# ICAI follow-up of:
# UK aid's contribution to tackling tax avoidance and evasion

a summary of ICAI's full follow-up review

**June 2017**

**The Independent Commission for Aid Impact** works to improve the quality of UK development assistance through robust, independent scrutiny. We provide assurance to the UK taxpayer by conducting independent reviews of the effectiveness and value for money of UK aid.

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# Executive summary

Each year, ICAI follows up on the response to the recommendations it made in reviews published the previous year. The process is a key link in the accountability chain, providing Parliament and the public with an account of how well DFID and other government departments have responded to ICAI reviews. It also provides feedback to the responsible staff, and serves as a useful learning exercise for ICAI in our quest to achieve greater uptake of our findings and recommendations.

This document is a summary which focused only on the results of our follow up of UK aid's contribution to tackling tax avoidance and evasion. The full Follow Up report of all our year five reviews, including overall conclusions from the process and details of our methodology, can be found on our website.

# Findings

## UK aid's contribution to tackling tax avoidance and evasion

One of the themes for ICAI's work programme is 'beyond aid' which, among other things, explores the UK's efforts to influence how the international system interacts with developing countries. In September 2016 we published a review of how DFID had influenced the international tax system as part of its efforts to help developing countries tackle international tax avoidance and evasion. The review also explored how DFID has worked with HM Revenue & Customs (HMRC) to strengthen revenue authorities in developing countries – given the commitment in the UK aid strategy to making more use of the expertise available across government in the aid programme.[1] It was a learning review, in view of the fact that this was a relatively new area of engagement for both departments, where the evidence on what worked was limited. We awarded DFID an overall **amber-red** score for its work. We found that while DFID had enjoyed some early success in helping developing countries participate in international tax processes, its efforts were not sufficiently grounded in the needs and priorities of developing countries, or informed by research or learning from its country engagements. We made four recommendations, in the areas indicated in Table 1.

Table 1: Area of recommendations and DFID's response

| Subject of recommendation | DFID's response |
|---|---|
| More attention to prioritising and sequencing international tax initiatives | Accept |
| Strengthening cross-government approaches to capacity building | Accept |
| A more strategic approach to influencing | Accept |
| Policy coherence for development - assessing the impact of UK tax policies on developing countries | Reject |

DFID has generally reacted very positively to the report: three of the recommendations were accepted and there has been significant progress in some areas. HMRC also informs us that it found the analysis useful.

> "Ending global poverty can only be achieved through ensuring the international system works for developing countries."
>
> ***DFID submission to the International Development Committee***[2]

### Prioritising and sequencing international tax initiatives

The review found that DFID's influencing work on international tax and its capacity building support on international tax initiatives were not based on sufficient analysis of developing country needs and interests. As a result, there was a risk of developing countries being encouraged to implement technically challenging initiatives without enough attention to the costs and benefits, and without sequencing them with the development of their national tax systems.

1. *UK aid: tackling global challenges in the national interest*, HM Treasury and DFID, November 2015, p. 10 link.
2. Quoted in *The Future of UK Development Co-operation: Phase 2: Beyond Aid*, International Development Committee, Tenth Report of Session 2014-15, January 2015, p. 6, link.

DFID acknowledged these concerns and has begun working with international partners on two initiatives that will help to address them. First, it is working with the OECD to develop a new cross-border tax diagnostic tool, which will help partner countries identify what they stand to gain from implementing particular tax initiatives, given their economic conditions, national tax systems and institutional capacity. Second, DFID is working with the International Monetary Fund to develop medium-term revenue strategies, which partner countries can use to sequence their international and domestic tax reforms. Both initiatives are still in the development phase and it is too soon to assess how well they will work in practice. In principle, however, they represent a strong response to the recommendation.

We also found that DFID's international tax work was not properly informed by experience from its country-level tax programmes. There is now a community of practice linking DFID and HMRC tax and development practitioners in headquarters and partner countries. Among other learning functions, it serves as a forum for bringing the country office perspective into the new international tax arena.

### Cross-government working

UK departments that are new to development cooperation face a steep learning curve on how to use their technical knowledge for effective capacity building. We found that DFID's support for HMRC's Capacity Building Unit was a good model for combining technical expertise from another department with DFID's knowledge of good development practice. However, we recommended that DFID be more active in ensuring that other departments engaged in capacity building draw on its experience and in-country knowledge.

At the time of our review, DFID, HMRC and the Treasury were working on a new strategic framework for tax capacity building, which was launched at an international event in October 2016. The document offers a comprehensive guide to programming on tax and development, with useful advice on various issues raised in our report, such as the need for political economy analysis, sequencing of reforms, matching reform initiatives to existing capacity levels and working collaboratively with DFID country offices. We find the document to be a useful summation of good practice.

DFID continues to offer technical support to the HMRC Capacity Building Unit, particularly in the area of results measurement. It is also designing a new resource centre for tax and development, which will include a panel of experts that both DFID and HMRC practitioners can draw on to support their work.

We are also interested to note that DFID is developing a new 'GREAT for Partnership' programme, which will help to promote, broker and support partnerships between UK government agencies and their counterparts in developing countries. It will focus initially on three sectors: extractive industries, health and anti-corruption and financial accountability. There are plans eventually to scale up the programme further, so that it can act as a central hub for government partnerships in developing countries. This suggests that DFID is beginning to marshal the resources it will need to support new entrants in the capacity building arena.

### A strategic approach to influencing

Our review found that DFID had been more opportunistic than strategic in its approach to international influencing on tax. We concluded that, if DFID considered 'beyond aid' initiatives to be an important part of its development agenda, it should approach the work more systematically, with clear strategies and objectives, adequate staffing and systems for monitoring and reporting on its results. While DFID accepted the recommendation, the management actions it proposed were noncommittal and its response since then has been disappointing. DFID informs us that it will continue to play a leading international role on tax and domestic resource mobilisation but does not see the need for a more formal planning to its influencing work.

## Policy coherence for development

'Policy coherence for development' is the principle that donor countries should strive for greater coherence between their development policy and other policy domains, such as trade, so as to create more opportunities for developing countries.[3] The International Development Committee has encouraged DFID to do more in this area.[4] We recommended that DFID take a more active stance on policy coherence in the tax arena, including by assessing the impact of UK tax policies and practices on developing countries and deciding whether to raise any points of tension with the Treasury.

The government decided to reject this recommendation. DFID informed us that, while there is good cross-government collaboration on tax and development, it does not have a role on domestic tax policy. In addition, it argued that 'spillover analysis' is a resource intensive exercise and that its efforts are better spent building capacity to tackle multinational tax at the country level. We are not entirely convinced by this argument. The UK government is not in a position to judge the impact of its tax policies on developing countries unless it does the analysis. We note that policy coherence for development is one of the commitments made under the Addis Tax Initiative, of which DFID was a sponsor.

> "All participants will ensure that relevant domestic tax policies reflect the joint objective of supporting improvements in domestic resource mobilisation in partner countries and applying principles of transparency, efficiency, effectiveness and fairness."
>
> ***The Addis Tax Initiative - Declaration,*** **Commitment 3, July 2015, link**

## Conclusion

This was a strong response from both DFID and HMRC in a number of respects. In particular, the steps towards better prioritisation and sequencing of international tax initiatives and strengthening inter-departmental cooperation on capacity building were well conceived and have the potential to improve practice. We were encouraged to hear from stakeholders that HMRC's capacity building work is steadily improving. The experience shows that cross-government partnerships can add real value to the aid programme, but need time and effort to become effective.

It is not clear to us, however, why DFID is resistant to the idea of approaching international influencing in a more structured way. 'Beyond aid' initiatives can be as important a contribution to international development as aid programmes, and should be treated with the same seriousness. We also believe that, as the UK increases its international engagement in preparation for leaving the European Union, DFID may need to take a more active stance on policy coherence for development.

3. *Busan Partnership for Effective Development Cooperation,* December 2011, p. 2, link.
4. *The Future of UK Development Co-operation: Phase 2: Beyond Aid,* International Development Committee, Tenth Report of Session 2014-15, January 2015, link.

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