

# VIII. Conclusions, Policy Goals & Recommendations

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## 1 Conclusion

In this chapter we explain the specific insights that emerged during the three year course of the study. The study on Tax Justice and Poverty experienced various challenges during the time line of its execution on account of the fact that comparability of data in real and nominal terms was often challenging. Further, given the dynamic nature of corporate taxation and tax justice and poverty the level of detail that was required was quite immense. The Research teams also had diverse opinions on some aspects of the research which entailed that unanimity had to be sought to pave the way to subsequent stages of the Study.

### 1.1 The context

First of all we note that a specific set of problems emerged in Germany, Kenya and Zambia roughly around the same time, due to the same causes which we have outlined to some extent in our Introductory chapter IV/5+6: Growing financial and ITC globalization, privatization and deregulation resulted at the lower end of society into an increase in atypical employment, leading in Germany to the emergence of a regular low-wage sector, in Kenya

and Zambia to an increase of the informal economy – with a growing number of people who no longer were able to pay taxes and SSCs. Subsequently, during the same period, private, corporate and criminal wealth holder profited over proportionately from the situation and increased their income and wealth.

All this needs to be seen on the background of a two speed development: Financial and economic business structures as well as Offshore Services for private, corporate and criminal wealth holders expanded fast and can easily be exploited, while states and their authorities remain caught in their respective “cages” defined by national legislation and dragging international treaty development. Even the OECD, in all due diplomatically cautioned language, cannot but state the obvious: that ‘the international common principles drawn from national experiences to share tax jurisdiction may not have kept pace with the changing business environment’ and practice (OECD, 2013a, p. 5+7).

On that background, some of our findings describing the Status Quo in our three countries are the following (see III/1)

1. Income and Wealth Inequality in our countries has reached unprecedented levels. The concentration of income and wealth at the top end of our societies is especially worrisome since it is going along with an increasing for formal and informal power those top wealth holder exercise over governments and legislators
2. We note that there is dispute whether or not the increase of inequality goes along with an increase in poverty – depending on the experts or statistics one consults. Our view is that the situation of the poor in our countries is quantitatively and qualitatively worsening, especially if observing what can be purchased from the money available.
3. Linked to the question of poverty we note the strain on Social Security and Social Welfare Systems: In Germany, due to the growing disbalance between SSCs paid and support needed, in Kenya and Zambia due to the inability of fledgling institutions to cope with the needs arising in an increasingly mobile society while due to rural-urban migration traditional networks of social security crumble.
4. Government spending capabilities in our three states are limited due to the obligation to pay interest or repay debt owed to institutions of the external market. The final Beneficial Ownership behind those institutions are, however, private and corporate wealth holder – that way contributing to that which is said in Nr. 1. Even Germany, which seems to be in a comfortable situation, should worry about its extent of public debt, especially, since outer circumstances may turn to the worse. In our view, today’s debts are an unfair burden upon the shoulder of tomorrow’s children.
5. All in all, we agree with the emerging consensus,<sup>1</sup> there is more money leaving developing countries via IFFs than entering them in ODA and FDI, while developed countries are at the receiving end, profiting from an inflow of illicit funds – but at best indirectly, since that which is entering Germany outside formal channels cannot be taxed either.

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<sup>1</sup> (OECD, 2013c) (High Level Panel, 2015a) (Kar & Spanjers, 2015) (Griffiths, 2014) etc.

A specific challenge for this research was right from the beginning the question of land ownership. Bavaria, Kenya and Zambia have a strong agricultural segment, in all three countries one can state a concentration of land ownership among the top wealth holder and it is obvious that the possession of land as asset within wealth portfolios will gain in importance. At the same time it offers itself for a “Wealth Tax” since it is one of the very few assets which cannot be locked away in Offshore Constructs. However, one can illustrate also taxation difficulties ranging from options aiding and abetting tax evasion and money laundering as well as regarding the valuation and collecting of rentals. Finally, land possession can be used to exploit the situation of others by expelling them or collecting overprized rents.

## **1.2 Tax relevant issues**

The context depicted also impacts upon the tax policy of our three countries, as we have described in parts IV, V and VI of this paper. For example: A major driving force is the different mobility between capital on the one side, and human labour on the other. This results in reduced taxation of private and corporate wealth holders both regarding their income from labour and their income from other sources, most importantly capital. In a process of tax competition with each other, states attempt to attract them or keep them and their assets in certain jurisdictions rather than others. At the same time, to offset losses occurring by those reductions, the tax burden upon those who are not of comparable mobility, is increasing, also because reductions in direct taxes are compensated through an increase in indirect taxation. Thus the principle of taxation in accordance to the ability to pay is replaced by the principle of taxation in accordance to Inescapability/the inability to avoid.

Of course, both laws and administrative practice should be reformed, but as a matter of priority we note some deficiencies in tax law enforcement. For example, today’s circumstances enable top income and wealth holder to conceal taxable assets from authorities by using numerous layers of secrecy via Offshore jurisdictions and (more often than not) declare only that which cannot be hidden. Qualified and experienced tax inspectors could nevertheless “follow the money” and uncover aggressive tax avoidance and tax evasion. But since governments have to reduce costs of collection, they are unable to employ more tax officers; but it is them whose task is to secure the states revenue and, in all three countries, they collect much more money than they cost. Worse: Some states keep their inspectors number low intentionally, because this, too, is part of their tax competition policy to attract and keep private and corporate wealth holder within their jurisdiction. It is telling that at least for Germany there is evidence that in the foreseeable future the number of tax consultants and tax lawyers in the private sector will outnumber tax inspectors.

Facing a world of increasing mobility of finance, commerce and global elites, a major concern arising from this research is the question of who is writing taxation rules according to which national tax authorities are able to cooperate. Here we note that it is the OECD driving forth its own process, not paying any attention to the concerns and interests of the G77, as was made obvious at the “Financing For Development” Conference in July 2015 at Addis Ababa. As long as this is the case we doubt that developing countries will get their fair share of the

global taxable pie but rather will remain with the crumbs developing countries are willing to leave them.

### **1.3 Ethical implications**

As evidenced in Chapter VII, debates of inequality, poverty or taxation policies are heavily influenced by apriori values and preferences. For example: Whoever takes the view that markets are the prime instrument to create income and wealth and reduce poverty will argue against strong governments institutions and advocate tax competition instead. Conversely, those advocating for a balance between markets, and their regulation by democracies and governments will be in favour of tax cooperation.

It is essential that those value judgments are known before any debate on taxation policy is attempted. Knowing about those value judgements is also important to judge the value of various instruments discussed, e.g. Impact Investment, Corporate Social Investment, the freedom of wealthy people to determine the area of charity by setting up own foundations etc.

Our research is firmly based upon the Christian Faith and inspired by the principles and values of Catholic Social Teaching and wants to point to the experience the Catholic Church has collected throughout the centuries to strike a balance between the private and the social, between markets and states, putting human beings by virtue of their shared and equal dignity in the centre of whatever she does.

### **1.4 Result**

Our Project Concept contains the statement: ‘it is evident that there is enough money for public tasks, but it is increasingly difficult for governments and tax authorities to get their hands on it.’ For this we could find support in all three countries, even though the situation is particularly dire for Kenya and Zambia..

At the same time, the motto of the Kenya Revenue Authority ‘Pay your taxes and set your country free’<sup>2</sup> is unheeded among Kenyan (and also Zambians and German) elites: Private, corporate and criminal wealth holder in our countries, as in others, hide wealth to a considerable extent from the tax administrations and other authorities view. But only if everybody pays in accordance to his ability to pay that which is fair, it is indeed possible that some hypotheses formulated in our Project Concepts will come true: That Germany, Kenya and Zambia acquire more independence from “the markets” and its actors, and have more to invest in public goods such as health care, education and infrastructure. Additionally, in the case of Kenya and Zambia, they would acquire more independence from Official Development Aid.

For these reasons, three insights are key among the findings which we have presented in this paper:

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<sup>2</sup> ‘Kulipa Ushuru ni kulinda Uhuru’ The saying implies that African states, after having reached their political sovereignty, now face the challenge to acquire fiscal sovereignty.

1. Tax competition needs to be replaced by tax cooperation among states.
2. Taxation needs to be executed again in accordance to the Principle of the ability to pay.<sup>3</sup> This applies both within states but also between states.
3. To establish a fairer and more just international regime of taxation, developed and developing countries need to cooperate rather be in competition or dependency which exists right now – which brings us back to point 1.<sup>4</sup>

Subsequent to these three key findings, everything else has to be implemented and proportions have to be determined: Transparency regulations, the use of ITC technology, the question of personnel and staffing, the question of intergovernmental cooperation, the question of whether, and how, developed states could assist tax administration in developing countries on account of the fact that capital invested in developing economies usually has residence in developed countries.

## 2 Policy Goals

On that background, we developed the following ten observations which summarize our main findings. This chapter is based on the decisions taken at the last joint researchers meeting in March 2016. We propose measure to address the following areas of concern and policy goals:

1. Finishing tax competition, advancing cooperation with other states, especially with the intent to close legal loopholes by legal cooperation/treaties, followed by effective combating of aggressive tax avoidance and tax evasion and other tax related crime by effective national and international cooperation of tax administrations.
2. Diminishing inequality via asserting taxation following the Principle of Ability to Pay once more and (re-)introducing Wealth Taxation, by that financing the effective securing of equality of opportunities for all. This needs increased transparency by striking a better balance between privacy concerns and the public interest in fair burden sharing.
3. Removing poverty by giving some sort of existential security and other forms of social security to all. Regarding social security systems, remove opt-out possibilities for the wealthy from public solidarity systems and replace capitalized life- or pension insurances once more by one based upon intergenerational solidarity.
4. Fulfilling national and international obligations, i.e. to ensure a life in equal/comparable dignity for all (with challenges arising from demographic developments), living up to promises such as fulfilling the 0.7% goal or filling the Global Green Fund.

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<sup>3</sup> We are aware that this principle is challenged at both ends of society: At the lower end by the Informal/Shadow Economy, at the top level by private, corporate and criminal wealth holder. According to another established Principle of Taxation (see I/V), the Principle of Efficiency, it is our view start with focus on private, corporate and criminal wealth; whatever will be done regarding private and corporate wealth will also result in pushing back the latter since criminals profit from the same Offshore Constructs as private and corporate wealth holder. Thus, for example, transparency of beneficial ownership will hit malpractices of three birds at one stonethrow!

<sup>4</sup> Regarding the question whether reforms on part of developing countries need to be implemented before this cooperation and support starts or whether reform processes can be facilitated by this cooperation (see VI#): conversation partners both from tax administration departments, internationally active businesses and civil society point out that the involvement of outside experts is already one step towards more transparency.

5. Revising relationship between direct and indirect taxation, assessing impact of taxes upon poor and low-income households, more justice in the area of indirect taxation (e.g. no exemption for financial products, luxury VAT)
6. Reducing the intrusion of the private and corporate sector in financing public goods and public services, as can be the case with CSR, foundations, donations, sponsoring of education or PPPs, when it is conditional and – in the end – serves rather the interest of the donor rather than the public.
7. Reducing the influence of private and corporate wealth holder in economy, society and politics, curb lobbyism, corruption and other forms of state capture, repair damage arising from neoliberal globalization, e.g. the replacement of.
8. Reducing public debt which binds governmental spending for the benefit of living and future generations because of paying interest and repaying debt, perhaps via Wealth Levies.
9. Tackling global challenges which did not exist in the past and require cooperation and funding, e.g. IFFs, global migration, climate change, transnational crime in accordance with the Principle of Common but Differentiated Responsibilities as an adaptation of the Principle of the Ability to Pay.

All in all:

10. We came to the conclusion that voluntary systems of charity and solidarity generate considerably less for the common good than state imposed alternatives, which is why we propose more mandatory forms of contributions to the common good. At the same time we concede that private property and enterprise should be respected due to their positive characteristics. Here, Pope Benedict XVI's proposal of fiscal subsidiarity<sup>5</sup> could be a compromise between state-imposed limits to excessive wealth accumulation on the one hand, and private freedom in spending assets for the common good on the other.

### 3 Policy Recommendations

From the preceding “Decalogue” follow some more detailed recommendations. The following set arises from findings of our three countries and may contain complex implications for changes in policies, laws and administrations. The recommendations agreed among the research institutions are written in *“italics”*, some comments illustrating the point are added

#### 3.1 Recommendations arising from common themes

*Consider an increase in direct progressive taxation while cutting on indirect taxes and levies*

It is our view that direct taxation is among the best ways to reduce inequality and to generate revenue to invest into the improvement of the situation of the poor – for example, by offsetting losses which would occur when reducing VAT on basic means of nutrition. We are aware that the costs of administrating direct taxes to be collected at private and corporate wealth holder (assessment, auditing, verification...) requires more personnel at tax

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<sup>5</sup> Benedict XVI Caritas in veritatem Nr. 60 ‘One possible approach to development aid would be to apply effectively what is known as fiscal subsidiarity, allowing citizens to decide how to allocate a portion of the taxes they pay to the State. Provided it does not degenerate into the promotion of special interests, this can help to stimulate forms of welfare solidarity from below.’

administration and, therefore, is considerably more costly than the collection of indirect taxation. We feel, however, that these costs are justified if, given the complexity of laws, the avoidance and evasion options available for private and corporate wealth holder, tax justice is to be secured. Given the surplus revenue collected in our countries by investigative tax administration personnel we feel that any investment here will be worth its while and pay-off.

*If the share of direct taxation cannot be increased consider at least a Luxury VAT to make indirect taxation more just.*

This is only the second best option since the holder of private, corporate and criminal wealth can easily avoid this tax by simply buying elsewhere (except in the case of real property).

*Remove privileged access of lobby groups serving private and corporate wealth holder and increase participation of CSOs in the formulation of tax policies and tax laws.*

The discussion surrounding the reform of the Inheritance and Gift Tax in summer 2016 in Germany is just the latest example of how private and corporate wealth holder are able to influence governments and legislators. In order to reduce their influence, more transparency regarding lobbyist activities is urgently required as is more investigation into the “legislative footprint” of lobbyists in laws under discussion. Regarding the participation of CSOs it is essential to enact freedom of access to information so that CSOs can access information relating to fiscal issues.

*Increase knowledge and interest of the public in tax matters, e.g. by making tax education part of secondary education*

This recommendation follows from the preceding. Since participation is an important principle of Catholic Social Teaching everything should be done that people can be empowered to do so. Knowledge about taxation is also essential to improve compliance, especially in Kenya and Zambia.

*Remove tax privileges of capital as opposed to labour, e.g. different tax rates for income from capital and income from labour*

We note that in all our countries income from (dependent) labour is taxed much higher than income from capital, both recurrent (interest) or once-off (capital gains). This is also unfair because income from labour is directly earned, while income from capital is at best indirectly earned and privileges its owner by the simple fact that he possesses it. We advocate to tax income from capital “synthetically” with the same rate as income from labour.

*Put a turnover tax on the trade with Financial Products*

Given the nature and options available in and driving financial globalization and privileging Rent Seeking behavior rather than investment into the real economy, we advocate the taxation of the trade with financial products (Financial Transaction Tax) and recommend considering a VAT on financial products. It does not make sense to tax bread, milk and nappies while at the same time privileging the trade in derivatives. A side-effect of a Financial Transaction Tax would be the reduction of algo-trading, thus bringing back more stability to financial markets.

*Implement a wealth tax on real property which is (beyond that which is self-used) rented out to others.*

A tax on real estate and real property is, in our view, besides a tax on capital the best and most justifiable approach to tax wealth and reduce its concentration among the few. We are aware that also churches are among those holding a lot of real estate and enjoying tax privileges. Here we argue that any income arising from this possession and is directly devoted to the service of the poor should remain tax free. The same applies which is used for direct payment

and social security, including retirement, of its employees. Any income which is used to accumulate profits and reserves should be taxed as is the income of private and corporate holder of real property since here, too, the community contributes to the value of assets and potential income deriving from it, which is why the community deserves some contribution.

### **3.2 General policies**

“General policies” address wider policy preferences underlying tax related policies and has implications for laws and administration alike.

*Stop Tax competition, improve Tax cooperation, most importantly, find ways to close down Tax Havens.*

This follows from our discussion of IFFs (see VI/#) and our ethical discussion regarding the “propria” of markets (competition) and states (cooperation, see VII#)

*Remove options inherent to existing economic and financial structures enabling IFFs, e.g. the present system of protecting beneficial owner of trusts and foundations. Take measures to increase transparency regarding assets of private, corporate and criminal wealth holder.*

The present form of financial and ICT globalization contains options which enable private, corporate and criminal wealth holder to hide assets from states and, accordingly, taxation. This applies to a whole range of financial products, e.g. derivatives or hybrid constructs, which can be used to diminish the tax bill, but most of all it applies to Offshore Constructs. Here we join ranks with those who advocate for transparency regarding the beneficial owner of corporations, trusts and foundations, preferably in public registers. We are aware of the concerns of private wealth holder regarding privacy and business regarding trade secrecy concerns but, on balance, we agree with former EU Commissioner Semeta who, facing the extent of tax dodging, argued that “Tax transparency is more important than data privacy.” We also recall the German Federal Constitutional Courts repeated ruling that privacy is not an absolute, but a composite of intimate, private and social components (Hüsken).

In addition we argue for the creation of publicly accessible registers regarding the beneficial ownership of financial assets and real property.

*All alternatives to taxation need to demonstrate that they contribute as much to the common good as taxation does.*

This policy recommendation arises from our ethical discussion of alternatives to taxation (see VII#)

*Explore ways how taxation or levies could be a way to diminish environmental degradation by, e.g., making the waste of non-renewable energy more expensive and saving more attractive.*

In our view, “taxing the bads” is a promising way to curb the overutilization and exploitation of natural resources and to encourage environmentally friendly innovation. An important caveat is, however, that the tax burden should be borne by all fair and square to avoid imbalances as in the case of Germanys Renewable Energy Levy which is largely borne by private households, while businesses obtained generous exemptions.

*Revise Double Taxation Agreements under the perspective whether they disadvantage the interests of developing countries.*

We welcome review processes of Double Taxation Agreements and request a fairer and more equitable outcome for developing countries.



*Developing countries should live up to their 0.7% commitment. The funds should not be given to governments but rather go, for example, into the build-up of Social Security and Social Welfare Systems, the build-up of Infrastructure and capability building programs for people.*

Looking at the demographic development, the extent of rural-urban migration and the extent of the informal economy we see the need of establishing modern social security and social welfare systems in Kenya and Zambia. Funds earmarked for social sector spending must be ring-fenced in order to guarantee progressive investments in this critical sector that mitigates extreme poverty. Similarly we advocate direct investment into improving the infrastructure of our countries which would increase the attraction to open businesses and generate formal employment.

*Reform existing systems of Social Security and Social Welfare to the extent that all citizens of a country are bound to contribute in accordance to their ability to pay and enable all in need to receive assistance.*

In all our countries, the burden of mandatory security contributions is unfairly distributed and a fairer burden sharing is called for.

*Regarding the extent of wealth inequality right now start public discussion about whether wealth holder contribute adequately to the common good or not and how this could be changed.*

Provided transparency and the implementation of a right to information as well as education of the wider public about the sense and use of taxation are implemented (see above, 2.1), a broad discussion within our respective countries should ask whether all members of the society contribute to the Common Good in accordance to their ability to pay and, if this is not the case, how could this best be changed within the respective country's context.

*Could Pope Benedicts proposal of "Fiscal Subsidiarity" be an acceptable compromise between private and corporate interests and the need to increase the contribution of private and corporate wealth-holder to the common good, especially the combating of poverty?*

Pope Benedicts proposal could be a good compromise between the states right to ask for a certain share of private and corporate wealth, and the freedom of choice on part of private and corporate wealth holder. For example: If the state requests in the case of any form of wealth transfer that, say, 10% of the transfers value should be devoted to the reduction of poverty, it could be up to the transmitter or receiver to decide how exactly the money should be spent.

### **3.3 General tax laws**

*Remove vagueness and loopholes within and between national and international tax law systems and tax treaties which right now enable aggressive tax planning and tax evasion.*

This recommendation follows from the examples given in #### and the fact that it is to a large extent those who are capable to employ expensive expert advice who are able to draw benefit from this situation.

*Remove all options so far available for tax fraud (e.g. Missing Trader Fraud or Trade misinvoicing and mispricing)*

This follows from the previous with a particular emphasis on IFFs, being mindful of the world leaders commitment to SDG Target 16.4, pledging to reduce IFFs until 2030 by half.

### 3.4 General tax administration

*Make easier cooperation between tax administrative staff on the one hand, and investigative bodies when discovering criminal acts (subject tax secrecy to public interest in fight crime).*

Besides time pressure and lack of resources when auditing books and accounts a major area of uncertainty seems to occur on part of tax officials as to when to break the tax secrecy and to forward a case to criminal investigation. Here it should be stated clearly that tax secrecy holds second place in case an initial suspicion arises during an audit that a case of IFF might be at hand.

*Improve options for national tax administration to cooperate in the enforcement of national and international tax laws, e.g. by enabling Joint Audits*

We agree with those conversation partners that the best way to uncover aggressive tax avoidance, tax evasion and other forms of IFFs is a close cooperation of different tax administrations, ideally in Joint Audits. That way, little information gets lost, it is more difficult to play inspecting teams off against each other and it is more difficult to hide information.

*All national tax administrations need well trained experts on international tax enforcement issues.*

As long as there are no comprehensive transparency regulations in place and as long as the international taxation system remains basically as it is, tax administrations need to step up their number of well-trained experts in those matters. Since for good people in this segment is a tough competition with the private sector, adequate payment etc. is key for attracting people. We recall our observation in VII/5.6.4 that such an investment pays off for the state.

*Developed states should step up their efforts to assist developing states in effective tax administration*

All examples we learned from experts from developed countries assisting tax administrations in developing countries were positive. This is why we would advocate this form of “developmental aid” as an important means for our countries to gain (true) independence, this time from external markets and IFFs. There are plenty of declarations, e.g. the Addis Ababa Action Agenda and many good proposals, e.g. (Kar & Spanjers, 2015, p. 19ff.) – they simply need to be implemented. Of course this should be augmented with knowledge transfer technologies to boost the productivity of developing countries industries.

*Developed states should share insights from AEOI and BEPS, even though developing countries might not yet be able to reciprocate.*

According to the present state of discussion, developing countries are excluded from many beneficial insights arising within the AEOI and BEPS mechanisms due to the lack of resources and the inability to reciprocate. One issue is that Country-by-Country reports are only accessible to tax authorities in the country of the companies headquarters, whereas it is our opinion that the information should also be made accessible to tax administrations of other countries where the company is active. Equally, data from AEOI agreements should be made accessible to the tax administrations even if those countries are not yet in the situation to reciprocate.

*Have an ITO in place to settle conflicts between states, similar to WTO*

Last not least we advocate changes in the present imbalance of power between developed and developing countries regarding the determination of the framework and rules according to which tax laws and tax cooperation are being defined. Since in this case conflicts will be

inevitable, an independent taxation organization outside the present line of conflict between OECD and G77 might be called for which is able to mediate in the case of conflict. In order to be accepted, this institution would need an own legal foundation so that it has at least the legal basis to be an impartial mediator. Proposals here are made by (Dietsch & Rixen, 2016a) and (Tanzi, 2016).

## 4 Final observation and outlook

This research and its policy recommendations highlight many tensions which are difficult to reconcile. For example between the Common Good of one state and the Global Common good, between markets and states, between elites, technocrats and democratic institutions etc. Some will lose when our recommendations are implemented. For example Germany, being among wealth states, would stand out to loose, if the international trade and investment pie is fairly shared and distributed. Subsequently, it would end up with less revenue as it is the case right now. On the other hand, there is emerging knowledge about the “good life”, namely that there are many things which markets cannot make and money cannot buy, for example a clean environment, social stability, less migration. From such a world everybody would profit, even those who would end up with a little less money.

We clearly draw from our work the conclusion that in today’s world, given the current structures of power and dominance, the discussion about instruments of taxation as instruments to combat the concentration of wealth and advance the Common Good via redistribution are not only reconcilable with Catholic Social Teaching, but essentially recommended by Catholic Social Teaching, which implies the entire question of “how to tax wealth” better than it is the case in contemporary economies.

We are alive to the fact that comprehensive tax reforms that addresses horizontal and vertical disparities is easier said than done. Nevertheless, states have no choice but to sustain efforts to pursue a taxation policy that aims at tax justice. Of course compromises remain unavoidable in this regard. But given our proposal in VII/2 that we should not waste our time to establish “Tax Justice”, but rather, by looking at the unfairly distributed profits and burdens in this world, for a *more fair* and *more just taxation* in comparison the situation right now relative to what is currently obtaining. Which we hope may contribute to a more fair and more just world with less inequality.

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