is a good proxy indicator of overall governance capability'.²⁰ Conversely, a sound tax system is a pillar and condition of good governance. How the connection between taxation and good governance was developed will be explained.

2.2 Tax good governance

It took a long time before the association between taxation and governance was discovered and became the subject of thorough research. The main reason for this may lie in the evolution of state revenues. The importance of taxes as the primary source of revenues has in recent centuries steadily gained significance. Earlier in the seventeenth century, taxation was linked to war expenditures.²¹ However, in certain earlier works of philosophers some recognition of the role of tax systems in developing a strong and stable country is evident. For instance, both Aristotle and Confucius identified a fair and effective tax system funding a political leadership and administration as a requirement for a prosperous and politically stable society.²² Adam Smith also observed that '[l]ittle else is requisite to carry a state to the highest degree of opulence from the lowest barbarism but peace, easy taxes, and a tolerable administration of justice; all the rest being brought about by the natural course of things'.²³

19 Many scholars later on in the literature referred to those principles. See eg U Karpen 'Good governance' (2010) 12 *European Journal of Law Reform* 16-31; JJ Shananbli 'Good governance' (2012) 2 *AGORA International Journal of Juridical Sciences* 176-181; V Mallika Vedantham & S Kamruddin 'Good governance and public policy in India' (2015) 1 *PEOPLE: International Journal of Social Sciences* 878-889.

20 M Everest-Phillips 'State-building taxation for developing countries: Principles for reform' (2010) 28 *Development Policy Review* 76.

21 M Moore 'How does taxation affect the quality of governance?' (2007) 47 *Tax Notes International* 19.

22 Everest-Phillips (n 20 above) 76.

23 Stewart reported this as the view of his friend Smith in D Stewart 'Account of the life and writing of Adam Smith, LLD' in Adam Smith's posthumous *Essays on Philosophical Subjects*, 1795, lxxx, lxxxi. <https://www.adamsmith.org/adam-smith-quotes/> (accessed 12 December 2017).

The literature review suggests that since the early twentieth century, taxation has been perceived as central to state building. At that time, it began to be associated with revenue creation; the redistribution of income and assets; the curbing of socially undesirable behaviour, for example, by means of tobacco and alcohol taxes (repricing); and the realm of democratic state building (representation). The last dimension – representation – was presented as the emanation of the need for revenues. A corollary of this was the creation of representative governments. This vision of the role of taxation evolved over the course of time, and it became obvious that there is a close association between taxation and government services in general.²⁴ The level of taxation is not contested as long as commensurate government services are provided to citizens. Stated differently, there is a direct link between taxation and democratisation as such.²⁵

In general, there now is substantial research material on the correlation between tax and governance. It is worth noting what Trevor Manuel, then Finance Minister of South Africa, recognised: 'Effective revenue administration contributes to a country more than simply filling its national coffers; it is an essential component of good governance.'²⁶

To paraphrase these words: There is no good governance without a tax system that would satisfy all the characteristics of good governance. It is the condition that addresses the operations of tax administrations and its organisation as well as the law and all legislative and administrative processes. All aspects of administering and creating a tax system must meet the criteria of good governance. What does this mean?

First, tax good governance should be consensus-oriented that could be translated as a requirement of a tax system that is the result of consensus reached not only in works of a parliament representing society, but also in cooperation with a wider society represented by civil society, trade unions, and so forth. In the context of the administration of a tax system, it may require openness to taxpayers and providing an opportunity to communicate. In this respect, it will also meet the requirement of being participatory and involving all stakeholders in building a tax system. Second, good governance requires that all stakeholders that can contribute to building a tax system be invited to do so. Third, a tax system should also meet the requirements as imposed by the rule of law, both its formal and substantive elements. This means that it should meet all institutional

24 ML Ross *Does taxation lead to representation* (2004) 230.

25 D Brautigam *Governance and economy: A review* (1991) WPS 815, World Bank as referred to in Moore (n 21 above) 9; W Prichard 'The politics of taxation and implications for accountability in Ghana 1981-2008' IDS Working Paper 330, July 2009 7.

26 Opening speech at the International Conference on Taxation, State-Building and Capacity Development in Africa, hosted by the South Africa Revenue Service as referred to in Everest-Phillips (n 20 above) 75.

requirements (laws made by duly-empowered institutions, access to independent courts), procedural requirements (fair representation, due process, rights of appeal), and requirements addressing the content of the law (generality, certainty, proportionality, equal treatment).²⁷ Fourth, the feature of effectiveness and efficiency requires that a tax system be administered by making the best use of the resources at its disposal. It may be reflected in development of risk management strategies and implementation of compliance risk management.²⁸ Fifth, a tax system should be based on accountable institutions. Sixth, a tax system should be transparent. Transparency currently is often used with respect to increased pressure on transparency among taxpayers' data.²⁹ In the context of tax good governance, the request for transparency requires not only transparent taxpayers but, first of all, transparency around tax administrations and their operations.³⁰ Seventh, a tax system should be responsive, which indicates that tax administrations should be able to modify their operations and decisions for a specific taxpayer's situation.³¹ Finally, it should be based on the principle of equity and inclusiveness which, building on substantive elements of the rule of law, is again supported by an invitation to all stakeholders for building a tax system.³²

2.3 Inter-agency cooperation as an effective and efficient measure in the promotion of a tax good governance agenda

As has been discussed, one of the pillars of good governance and tax good governance is effectiveness and efficiency. Whereas effectiveness addresses the results of tax administrations' operations, efficiency refers to the issue of costs that tax administrations must bear. Achieving these goals may require different measures depending on the types of operations. Among many functions allocated to a tax administration, one of its core roles is to enforce tax law. Currently, many tax administrations develop various risk management strategies that allow for adjusting their operations to targeted tax behaviour. Thus, they build their operations based on the enforcement pyramid that differentiates between compliant;

27 J Freigang 'Is responsive regulation compatible with the rule of law?' (2002) 8 *European Public Law* 463.

28 See eg OECD 'Compliance risk management: Managing and improving tax compliance' (2004) <https://www.oecd.org/tax/administration/33818656.pdf> (accessed 16 October 2017).

29 J Grocott 'Time for tax transparency and clarity' (2010) 21 *International Tax Review* 13-15; TA Kaye 'Tax transparency: Tale of two countries' (2016) 39 *Fordham International Law Journal* 1153-1200; A Pross 'How tax transparency went global in 2014' (2015) 26 *International Tax Review* 10-13.

30 This is also a requirement under the Tax Administration Diagnostic Assessment Tool. For more, see <http://www.tadat.org> (accessed 16 October 2017).

31 For a discussion on responsiveness in the context of tax administration, see L Osofsky 'Some realism about responsive tax administration' (2012) 66 *Tax Law Review* 121.

32 M Everest-Phillips & R Sandall 'Linking business tax reform with governance' *Investment climate in practice* (2009) 48314 <https://openknowledge.worldbank.org/bitstream/handle/10986/10572/483140BRI0link10Box338894B01PUBLIC1.pdf?sequence=1> (accessed 16 October 2017).

willingness to be compliant; compliant only if they are controlled; and non-compliant taxpayers.³³ Whereas most operations can be undertaken by tax administrations on their own solely with capacities they already are equipped with, in some cases they may require support from and expertise of other agencies. In particular, this is the case when they identify non-compliant taxpayers who commit tax crimes.³⁴

Tax crimes commonly are committed along with other crimes such as money laundering, corruption, drug trafficking, and many others. They sometimes are referred to as 'illicit financial flows' (IFFs).³⁵ It is important to emphasise that there are substantial similarities between the techniques exploited to commit these different types of crimes. Money launderers, tax evaders and bribe takers intend to conceal the illicit origins of funds and integrate them into apparently legitimate sources. Therefore, they manipulate prices (over- and under-invoicing), manipulate turnover/sales, fabricate loans, fabricate a rise in net worth of purchased and sold items, and use trusts and shell companies. Their ultimate goal is to create apparent legal origins of illicitly-obtained proceeds to enable them to use these and benefit from them as if they were legal. All activities undertaken here thrive on secrecy, inadequate legal frameworks, tax regulation, poor enforcement, and weak inter-agency cooperation.³⁶ Moreover, conduct involving money laundering, corruption or other economic crimes usually is also a tax crime. In this context, it should be recalled that international standards³⁷ recognise a tax crime as a predicate offence to money laundering.³⁸

Bearing this in mind, it is not surprising that a large number of agencies may be involved in countering IFFs. They detect, investigate and prosecute crimes resulting in IFFs. They also carry out preventive activities. Finally, they are in charge of the recovery of proceeds.³⁹ Considering the criminal character of most IFFs, police forces and prosecution authorities play an important role here. Tax and customs administrations as well as financial regulators also are relevant. In the course of their normal activities, tax and customs administrations and financial regulators collect and retain information which might be

33 OECD (n 29 above) 41.

34 OECD *Tax administration 2017: Comparative information on OECD and other advanced and emerging economies* (2017) 103 http://dx.doi.org/10.1787/tax_admin-2017-en (accessed 16 October 2017).

35 OECD (n 6 above).

36 A Fontana & K Hansen-Shino 'Implementing the illicit financial flows agenda: Perspectives from developing countries' (2012) Chr Michelsen Institute (U4 Brief 2012:8) 4.

37 FATF (n 7 above).

38 See, inter alia, R Tavares 'Relationship between money laundering, tax evasion and tax heavens' (2013) EU Special Committee on Organized Crime, Corruption and Money Laundering (CRIM) 2012-2013, thematic paper on money laundering; A Storm 'Establishing the link between money laundering and tax evasion' The Clute Institute Academic Conference, Munich, 2014.

39 OECD (n 6 above).

necessary in the detection and investigation of IFFs. With respect to tax administrations, it should be emphasised that a tax crime is perceived as one of the major sources of IFFs. Some studies even indicate that the majority of all IFFs are related to cross-border tax-related transactions which would require cross-border cooperation.⁴⁰ That is why, in order to be effective and efficient, as is required by good governance criteria, a tax administration should establish cooperation with law enforcement agencies, a so-called inter-agency cooperation which builds on a 'whole-of-government' approach.

Entering into inter-agency cooperation may substantially enhance efforts of a tax administration and also other agencies in stemming illicit financial flows. Among many benefits of the concept of inter-agency cooperation are increased effectiveness of agencies participating in this cooperation; improved chances of stemming IFFs; operational efficiency; and an improvement in agencies' skills due to collaboration. It is also a way in which a tax system may become better integrated with other agencies. From a good governance perspective, it may contribute to promoting inclusiveness by replacing separate actions of different agencies with a collaborative effort. Inclusiveness is being repeated by many fora as a key element in building capacities, ensuring sustainable sources of government revenue and, finally, supporting good governance.⁴¹

Inter-agency cooperation may be framed in different ways. This may range from tools as simple as joint training that supports an exchange of expertise and discussing obstacles faced, to more enhanced forms such as joint investigations or even special task forces.⁴²

The value of inter-agency cooperation has been recognised by the international community. Many developed countries have initiated special programmes based on inter-agency cooperation as an effective and efficient way of preventing, detecting, tracking and prosecuting illicit financial flows. Joint investigation teams, inter-agency centres of intelligence and secondments, and co-location of personnel are but some

40 United Nations *Final study on illicit financial flows, human rights and the 2030 Agenda for Sustainable Development of the Independent Expert on the effects of foreign debt and other related international financial obligations of states on the full enjoyment of all human rights, particularly economic, social and cultural rights* (2016) 15 January 2016, A/HRC/31/61 3.

41 It is worth referring to the Agenda 2030 that states: 'We envisage a world in which every country enjoys sustained, inclusive and sustainable economic growth and decent work for all. A world in which consumption and production patterns and use of all natural resources – from air to land, from rivers, lakes and aquifers to oceans and seas – are sustainable. One in which democracy, good governance and the rule of law, as well as an enabling environment at the national and international levels, are essential for sustainable development, including sustained and inclusive economic growth, social development, environmental protection and the eradication of poverty and hunger. One in which development and the application of technology are climate-sensitive, respect biodiversity and are resilient. One in which humanity lives in harmony with nature and in which wildlife and other living species are protected.'

42 OECD (n 6 above) 14-18.

examples of existing strategies of inter-agency enhanced cooperation. A number of interesting initiatives were developed in The Netherlands,⁴³ the USA,⁴⁴ Australia and Finland.⁴⁵

International organisations have also recognised the value of inter-agency cooperation. It began with the Communiqué by the G20 Leaders who, at the 2011 Cannes Summit, called for the adoption of and compliance with the international standards in the tax, prudential, and AML/CFT areas, and requested international organisations to ‘work closely together to enhance transparency and facilitate cooperation between tax and law enforcement agencies in the implementation of these standards’. The initiative was adopted by the OECD, the World Bank, the International Monetary Fund (IMF), the FATF and the UN. However, thus far there has been no involvement of the EU. This may be surprising considering the fact that the EU promotes the concept of good governance and tax good governance.

3 European Union tax agenda as a case study

3.1 Rationale for the new tax good governance agenda within the European Union framework

The EU introduces itself as a leader in promoting good governance in tax matters and the principles of transparency, the exchange of information, and fair tax competition that are now worldwide gaining traction. It is noteworthy to recall the OECD discussion paper on ‘A Contribution to the Third Financing for Development Conference in Addis Ababa’. Here the EU stated:⁴⁶

... put the EU at the forefront in improving tax governance within its own borders and given the EU a leading role in pushing for an ambitious global agenda. Major improvements have been made in tax governance in the EU internal market while taking into account implications for third countries.

43 In 2013 the criminal investigations leg of the Netherlands Tax and Customs Administration established a Centre for Intelligence and Operational Excellence. The Centre consists of authorities that are involved in any actions against money laundering.

44 The United States established the Organized Crime Drug Enforcement Task Force Fusion Center (OCDETF-FC) in 2006 under the auspices of the Department of Justice, Homeland Security and the Department of Treasury.

45 Eg, in Finland the Grey Economy Information Unit (GEIU) was established. It aims at promoting the fight against the shadow economy. The GEIU collects information from different authorities, regardless of existing confidentiality provisions.

46 European Commission ‘Collect more – Spend better. A contribution to the third financing for Development Conference in Addis Ababa’, Discussion paper (2015), https://ec.europa.eu/europeaid/sites/devco/files/com_collectmore-spendbetter_20150713_en.pdf (accessed 19 October 2016).

Tax good governance was developed by the EU primarily with respect to a policy that addresses third countries. The first proposal of minimum standards of tax good governance was issued in the Commission Recommendation regarding measures intended to encourage third countries to apply minimum standards of good governance in tax matters in 2012,⁴⁷ although the concept of pure good governance had even earlier been present on the EU agenda.⁴⁸ The recommendation included the set of rules addressing third countries. The rules were aimed at incentivising third countries to meet the standards of tax good governance. Three of these standards, namely, transparency, exchange of information and fair tax competition, were regarded as the core of the recommendation. Thus, they were seen as criteria in the assessment of third countries' tax regimes. In case of non-compliance with these core rules, common counter-measures could be applied. The criteria were approved by the Economic and Financial Affairs Council (ECOFIN). Next, they were used in the course of work of the Platform for Tax and Good Governance.⁴⁹ Very soon it was recognised that the rules needed to be updated.

First of all, over the course of time it was recognised that the criteria were used in an inconsistent manner, and sometimes not at all⁵⁰ in regard to both their application by the Platform for Tax and Good Governance as well as by member states. This lack of a coherent approach resulted in the need for more clarity.

In addition, the EU Tax Good Governance criteria had become obsolete. Since 2012, when the recommendation was issued, there have been many advancements on the tax agenda. The automatic exchange of information has become widespread across many countries around the world and gathered the support of the largest economies.⁵¹ However, it was the BEPS project,⁵² led by the OECD under the auspices of the G20 Leaders, who significantly reshaped the international tax agenda and

47 Brussels, 6.12.2012 C(2012) 8805 final.

48 As early as 1991 the European Council in Luxembourg (European Council 1991) and the Council of Development Ministers each adopted a declaration (Resolution of the European Council, 28 November 1991, OJ EEC 11-1991: 122ff) responding to the international debate on good governance. For more, see TA Börzel et al 'Good governance in the European Union' Berlin Working Paper on European Integration, No 7, 2008, http://www.polsoz.fu-berlin.de/polwiss/forschung/international/europa/arbeitspapiere/2008-7-Boerzel_et_al_GoodGovernance.pdf (accessed 21 October 2016).

49 The Platform for Tax and Good Governance brings together representatives from business, civil society, trade unions and national tax administrations. It was established in 2013 in the context of an Action Plan to strengthen the fight against tax fraud and tax evasion presented by the Commission in 2012. In 2015 it was decided to prolong its mandate. For more, see https://ec.europa.eu/taxation_customs/business/company-tax/tax-good-governance/platform-tax-good-governance_en (accessed 16 October 2017).

50 The Communication, point 2.

51 For more details, see: <https://www.oecd.org/tax/automatic-exchange/> (accessed 21 June 2016).

52 Base Erosion and Profit Shifting (BEPS) Project. For more details, see <http://www.oecd.org/ctp/beps-about.htm> (accessed 16 October 2017).

influenced the understanding of good governance criteria. Following the creation of new standards created by the OECD under the BEPS project, the EU faced the necessity to update its agenda and apply a common approach across all member states in order to answer the current tax challenges in a consistent matter. As a result, the Action Plan for Fair and Efficient Corporate Taxation in the EU (Action Plan)⁵³ was developed. The Action Plan proposed five key areas for action: re-launching the Common Consolidated Corporate Tax Base (CCCTB); ensuring fair taxation where profits are generated; creating a better business environment; increasing transparency; and improving EU co-ordination. From the perspective of the EU Single Market, it aims at ensuring that all member states adopt a coordinated approach against the phenomenon of profit shifting and base erosion.

As a follow-up to the Action Plan, on 28 January 2016 the European Commission released the Anti-Tax Avoidance Package (ATA Package).⁵⁴ The new set of measures was suggested with the intention of ensuring that a minimum standard against the phenomenon of base erosion be established across all member states. As was explained by the European Commission, the ATA Package offered immediate solutions to tackle tax avoidance, boost tax transparency, and ensure a fairer and more stable business environment. As a next step, the Commission proposed the relaunch of the Common Consolidated Corporate Tax Base (CCCTB) project.⁵⁵ The relaunch was announced in October 2016.⁵⁶ It was suggested that the project would be implemented through a two-step process and that it would be compulsory for the largest groups of taxpayers in the European Union.⁵⁶

The integral part of the ATA Package is Communication. The Communication does not have a binding form, constituting only soft law. Thus, as a soft law instrument, it only requires endorsement by the Council

53 See press release http://europa.eu/rapid/press-release_IP-16-159_en.htm (accessed 16 October 2017).

54 On 20 June 2016 tax commissioner Pierre Moscovici stated that the EU Commission would relaunch proposals for a common consolidated corporate tax base (CCCTB) in the EU in the autumn of that year. He confirmed that '[b]usinesses and investors need simplicity, certainty, and a level playing field. They also need a swift and efficient system to solve double tax disputes and the Commission will make proposals to improve the current situation by the end of this year. This will come together with the real prize for businesses: the CCCTB, which the Commission will re-launch in the autumn.'

55 European Commission 'Commission proposes major corporate tax reform for the EU' Press release, 25 October 2016, Strasbourg, http://europa.eu/rapid/press-release_IP-16-3471_en.htm (accessed 23 November 2016).

56 European Commission, Proposal for a Council Directive on a Common Corporate Tax Base, COM (2016) 685 final, 2016/0337 (CNS), https://ec.europa.eu/taxation_customs/sites/taxation/files/com_2016_685_en.pdf. (accessed 23 November 2016).

and Parliament. Communication on an External Strategy already has been endorsed by the ECOFIN.⁵⁷

3.2 New approach to promoting tax good governance

Within Communication, the EU Commission suggested several tools that should internationally promote tax good governance. These are implementing tax good governance clauses and state aid provisions in agreements with third countries; assisting developing countries in improving their tax systems and increasing their domestic resources; developing a common approach to listing third countries; and strengthening the relationship between EU funds and tax good governance. To understand how these tools fit the definition of good governance and tax good governance, it is essential to comment on each of the suggested tools.

The first items proposed in Communication suggests inserting a good governance clause to treaties concluded with third countries. The idea as such is not novel. Since 1995 it has been the official policy of the EU to include references to democratic principles and human rights in agreements between the EU and third countries. The most prominent of this practice is the clause agreed to in the Cotonou Agreement.⁵⁸ In 2008, the uniformed wording of such a clause was agreed upon. It was seen as a basis for future tax good governance clauses in international agreements. The Commission was given a mandate to negotiate this type of clause. In the meantime, the international tax environment dramatically changed, whereas the suggested good governance clause quite often was the subject of discussion during the negotiations around the treaties, and caused delays in reaching final consensus. In a direct response to these issues, the EU Commission set out core elements in the Communication of good governance which should be included in a negotiated treaty. The Communication included transparency and exchange of information upon request; Automatic Exchange of Information (AEOI) of financial account information; fair tax competition; G20/OECD BEPS Standards; and FATF Recommendations.⁵⁹

The EU Commission acknowledged that in some cases, countries may not be prepared to meet all the criteria. It was suggested that in these cases member states should adopt a different approach. The EU Commission

57 Council conclusions on an external taxation strategy and measures against tax treaty abuse, 25 May 2016, <http://www.consilium.europa.eu/en/press/press-releases/2016/05/25-conclusions-tax-treaty-abuse/> (accessed 15 June 2016).

58 Art 9 of the Cotonou Agreement signed in Cotonou on 23 June 2000 includes reference to good governance standards that should underpin the domestic and international policies of parties to the agreement and constitute a fundamental element of the agreement.

59 FATF (n 7 above).

referred to two potential solutions. Member states can try to offer a so-called 'simplified approach'. Another option would be to support these countries in the implementation of the clause. It remains to be seen whether member states will abuse this gateway to create a myriad of differentiating good governance clauses. Considering that there are 28 member states, it is easy to conceive that each of these may compose dissimilar good governance clauses. Whereas diversity should be welcomed, it should not be equal to diminishing standards.

A new interesting measure that was suggested in Communication is the monitoring of whether a third country is compliant with the good governance clause inserted in the agreement. In the event of its violation, the agreement's consultation mechanism should be initiated. The implementation of this proposal would be a long-anticipated change on the EU good governance agenda. One of most important weaknesses of previous good governance clauses was the lack of a proper operational mechanism for the implementation, the monitoring of compliance with the clause, and an evaluation of the effectiveness of sanctions. As was sometimes pointed out, the EU policy in respect of enforcing good governance was 'aspirational' and aimed at fostering dialogue.⁶⁰ The EU Communication provides no additional details of how this mechanism will function.

Along with the good governance clause, state aid provisions would have a dissuasive influence on any type of harmful subsidies when included in agreements with third countries, and would ensure that government interventions do not distort competition. Therefore, it was also suggested that they be included. Taking into account the active position over previous years of the European Commission in enforcing state aid provisions, it could be accepted that the new clause may play an important role in shaping the relationship with companies from third countries that are active in the EU.

Communication also discusses a suggestion to assist third countries in mobilising domestic resources. In particular, this can be done by strengthening their tax systems. It is an important position on the EU tax good governance agenda since it is an indication of preference for an active approach towards promoting good governance in third countries. Good governance should be not only a clause in a treaty, but should also demand implementing a certain policy agenda, and the EU should provide the required support in its implementation. In this respect, the EU intends to follow its strategy regarding developing countries that was presented in the 'Collect More – Spend Better'.⁶¹ Within this initiative, the EU intends to

60 N Hachez 'Essential elements clauses in EU trade agreements making trade work in a way that helps human rights?' Working Paper 158, April 2015 21, <https://ghum.kuleuven.be/ggs/publications/wp158hachez.pdf> (accessed 17 July 2016).

61 European Commission (n 48 above).

address tax policy and tax compliance gaps. This can be achieved by adopting various measures addressing both the substantive laws of taxation as well as law of tax administration and procedure. The aim of the EU is to address aggressive tax avoidance and tax evasion. In this respect, the EU Commission also alludes to the issue of illicit financial flows. However, it does not articulate what should be initiated to address the issue. Only in a number of earlier documents was there a proposal of strengthening monitoring capacities in the fight against illicit financial flows.⁶² This suggests a rather limited scope of operations that target these flows, whereas nothing has been suggested with respect to inter-agency cooperation. It appears that the EU agenda is focusing only on pure tax or public finance issues. The EU Commission is silent on a 'whole-of-government' approach.

The next suggested measures resurrect the antiquated concept of blacklisting.⁶³ In Communication, the Commission suggests a system consisting of three steps. These are assessing; screening; and listing third countries. The first 'go' of the EU blacklist was in 2015, but it was heavily criticised internationally. The wider society commented that it lacked objectivity and logic concerning which jurisdictions were on the list.⁶⁴ The new EU blacklist is based on a screening and listing process. The process addresses countries that do not 'play fairly'.

In order to identify these countries, a common EU list of third countries will be developed within a three-step process (a scoreboard phase, a screening phase and a listing phase).⁶⁵ The first step is the identification of the jurisdictions to be prioritised for screening at the EU level. The basis for prioritisation would be a scoreboard of indicators described in Communication.⁶⁶ The second step consists of a selection of jurisdictions for the assessment and the actual assessment. The selection would be done based on the outcome from the first step. This would be followed by the assessment, done by the EU Commission. In the assessment, the EU Commission would take into consideration the Code

62 Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee – Tax and Development Co-operating with Developing Countries on Promoting Good Governance in Tax Matters COM (2010) 426.

63 In a report issued in 2000, the OECD identified a number of jurisdictions as tax havens according to criteria it had established. However, in 2009, the last three countries were removed from the list and, since then, the initiative has not been relaunched. For more, see <http://www.oecd.org/countries/monaco/listofunco-operativetaxhavens.htm> (accessed 17 July 2016).

64 For more comments, see V Houlder 'Tax blacklist provokes offshore fury' *Financial Times* 22 June 2015.

65 For a detailed description, see 'Common EU list of third country jurisdictions for tax purposes', https://ec.europa.eu/taxation_customs/tax-common-eu-list_de (accessed 17 October 2017).

66 On 14 September 2016, the Commission completed a scoreboard of all third countries and jurisdictions for tax purposes. For the results, see https://ec.europa.eu/taxation_customs/sites/taxation/files/2016-09-15_scoreboard-indicators.pdf (accessed 17 October 2017).

of Conduct for Business Taxation. Finally, the third step is an agreement on a list. Based on a recommendation by the Commission, member states will agree on the countries that need to be on the list. Communication did not address the counteraction⁶⁷ against listed countries.⁶⁸

The developed procedure promotes good governance and enhances its implementation. It attempts to avoid the previous massive criticism of being arbitrary.⁶⁹ According to the EU Commission, the procedure should be more transparent. The format of the information should also be easier to access. This proves that high standards of good governance mirrored in a transparent policy are relevant to the EU.

Nonetheless, it may be doubtful how effective the mechanism of the listing will be. The entire process of listing third countries seems to be quite complex and long. It is not surprising that the Commission stated that it will be applied only in exceptional cases. According to the Commission, '[l]isting a jurisdiction should always be considered as a last resort option. It should be reserved for those jurisdictions that refuse to engage on tax good governance matters or fail to constructively acknowledge EU concerns with their tax systems.'⁷⁰ This may undermine the idea of listing and make it an even weaker mechanism. The process already has been criticised by some non-governmental organisations (NGOs) as being 'doomed to fail' because it will not include some countries where international financial secrecy thrives.⁷¹

Finally, Communication also recognised the role of international financial institutions in promoting good governance. The EU Commission referred to the EU Financial Regulation⁷² (article 140(4)). In particular, it discussed the ban on investing and channelling EU funds through entities in third countries if these do not comply with international tax transparency standards.

67 The options that have so far been considered are a possibility to review and even suspend free trade agreements and prohibiting access to EU funds.

68 A detailed description of the process of deciding on the EU list of non-cooperative jurisdictions is described in the Communication.

69 Although the new list will be the result of certain proceedings and will be based on clear criteria, it was welcomed with some criticism, particularly by NGOs. They claim that it is 'a highly political exercise, where rich and powerful countries such as the US and Switzerland are protected from blacklisting'. See <https://financialtransparency.org/false-eu-promise-listing-tax-havens/> (accessed 17 July 2016).

70 Communication, 5.3.

71 Tax Justice Network 'The false promise of tax haven blacklists' <http://www.taxjustice.net/2016/05/31/the-false-promise-of-tax-haven-blacklists/> (accessed 21 October 2016).

72 Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council of 25 October 2012 on the financial rules applicable to the general budget of the Union and repealing Council Regulation (EC, Euratom) No 1605/2002 (Official Journal L 298 of 26 October 2012).

4 Call for promotion of inter-agency cooperation as a way of enhancing tax good governance in third countries

The new EU agenda promoting good governance in relationship to third countries is an important increment in promoting and enhancing good tax governance. Many developing countries experience weak governance and, as a result, widespread corruption, tax evasion and money laundering. With the suggested set of policy instruments, the EU, given its unquestionable political impact and important role on the international agenda, may have a unique opportunity to improve the situation whereby none of the competing parties has an advantage at the initiation of a competitive activity in many third countries. However, a thorough analysis reveals certain weaknesses of the updated EU agenda.

In the context of the conducted analysis, it appears that the EU thus far has not recognised the value of inter-agency cooperation as a tool that not only tackles illicit financial flows, but also increases the effectiveness and efficiency of tax administrations and promotes inclusiveness within a frame of a 'whole-of-government' approach. This is quite surprising considering the wide array of actions suggested in Communication.

It may even be more surprising considering current initiatives undertaken over the last few years by many member states of the EU. On such an initiative, the Croatian State Prosecutor's Office for the Suppression of Organized Crime and Corruption (USKOK) is a Croatian agency supervised by the state attorney's office but which also cooperates with the tax administration⁷³ or Tax Cobra, a cooperation of police, custom and finance administration in the Czech Republic.⁷⁴ The concept of inter-agency cooperation seems to be widespread in Europe, and many countries have well-grounded experience in this field.

Considering the experience of developed countries experienced in this area, they could assist those that are still developing to increase their knowledge on how the effective and efficient inter-agency cooperation should be constructed. Existing studies suggest that there still are many legal and practical challenges that will need to be overcome.⁷⁵ The role of developed countries is to share their experiences of how the issues of confidentiality, sharing information and responsibilities could be addressed. It seems that thus far not much has been done. Various

73 S Hodžić 'National report: Croatia' paper presented at the conference 'Improving tax compliance in a globalised world', Rust, Austria, 30 June-2 July 2016.

74 D Nerudová & J Tepperová 'National report: Czech Republic' paper presented at the conference 'Improving tax compliance in a globalised world' (n 74 above).

75 A Majdanska et al 'Inter-agency co-operation and illicit financial flows in Africa' Working Draft.

international stakeholders are focusing on tax cooperation whereas, to face the challenges of many modern threats (eg IFFs) and to ensure sustainable sources for development, cooperations should include more agencies than tax administrations.

At the same time, when examining the experience of some developing countries, it appears that many of these countries continue to struggle with constructing efficient channels for inter-agency cooperation.⁷⁶ A good case study may be sub-Saharan African countries. Capacity in sub-Saharan African countries is limited and further complicated by the need to significantly improve cooperation between existing institutions. Even where appropriate architectures of government agencies are in place, the effectiveness of their work is diminished by the lack of cooperation. Responsibilities are duplicated, and information is very limited.⁷⁷

Nigeria is an example of an African country where many regulatory agencies already exist, for instance, the Special Control Unit Against Money Laundering or the Nigerian Financial Intelligence Unit. Nevertheless, the country ranks in the top five African countries by cumulative IFFs in the period 1970 to 2008. The situation may be the result not only of inadequate capacities of existing institutions, but also the lack of coherence between them. Again, some responsibilities between agencies are duplicated.⁷⁸

On the other hand, a slow move in the direction of inter-agency cooperation can be observed. Kenya is an example of a less-developed country that implemented inter-agency strategy. In 2015 Kenya established the Multi-Agency Team (MAT) on Corruption and other Economic Crimes that ensures the cooperation of a number of agencies on a regular basis.⁷⁹ There is evidence that the MAT has been used successfully to share information between the various agencies, and a number of cases are currently before court as a result of information sharing.⁸⁰

76 Report of the High-Level Panel on Illicit Financial Flows from Africa commissioned by the AU/ECA Conference of Ministers of Finance, Planning and Economic Development 36 (UNECA Report) http://www.uneca.org/sites/default/files/publications/iff_main_report_26feb_en.pdf (accessed 10 September 2016).

77 S Chrispin, 'Pressure grows to tighten global tax rules' 31 October 2014, <http://www.bbc.com/news/business-29850055> (accessed 15 September 2015).

78 UNECA Report (n 77 above) 36.

79 Country Statement by Ambassador Michael AO Oyugi, Ambassador/Permanent Representative of the Republic of Kenya to the UN and the International Organisations in Vienna, Austria and Leader of Delegation, 15 November 2016, 7th session of the Meeting of the Implementation Review Group of the UN Convention Against Corruption, Vienna, Austria, <https://www.unodc.org/documents/treaties/UNCAC/WorkingGroups/ImplementationReviewGroup/14-16November2016/Statements/Kenya.pdf> (accessed 17 October 2017).

80 A Majdanska et al 'Inter-agency co-operation and illicit financial flows in Africa', paper presented at the 2nd annual congress on Financing Sustainable Development in Africa: Identifying Untapped and Underutilised Sources of Revenue, Seychelles, 5-7 September 2016.

It cannot be ignored that inter-agency cooperation not only is a tool that affords an opportunity to effectively address certain types of crimes. It may also address issues of scarce capacities which, when coupled with complex law systems and opaque administration, become unable to effectively utilise law enforcement and ultimately enables IFFs to flourish. Efficient inter-agency cooperation could mitigate some of these problems. The benefits of implementing this strategy that may be most important from the perspective of the least developed countries could be providing a sustainable source of revenues; promoting good governance; capacity building; and, finally, improving effectivity and efficiency of law enforcement.

The effective fight against illicit financial flows demands the participation of different sets of actors. Among them, tax authorities, customs administrations, the police, financial intelligence units and anti-corruption agencies play the most significant role. Therefore, the slow move to inter-agency cooperation in some developing countries must be welcomed and support from international fora must be demanded.

5 Conclusions

In terms of enhancing good governance, the inclusiveness and participation of main stakeholders are of great value. An important dimension is cooperation. Cooperation should stand as an invitation to all stakeholders. It also refers to good governance in taxation. This statement implies a twofold collaboration. It not only is about collaboration between tax administration and taxpayers. Cooperation between tax administration and other types of law enforcement agencies, both at the international and domestic levels, plays an equally significant role in countering different types of illicit financial flows. The shift to a cooperative approach among different governmental bodies could be a long-term project that may result in preventions that are more effective and efficient in detecting, investigating and prosecuting different types of illicit financial flows. From the perspective of developing countries, creating this type of cooperation is of the greatest importance. It also equals access to data, experience and knowledge of other agencies required by the tax administration. Their limited capacity could gain in cooperation with financial intelligence units and different law enforcement agencies.

Taking into account the rich experience of member states, the EU has a unique opportunity to promote the concept of inter-agency among developing countries. It may help design appropriate modes of information exchange and subsequent communication channels. By improving cooperation between tax administrations and other law enforcement agencies, the efficiency and effectiveness of tax administrations could be improved. In this manner, it may fulfil its commitment to strengthen domestic resource mobilisation in developing countries. Tax

administrations as well as other law enforcement agencies would be better informed and equipped to conduct investigations. Finally, by supporting cooperation at the inter-institutional level, the EU could contribute to building enforcement agendas of third countries that are more coherent. In the same way, the EU would also fulfil its obligation of supporting the achievement of Sustainable Development Goals.

In examining the operations of other international bodies, inter-agency cooperation already is present on the agendas of the OECD, the World Bank Group and the IMF. Perhaps it is the right time for the EU to join these institutions and support developing countries in building their good governance agenda by implementing inter-agency cooperation.

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