

Panel Reforming Finance for the MDG's

Ladies and Gentlemen

Concerted global action propelled by the time-bound MDG commitments that leaders made at the turn of the millennium have led to some progress on specific targets. But the deficiencies of the MDG framework: their failure to incorporate human right principles; to pay as much attention to development processes as to development outcomes; their limited ambition; and the lack of ownership of the MDGs by those they seek to address, has resulted in progress being uneven and impacts on the structural causes of poverty being limited or non-existent.

The food and financial crises have negatively affected the ability of millions of men, and particularly women to live and work decently across the board- whether in industrialized or poor countries. However, at a macro-level, the effects of the crises and required responses have been different for so called 'emerging economies' as compared to industrialized countries. This has led to a shift in geopolitical axes of influence and loci of responsibility and the consequent global partnership of development, one of the MDGs. Global efforts to tackle the multiple global crises have revealed key gaps in this existing global partnership for development. Action needs to be taken to fill these gaps in the quest for a genuine global partnership for development that so far has proven elusive.

The Financial Crisis

Figures from the World Bank revealed that net private capital inflows to developing countries fell to half in 2008.¹ Sub-Saharan Africa was hit hardest by reduced external demand, reduced export prices, weaker remittances and tourism revenues, and greatly reduced capital inflows, particularly Foreign Direct Investment. Grappling with the effects of climate change and food scarcity, alongside existing problems such as a small amount of fiscal revenue due to capital flight and tax evasion and debt burdens, these countries have had little budgetary space for maneuver to invest in their development. There is an urgent need to review current channels by which revenue is generated that moves away from the prevalent model of financing for development that presupposes the primacy of donor assistance and recognises the need to reinforce a country's ability to raise domestic resources justly and progressively.

Tackling capital flight and tax evasion

Taxation is crucial for development, not only to finance it but also to foster economic independence and to strengthen democratic accountability and participation, both at the national and international level. However, developing countries have been limited in their ability to effectively implement progressive tax regimes. Along with the usual reasons given such as capacity and good governance limitations, there are a number of external

¹ World Bank, Global Development Finance: Charting a Global Recovery, Washington 2009

factors influencing countries' ability to effectively mobilize domestic resources. These include advice from institutions such as the International Monetary Fund (IMF) or requirements to reform tax regimes imposed by trade agreements or conditionality related to debt relief or development assistance; tax competition; trade mispricing strategies of trans-national companies; and the continued existence of tax havens. Africa, for instance, lost between \$854 billion and \$1.8 trillion in cumulative capital flight over the period 1970-2008. This figure would have been enough to repay the region's total outstanding external debt and leave over \$600 billion for poverty alleviation and economic growth.² Cross-country cooperation, transparency of revenues and properly regulated financial institutions are central to enable governments to effectively mobilise resources from taxation. This requires joint effort and international pressure on those that perpetrate the problem.

Financial Transaction Taxes to tackle global systemic weaknesses and generate resources for development

Financial markets have grown spectacularly in the last two decades. In 2008, for example, the trading of financial transactions was approximately 74 times higher than nominal gross domestic product. In 1990, it was only 15 times higher.³ These markets, in which money is the commodity to be traded, not goods and services, has divorced real growth, production and job creation from the majority of financial transactions which are purely speculative and have damaging effects on the real economy and consequently on development. Countries in East Asia in the 1990s and countries in the Euro monetary-zone in spring 2010 have directly experienced the destabilizing impact of speculation on their currencies.

Financial Transactions Taxes are taxes that can potentially contribute to the stabilization of financial markets while generating large amounts of revenue. FTTs would increase the cost of speculative trading and thus help mitigate fluctuations of asset prices in stock markets, of exchange rates and commodity prices. At the same time they would have a minimal effect on the real economy as the taxes would be limited to transactions between financial market actors while transactions between customers and financial institutions, for example, the purchase of goods, labour market transfers and so on, would be exempt. FTTs at rates between 0.01% and 0.1% would generate tax revenues ranging between 0.5% and 2.4% of world GDP if all transactions are covered, a scale of resources that responds to the scale of financing needs for the MDGs and other development imperatives in the face of climate change and other crises today.

Taxes on financial transactions (FTTs) have been debated widely in the wake of the global financial and economic crisis:

- The UN General Assembly's Commission of Experts on Reforms of the International Financial and Monetary System (the "Stiglitz Commission") mentioned a financial services tax as a way of providing more stable and sustainable development finance that would also help to stabilize markets.

² Global Financial Integrity. Illicit Financial Flows from Africa: Hidden Resources for Development. Dev Kar and Devon Cartwright-Smith. March 2010.

³ Schulmeister, WIFO, 2009.

- A number of European countries including Belgium, France and Austria made clear political decisions to support currency or financial transaction taxes. Recently Germany joined them.
- end of March 2010 the European Parliament passed a Resolution to the European Union to establish a number of financing mechanisms for development and also called for an FTT.
- The General Assembly of the United Nations, in a resolution of December 2009, recognized the potential of various voluntary innovative sources of financing to supplement traditional sources of financing, stressed that those funds should be disbursed in accordance with the priorities of developing countries and should not burden them unduly, and encouraged the Secretary-General to organize an informal event in 2010 on the potential of voluntary innovative sources of development finance. This event took place on the 3rd of June here in the UN and FTT was discussed as well.
- The Leading Group on Innovative Financing for Development - an intergovernmental forum with representation from all continents – recently established a Taskforce on International Financial Transactions for Development. An expert group is currently examining the feasibility of financial transaction taxes, including currency transaction taxes and will present proposals for political decisions in the coming days.

Objectives of an international tax on financial transactions

International taxation has the potential to contribute to global justice and development objectives by fulfilling key functions of taxation: revenue raising and regulation as well as redistribution of wealth to contribute to global justice not only within states but also at the international level.

Taxing currency transactions or more broadly financial transactions is one way in which the fast-expanding financial sector could contribute towards sharing the burdens on governments and the poorest people of the multiple global crises. Revenues generated by such taxes should be used to support global efforts to achieve internationally agreed development goals. At the same time, this type of taxation would play a role in the stabilisation of the global economy.

Although action at the national level is possible, highly interlinked global financial markets on the one hand and the high concentration of activities on the other, suggest regional and international cooperation. Joint action through regional and international taxes could contribute to the strengthening of representative democratic global institutions and a sense of global responsibility.

Arguments to promote a tax on financial transactions:

- Contribution to global justice: A tax on financial transactions is a measure of political fairness and social justice as it will ensure contributions by the financial sector, which was at the core of the crisis, towards crisis resolution and global recovery. It would also shift the burden of taxation from wages and consumption to capital thus making the overall tax system more equitable. Using the ensuing revenues for financing development and global public goods would contribute to more just international distribution of wealth and to the reduction of inequalities between North and South.

- Revenue generation: Possible revenues depend on the rate and scale of introduction. All estimates suggest that substantial revenues can be achieved with a rather low tax rate.

Even when assuming a reduction of transaction volumes due to taxation in North America and Europe, estimated tax revenues would range between 0.5% and 2.4% of world GDP if all transactions are covered. At the European level even a tax at a minimal rate of 0.01% would generate income of about EUR100 billion per year.

- Regulation: According to the Austrian Institute for Economic Research (WIFO), a general and uniform FTT on all kinds of financial asset transactions would have a stabilising effect on financial markets, even if introduced at a low rate. The FTT would increase the cost of speculative trading and thus help mitigate fluctuations of asset prices in stock markets, of exchange rates and commodity prices. At the same time it will have minimal effect on the real economy (especially compared to other measures such as an increased VAT) and thereby improve the general macroeconomic performance

- Feasibility: A general FTT is technically feasible because of the use of standardized electronic settlement systems. Circumvention of electronic platforms would be very costly and hence unlikely. The FTT could be introduced step by step both in terms of geographic expansion and coverage of types of financial transactions. Regional introduction is possible. Due to high concentration of trading, in the short run it would be sufficient to get a few major players on board, such as the UK and Germany in Europe (which account for over 90% of European financial trading). Emigration of trading is not expected because other factors such as network externalities of market places are most important. The British stamp duty on stock transactions of 0.5% did not harm the City of London as major financial centre. In the medium run, the FTT could be introduced within the European Union (as well as Switzerland and Norway, as major non-EU financial centres in Europe), while in the long run global implementation should be considered

- Use of revenue: The global dimension of the economic crisis demands international burden sharing. Poor countries are especially badly hit by the crisis, which they were least responsible for, and have the fewest resources to counteract or take meaningful steps for its resolution. Therefore collected funds should to be used to finance global development, especially achieving the Millennium Development Goals and delivering global public goods. Such an approach would ensure equitable global redistribution both of resources to offset the immediate effects of the crisis and of accumulated wealth in the long run.

- Governance of funds and representation: The ensuing tax receipts need to be administered in a responsible and accountable manner whereby representative democratic governance of funds is imperative. Decisions with respect to the administration and allocation of revenues should be placed in a multilateral setting and taken based on equal rights of all actors and inclusion of a wide range of stakeholders to ensure joint ownership, transparency and accountability. CIDSE believes that the UN, being universally representative, is the only institutional framework which would have the required legitimacy to administer funds dedicated to global purposes. Additionally, with its extensive expertise in the area of international development, the UN would be best placed to make informed decisions about effective fund allocation and the respective channels to be used for this purpose.

Let me conclude, Ladies and Gentlemen, with a few major achievements we expect from the September MDG summit:

- Taxation as a crucial means for development should become an important issue in the Outcome document of the summit. Taxation not only as an instrument for additional finances, but also as an instrument to foster economic independence and to strengthen democratic accountability and participation at national and international level.
- Leaders should reach a global agreement on innovative sources for development and decide to implement Financial Transaction Taxes that not only increase financial resources but also have a potential to tackle global systemic weaknesses.
- The revenues from FTTs should be used for funding development needs, including the MDGs and responding to climate change. These funds must be additional to ODA commitments.
- The UN should play an instrumental role in determining the destination of FTTs' revenues.
- Administration and revenue allocation decisions should take place in a multilateral setting on the basis of equal rights of all actors and the inclusion of a wide range of stakeholders.

Thank you!

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