

BOUSTEAD ANNUAL GLOBALISATION LECTURE 2013

Trade, Tax and Transparency: the G8s Priorities in an Asian Context.

Introduction

Distinguished Guests, Ladies and Gentlemen. It is a great honour to have been asked to give the Boustead Annual Globalisation Lecture for 2013.

Let me begin my paying tribute to our Nottingham University hosts for their far-sighted and innovative contribution to transnational education both here in Malaysia and also in China, where I have spent much of my career. I am delighted that other British Universities such as Newcastle, Southampton, Heriot-Watt and Reading are now following suit by setting up campuses in Iskandar and Putrajaya. But it was Nottingham, in partnership with Boustead, who deserve the credit for so successfully blazing a trail here over a decade ago.

It was therefore particularly fitting that last April Prime Minister Dato Seri Najib Razak – himself a Nottingham graduate – and Prime Minister David Cameron stood side by side at an event in Nottingham's Semenyih campus in a joint session to promote the Global Movement of Moderates. As it happens tackling extremism and terrorist violence will be one of the key security themes for the UK's Presidency of the G8 this year.

Theme of the speech

I want to focus today on the Prime Minister's G8 economic priorities – the three Ts: Tax, Transparency and Trade.

David Cameron said at this year's World Economic Forum in Davos:

"We need more transparency on how governments and companies operate.

We need fairer tax systems. When businesses aren't seen to pay their taxes that is corrosive to public trust.

We need more trade. When trade isn't free we all suffer."

What these three Ts have in common is that they are essentially about the rules which shape the global economy and the fairness and openness that should characterise it.

Of course fairness isn't only important in an economic context. In sport for example we hate it when we discover that people have been taking performance enhancing drugs or that match-fixing has been going on.

It is said incidentally that the definition of a good football referee is that he needs to 1. Be Fair, 2. Be Consistent. 3. Make correct judgements, 4. Be able to stay in control and finally 5. Award at least two penalties to your team and at least two red cards to the opponents.

My career and the 3Ts

I'll be coming back to a football theme in a moment, but first let me inject a more personal note about how I have come across the three Ts in my previous jobs and postings, as well as my current role as British High Commissioner to Malaysia. My experience illustrates how the economic agenda now lies at the heart of British diplomacy.

In the mid-90s as Consul-General to Shanghai, my main task was to develop commercial links between Britain and China. Back then it was already clear that China was well on its way to becoming the economic powerhouse of the Asian region. Shanghai itself was a city in transition - rumoured to have more construction cranes than in the rest of Asia put together. Fifteen years later I was privileged to be back in Shanghai in my capacity as UK Director for Shanghai Expo where it was amazing to see the transformation which had taken place from the world's biggest building site to an ultra-modern financial hub, with the huge skyscrapers of Pudong, a new airport and over a dozen metro lines.

Between 1998 and the end of 2002 I was head of the Foreign Office Department responsible for UK Trade policy. I was at the WTO Ministerial meeting in Seattle, where anti-globalisation demonstrators were tear-gassed, but no new Trade Round was launched. I was also at Doha where a Development Round was successfully launched and very significantly China was admitted to WTO membership.

Between 2004 and 2008 I was British Ambassador to Switzerland and Liechtenstein where overlapping issues relating Banking Secrecy, Taxation and Transparency were important aspects of my work. Following discussions begun during that period I am pleased to report that important tax agreements have now been reached with both countries.

Here in Malaysia the Prosperity agenda is a key focus of my work as High Commissioner and of the High Commission itself. A new prosperity unit has been formed alongside our existing trade and investment team benefitting from a strategic decision by the Foreign and Commonwealth Office to shift human resource out of certain European posts and into emerging powers such as Malaysia. We devote much of our effort to helping British companies who want to export to Malaysia and Malaysian companies who are interested in investing in the UK - an example being the recent high profile investment in the Battersea Station site by a Malaysian consortium.

Last April our two Prime Ministers gave us the daunting challenge of doubling trade by 2016: the Head of MITI and I are co-chairing a working group to devise ways of achieving that target including addressing any barriers to trade as well as trade promotion activities. As I will explain later, we are also following very closely the negotiations underway for an EU/Malaysia Free Trade Agreement.

Before elaborating on the three Ts in an Asian context, I'd like to talk more generally about the rules underlying globalisation, the so called **RuBIES (Rules Based International Economic System)**.

First, allow me to tell you about a meeting which took place in an English pub exactly 150 years ago this year. On 26 October 1863 in The Freemasons Tavern in Lincolns Inn Field in London the rules of Association Football were agreed. Although there have been several amendments of those rules over the decades since including FIFA's decision last night to allow goal line technology at the 2014 World Cup, it was the initial settling of the rules that day in 1863 which undoubtedly created the foundation for the beautiful game of football.

A lot of people don't realise that for the previous 20 years football was played according to many different variants in different British public schools.

- In Charterhouse School, which was housed in a cramped old Carthusian monastery the art of "dribbling" the ball was developed:
- On the vast playing fields of Eton the ball could be kicked high and long, and it was:
- At Rugby the boys caught and ran with the ball and began to develop what would become a separate game, but was then called, as they all were, football.

The problem arose when the boys from different schools went to University and found that they were playing by different rules. It became common practice to play half a match by one side's rules, the second half by the other's. That's how the idea of half-time evolved.

When that meeting in the pub took place the central discussion was whether a player should be entitled to pick up and run with the ball. That idea was eventually defeated by 13 votes to 4. Association football, or soccer, was formed and Rugby football went off on its own – more popular with many public school headmasters as it more obviously encouraged the courageous and aggressive traits. A few decades later when the industrial teams moved in it was only half-jokingly said that "Football is a game for gentlemen played by ruffians, Rugby is a game for ruffians played by gentlemen".

I can sense you asking yourselves why the High Commissioner is spending so long talking about football. The answer is that in many ways I think the current global economic system resembles football 150 years ago. Different parts of global economic rulemaking are at different stages of development and there is insufficient consensus about the fundamentals. We need the equivalent of the Freemasons Tavern meeting to agree the rules of the game.

Of course it is a little more complex to agree rules for the international economic system than for a game. Some aspects of the rules are in fact already well-developed – for example the WTO rules on trade, which include a binding

dispute settlement system with sanctions. But in other areas such as competition there is so far very little in the way of international governance.

The current set of standards and norms were drawn up by a specific set of actors – mostly advanced economies – and reflect the specific circumstances and economic integration challenges at the time of their development. However, as new and significant economic actors emerge, and as the structure of the global economy evolves, the international processes and fora that continue to develop these standards should become increasingly flexible and involve all major or relevant actors at an earlier stage, especially where there are close or mutual interests. There is therefore a strong case for developing and extending existing standards and rules to embrace key participants more readily and at an earlier stage of their economic development, as is already happening in some areas. It is important in developing existing and future standards, to involve all of the key actors to ensure that these standards become truly global.

As in sport, so in the economy - it is in the long-term interest of everyone to have an inclusive set of rules which all abide by.

So to the specifics:

An area where it is clear that the rules need to keep pace with global economic realities is my first T - **Tax**.

Nobody usually has a good word to say for tax collectors, but today I want to talk more about tax accountants. I have heard it said that the definition of a good tax accountant is whether he has had a loophole named after him!

An OECD report published last week makes fascinating reading. It argues that international rules about what it calls “base erosion and profit shifting” (which I would term aggressive tax avoidance) haven’t kept pace with changes in the world economy, including for example the importance of the internet for online purchases. Domestic rules for international taxation and internationally agreed standards were formed when there was much less economic integration across borders.

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Many of the strategies employed by companies cleverly take advantage of the complex interface between the tax rules of different countries. There are a plethora of treaties about double-taxation, but some multinationals with the help of those who understand the ins and outs of the rules find ways to exploit differences in tax rules to create a situation of double non-taxation.

Failing to respond to these schemes creates a non-level playing field. Some businesses, which operate across borders and have access to the right expert advice have a clear competitive advantage compared with enterprises that operate mainly at the domestic level. Moreover, if other taxpayers (including ordinary individuals) think that multinational corporations can legally avoid paying tax it undermines the voluntary compliance upon which tax administration depends.

G20 Finance Ministers last weekend welcomed the OECD report and expressed a determination to take necessary coordinated actions on the basis of the action plan to be presented by OECD in July. The UK, Germany, France and the US are all very involved in the preparation of that action plan.

Ensuring that tax is levied and paid by companies in the place where profit is generated is of importance to all countries, not just those in the G8, OECD or G20. To ensure that tax systems are competitive firms need to be paying their fair share. So I hope that Malaysia and other ASEAN countries will play a full part in the debate about how to close the tax loopholes which companies have been able to exploit so cleverly.

But aggressive tax avoidance by companies is only one of a number of tax challenges facing us. The UK collects approximately £550 bn per year in tax. The principal yields are from Income Tax, VAT, Corporation Tax, and the excise duties on hydrocarbon oils, tobacco and alcohol. Like other modern economies we also need to address the 'tax gap', ie the amount of tax we should be collecting but aren't through fraud, evasion and aggressive avoidance. Although the exact size of this tax gap is very difficult to assess it is clearly in the £ tens, if not hundreds, of billions.

Of this lost tax as much as £10 bn per year may be through criminal attacks on our fiscal system by serious organised crime groups. Organised crime groups in the UK are particularly active in cigarette smuggling and large VAT frauds known generically as 'Missing Trader Inter Community' fraud (MTIC). Cigarette smuggling alone is estimated to cost the UK over £1billion.

A growing threat of cigarette smuggling from South East Asia underpinned the UK decision to post an official from HM Revenue & Customs to the British High Commission in Kuala Lumpur in 2010. This posting has been a success. In this financial year alone (since Apr 2012), our Fiscal Crime Liaison Officer has been responsible for the seizure of over 200 million cigarettes destined for the illicit UK market. This represents a tax loss of approximately £30 million had these cigarettes had been successfully smuggled into the UK.

Key to this success is transparency and the excellent working relationship the FCLO enjoys with Royal Malaysian Customs and other Malaysian law enforcement, prosecution and fiscal authorities. HM Revenue & Customs seeks to share its knowledge with international partners. For example should Malaysia introduce a Goods and Services Tax in the future (as is heavily rumoured) HMRC will be keen to share the experience of combating VAT frauds.

We also need to build on the relationships with our international partners. In an age where illicit funds (either the proceeds of crime, untaxed income or both) move freely across international borders, we need a strong effective international response to identify these illicit money flows and to stop them through effective supervision and enforcement of money-laundering rules, and by helping developing countries to build robust anti-money-laundering and counter-terrorist-financing regimes.

This brings me neatly to another priority for the UK's G8 Presidency and our second T: **Transparency**. This is, of course, closely linked with the Tax issue. Tax fraud, evasion and aggressive avoidance (whether by companies or individuals) all thrive in situations where there is secrecy and a lack of transparency. One of the trends noted in the OECD report I referred to earlier was that some countries are now requiring tax avoidance schemes and/or any uncertainties relating to tax liability to be disclosed to the tax administration. Such rules make it much riskier for companies to pursue aggressive tax strategies, not least from the point of view of their reputation with the public. The very act of forcing companies to be more transparent about their tax arrangements is a strong encouragement to them to behave more ethically.

But the importance of Transparency goes much wider than Taxation issues. Many of the world's poorest countries have some of the greatest supplies of natural resources, but are plagued by a lack of transparency, poor rules and corrupt practices that prevent oil, gas, mining and other resources, such as land, benefitting local communities and economies. An important part of the G8 transparency agenda is to look hard at ways in which we can encourage stronger global standards, greater transparency and better information about land and extractive resources to enable citizens to hold governments and companies to account for their decisions and activities. To ensure natural resource revenues are not diverted or mismanaged we are working to promote tax transparency and combat illicit flows, to ensure growth and private sector investment are not stymied by bribery and corruption. Finally, we are exploring how to promote greater openness in government, by encouraging the availability of more accessible and comparable data for citizens and the private sector, including by harnessing new technologies.

Transparency is the biggest antidote to corruption more generally. Corruption is estimated to cost the equivalent of around 5% of global GDP (\$2.6 trillion).

The countries in this region vary considerably in the extent to which corruption is a problem. Transparency International's Corruption Perception Index, which is only one - rather subjective - measure ranks Singapore 5th, Brunei 44th, Malaysia 60th, Thailand 80th, Indonesia 100th, Vietnam 112th, Philippines 129th, Laos 154th, Cambodia 164th and Burma 180th.

A particular issue in many of the countries of South East Asia is that of transparency in government procurement.

Which brings us neatly to my final T – Trade.

Increased and freer trade plays a major part in driving global growth.

A multilateral trade deal (completion of the Doha Round) would be the best way of freeing up trade. It is estimated that the current impasse in the negotiations costs the world economy \$180bn a year. Nonetheless there are some encouraging signs from Geneva.

Preparations for Bali's WTO Ministerial in December are moving ahead with some progress towards a trade facilitation deal which could add \$70bn to the global economy by reducing the bureaucracy at borders – every day that goods are delayed in transit reduces exports by 7%.

Separate talks aimed at launching a plurilateral deal in trade in services are progressing well, with negotiations expected to start in late spring with the promise of some early and valuable liberalisation in this area.

But given that a comprehensive WTO Round will be a long haul, bilateral agreements are the next best option.

SE Asia is a key hub and transit point for world trade. Indeed about 40% of world trade passes through the Straits of Malacca. The region's economy is expected to grow by more than 5% this year and ASEAN countries now represent significant markets for third countries. So it is unsurprising that a growing number of regional trade agreements are being negotiated.

Of particular interest in this region is the decision by ASEAN leaders to form the ASEAN Economic Community by 2015 – the same year Malaysia will be chairing ASEAN – this represents an immense opportunity for cooperation and trade, with ASEAN predicted to become the 4th largest market in the world by 2030 after the US, EU and China

Trade is an EU competence, with the negotiations conducted on the EU side by the European Commission. I am delighted that the Commission concluded negotiations with Singapore just before Christmas. The resulting FTA will deliver improvements on public procurement and retail banking. Next in line are possible agreements with Malaysia, followed by Vietnam, Thailand and the Philippines.

The ultimate goal is, of course, an EU/ASEAN deal. But we need to bear in mind the diversity of ASEAN. Singapore's GDP per head is 60 x that of Burma (EU differential 16). Indonesia's population is 600 x that of Brunei. There has also traditionally been a diversity of approach between ASEAN countries to free trade – Brunei, Malaysia, Thailand and Singapore have been more active/advanced in signing bilateral FTAs – others have fewer than 2 FTAs signed, with Cambodia and Myanmar without any.

Our big focus here is of course Malaysia where the EU expects the Malaysian side to be given a fresh mandate for the FTA negotiations after the forthcoming general elections. Only then will it be possible to engage substantively in sensitive areas such as procurement, export duties, IPRs, automotives and alcoholic beverages.

I would like to particularly highlight the importance of services liberalisation. We believe Malaysia would benefit four times as much from liberalising both goods and services as opposed to just goods. The efficiency gains from freeing up heavily protected sectors such as architecture, engineering, law and retail would be very significant.

So I would urge the incoming Malaysian government after the election to give priority to concluding a wide-ranging and ambitious Agreement.

Conclusion

In conclusion then Prime Minister David Cameron has said “If you want open economies, low taxes and free enterprise then you need to lay down the rules of the game – and be prepared to enforce them.... This is a vision of proper companies, proper taxes, proper rules, a vision of open societies, open economies and open government.”

For business to thrive it needs the assurance of a level playing field. Or to go back to the football example, to be sure that some competitors won't be allowed to pick up and run with the ball when others are only being allowed to use their feet.

Football is rightly called the beautiful game. Everyone can understand it and most people have tried playing it. It teaches sportsmanship. But in order for players and spectators to enjoy it the rules needed to be agreed and to be applied.

Globalisation can also be beautiful. International trade allows more choice for consumers, a more rational allocation of resources, provided rules can be established and applied which are fair, sensible and binding on all. That needs dialogue, a listening to each other and eventually communal decisions of the kind which were taken for football back in 1863.

My hope is that the economic themes – Trade, Tax and Transparency - identified for this year's UK G8 Presidency will generate a debate which goes wider than the G8 members, in particular embracing the vibrant emerging powers of South East Asia. And that such a debate will lead to decisions which are in the interests of the global economy as a whole.

Thank you for your attention. If you'd like to tweet any comments please do so using my twitter account @HCSFeatherstone and #HCTTT.