MINISTRY OF FINANCE
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SPEECH BY MINISTER OF FINANCE MR NHLANHLA NENE

The ATAF Conference on Cross Border Taxation in Africa
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The ATAF Chairman, Commissioner General Gershem Pasi,
Members of the ATAF Council,
The ATAF Executive Secretary, Mr Logan Wort,
Delegations of African Ministries of Finance and Revenue Authorities,
Representatives of the Business and Civil Society sectors,
Ladies and Gentlemen,

Good morning, and for those of you who are visiting us from abroad – Welcome to South Africa!!

At the onset, the Government of South Africa condemns the attacks on foreign nationals in the strongest possible terms. We can assure you that we as Government are doing everything in our power to deal with this scourge. We have mobilised our security apparatus and are focusing our efforts on social mobilisation to isolate the criminal elements that are responsible for these acts of violence against our own brothers and sisters.

These acts of violence are worse than the terrorist attacks that we have seen in some parts of the world; because this is nothing, but violence within the family. The President had to cancel his overseas travel to address this whilst His Majesty The King of the Zulus also addressed his subjects in Kwazulu-Natal.

Over the weekend I attended the Spring Meetings of the IMF and the Wold Bank; one of the issues that were extensively discussed was the 3rd International Conference on Financing for Development. It was acknowledged by all stakeholders (developing countries, developed countries, international financial institutions) that the meeting in Addis Ababa will be one of the key steps in determining the framework for financing the Post-2015 development agenda, including the sustainable development goals. The matter that we must be seize with is how we can finance development especially on the African continent. As one of the most under-developed regions, we on the African continent must find new ways in which we no longer speak of aid but rather of sustaining our development through our own resources. And a significant part of those resources have to come through taxation.

So the discussions you will be having over the next few days on the taxation of cross-border transfers could not come at a more appropriate time.

Importance of African Economic Development

Never has Africa gained so much attention for all the right reasons! Our economies are developing at an average rate of 5% and investors are becoming more interested in Africa. The continent has enjoyed reasonably good progress and in many instances countries have been able to assert their sovereignty to develop and structure their own economies.

While challenges remain in Africa, it is pleasing to see that from an economic point-of-view, the continent remains the central destination for European export markets. With a relatively stable democratic climate and national elections having taken place in 28 countries in 2014 with little to no political violence, it is evident that Africa is “getting it right”. Despite the terror attacks and a growing insurgency in West Africa, the continent is resilient in its economic growth and prospects. So allow me to briefly dwell on some of these aspects.

Growth Figures in Sub-Saharan Africa

Sub-Saharan Africa's growth improved, for the second consecutive year, to 4.5% in 2014 and is projected to pick up to 5.1% by 2017. In Nigeria for example, the region's largest economy, activity expanded at a robust pace (6.3 %), supported by a buoyant non-oil sector. Growth was also strong in many of the region's low-income countries, including Côte d'Ivoire, Mozambique, and Tanzania. Excluding South Africa, the average growth for the rest of the region was 5.6%. This is a faster pace than other developing regions, excluding China.

Risks to Growth in Sub-Saharan Africa

However, the risks to the region's outlook stem from both external and domestic factors. Domestic factors include the Ebola epidemic, expansionary fiscal policy and currency weaknesses, and the precarious security situation in several countries. A sudden increase in volatility in international financial markets, and lower growth in export markets are among the major external risks to the region's outlook (2015 Global Economic Prospects, The World Bank). Other risks include the increasing fiscal vulnerabilities, with large deficits prompted by an acceleration of recurrent spending in a few countries (2014 Regional Economic Outlook: Sub-Saharan Africa, IMF)

Taxation and the Globalised Economy

New ways of doing business in a globalised economy urgently call for a re-think on how taxation of new forms of business should take place – notwithstanding the fact that some of the rules have not kept up with the pace of changes. I would like to highlight some key tax challenges in the new globalised economy:

a) The increasing mobility of capital and people, and the rapid adoption of technology to improve communications, has resulted in restructuring of MNE business models and operations;

b) Such restructurings offer the opportunity to contractually shift risk and valuable intellectual property from, for example, local distributors to a central entrepreneurial company (the principal) in a low tax jurisdiction. This ability to contractually shift risk and intellectual property among the members of an MNE (but not outside the MNE group as a whole) allows MNEs to plan where profits are reported, and thus where tax is paid;

c) Developing country tax administrations are seeing many such restructurings, and challenging them frequently involves the interaction of a number of international tax rules – transfer pricing rules, tax treaties, the taxation of non-residents, and rules concerning the transfer of intangible assets.

What does this mean for taxes in Sub-Saharan Africa? Tax revenues in Africa continue to increase

External financial flows and tax revenues continue to be an important contributor to Africa's development (African Economic Outlook, 2014). To fund Africa's development, mobilising domestic resources and developing a sound revenue generation capability is crucial. Strengthening domestic resources offers an antidote to aid dependence and increases the country's ownership of its development and growth agenda. However, beyond its fiscal role, the tax system has a more substantive role in Africa: it is an important tool for good governance, democracy and the basis for the social fiscal contract between governments and its citizens and corporations.

For Africa as a whole, the tax burden stood at 26.0% of GDP in 2012, compared to 24.4% in 2011. In 2011, tax accounted for 26.8% of Africa's GDP, up from 26.6% in 2010. The tax-to-GDP ratio peaked at 31.1% in 2008 as the financial crisis hit, which suggests there is still room to increase tax revenues.

In 2012 low-income African countries on average mobilised only around 16.8% of their GDP in tax revenues, below the minimum level of 20% considered by the United Nations as necessary to have achieved the Millennium Development Goals.

- Lower-middle-income African countries fared little better, with an average tax burden, i.e. the share of tax revenues to GDP, of 19.9% in 2012.
- With an average tax burden of 34.4% in 2012, upper-middle-income countries came closer to the average in OECD countries of 35% (African Economic Outlook, 2014).

Risks and challenges to the African tax base

Reliance on single source of revenue, inadequate tax-mix

Resource-related tax revenues typically distract governments from generating revenue from more politically demanding forms of taxation such as the corporate income tax (CIT) on other industries, the personal income tax (PIT), the value-added tax (VAT) and excise taxes. In addition, this makes Africa's resource revenue vulnerable to highly volatile international commodity prices and external shocks. For example, during the commodity price boom between 2002 and 2008, resource revenues increased from about USD 45 billion to USD 230 billion. But as the global economic crisis hit Africa in 2009, resource taxes fell back to USD 129 billion. So it is important to get the tax-mix right, in order for us to develop more resilient and sustainable economies.

BEPS-related issues

But there are also other significant risks and challenges to the African tax base. I allude to the problems associated with tax-base erosion and profit shifting (BEPS) through the activities of multinational corporations (MNCs), which tend to use tax reducing financial strategies to shift profits across borders to take advantage of favourable tax rates. There is no doubt that current tax regimes have failed to keep pace with an increasingly globalised economy. The result is that multinationals are able to take advantage of the outdated international tax laws to minimise their tax liability, that is, partake in Base Erosion and Profit Shifting (BEPS), as was so sharply illustrated in the United Kingdom when in 2012, a series of news articles described the tax affairs of three US-based multinational groups, Starbucks, Amazon and Google. The news reports prompted not only public protests, but also parliamentary hearings and a call for legislative action to curtail base erosion.

In Africa, Multinational Enterprise (MNE) activities constitute large and significant proportions of national income. In some African countries, tax revenue from MNEs often represents a significantly greater share of the tax base than in more developed countries and such countries rely very heavily on MNE taxation. For example, Rwanda reported that 70% of its tax base comes from MNEs and Nigeria reported that MNEs represent 88% of the county's tax base (ATAF Consultative Conference on New Rules of the Global Tax Agenda, March 2014). Burundi has stated that one MNE taxpayer contributes nearly 20% of the country's total tax collection.( ) In this context, the revenue loss from BEPS can be very substantial for some countries in Africa and addressing these BEPS issues is therefore crucial.

Developing countries' wealth is increasingly being held offshore: 1/4 of all Latin American household wealth and 1/3 of all Middle Eastern and African wealth is held offshore (Boston Consulting Group, Global Wealth, "Shaping a New Tomorrow" June 2011). The Global Financial Integrity Report (2008) estimates tax losses to Developing countries at US$ 100 billion per year (GFI, 2008 and OECD DAC 2009). They further report that for every US$ 1 that goes into developing countries as development assistance (ODA), US$ 10 flow from the country through illicit means (Global Financial Integrity, 2012).

Non-BEPS-related issues

While base erosion and profit shifting is a problem affecting almost all developed and developing countries alike, profit shifting is not the only driver of the erosion of the African tax base. Factors contributing to erosion of the continents tax-bases are exacerbated when, for instance, governments sign away their own tax revenues through:

- Ill-conceived tax incentives,
- Insufficient tax mix and overreliance on single source taxation,
- Poorly negotiated contracts and non-transparent concessions (especially in the extractive industry),
- Inadequate taxation of high net worth individuals,
- The lack of automated systems in tax administration,
- A disconnect between tax policy and tax administration – which leads to weak policies and legislation and under-resourced tax administrations.

It has been suggested that weaknesses in Africa's tax regimes give away so much of the tax base that some of these new international tax rules may not even matter.

Other drivers of tax base erosion in Africa, but not significantly related to MNEs, also include trade mis-invoicing, that is, the fraudulent over- and under-invoicing of trade transactions. Of the illicit flows of capital through developing countries (i.e. approximately US$ 542 billion per year on average over a 10-year time series), trade mis-invoicing represents close to 80% of this amount - or US$ 424 billion (Global Financial Integrity, 2014). Capital flight not only drains domestic resources much needed to fund developing countries' development agenda, but it also exacerbates inequality and facilitates crime and corruption. Using case studies of Ghana, Kenya, Mozambique, Tanzania, and Uganda, a study produced by the Global Financial Integrity (GFI) found that trade mis-invoicing is a significant source of illicit outflows and inflows of capital in each country, resulting in billions of dollars of lost investment and hundreds of millions of dollars in unrealized domestic resource mobilization.

Further drivers of base erosion not adequately addressed in the BEPS Action Plan but of significance to Africa are the issues relating to the taxation of natural resources and, most importantly, tax incentives and tax exemptions. Much still needs to be done in these areas.

Africa's response to BEPS

Having identified these contributors to the erosion of the African tax base, it is imperative that in our collective efforts we work to make an impact at the international level as well as continue to develop our own capacities to deal with the challenges. Therefore, it is imperative that all African, and other developing, countries be involved in the BEPS process to ensure that sufficient attention is given to the different levels of readiness of developing country tax administrations and the resource and capacity limitations they face.

These specific risks and challenges faced by African and other developing countries need to be addressed if the OECD / G20 BEPS project is to adequately deliver the necessary solutions to these global tax problems. It is therefore critical that African countries use all the opportunities to make their inputs into the BEPS project to ensure that the views and experiences of African countries shape the development of the potential BEPS-related solutions. I am pleased that the African Tax Administration Forum (ATAF) has been mandated to define the African position with its members and to communicate the African response to the BEPS project. And this gathering here today, is another important step for the continent in contributing to the crafting of the global solutions.

It cannot be over-emphasized that the continent must endeavour to mobilise its own resources through the development of strong and capable tax systems and reliable trade facilities, as well as by strengthening and developing the supporting infrastructure.

Taking the work forward

Africa must protect its own tax base and advance Domestic Resource Mobilisation through a common voice, a common concern and a common action plan. The discussions that will be taking place here over the next two days provide an encouraging continuation of efforts in presenting coordinated African contributions to the international tax developments. The current global focus on international taxation offers a unique opportunity for African leaders to embark on their own continental taxation renaissance. And this should include giving consideration to the establishment of a Tax Policy and Tax Administration Commission (glaringly missing within the structures of the African Union) that would deal with harmonising the continent's tax policy, legislation and administration, as well as seeking ways to improve cross-border cooperation and thereby optimising continental revenue mobilisation. It is in this way that we would move closer to firmly placing Africa on a steady path to achieving the African Union's Agenda 2063 (the approach to how the continent should strategically exploit all possible opportunities available in the short, medium and long term, so as to ensure positive socioeconomic transformation within the next 50 years) as well as the Sustainable Development Goals.

Over the next few days, this gathering has a significant opportunity to strengthen the African voice in the G20 / OECD process on Base Erosion and Profit Shifting. It is imperative that we ensure that any redefinition of the international tax rules currently being developed take into consideration the needs and conditions of the African continent. I wish to further appeal to African revenue administrations to make available their expertise and technical resources in this important global process in order to unlock the revenue mobilisation blockages in Africa, as led by the ATAF Technical Committee on Cross-Border Taxation. And lastly, I wish to urge African Ministries of Finance to fully participate in these efforts to optimise Africa's revenue collection capabilities.

I thank you.