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Haven no more

Tax dodging happens because wealthy nations let it. It's time for poorer countries to shape the rules

Tax dodging and illicit financial flows began to emerge as a major source of concern for civil society organisations around the year 2000. Since then, revelations that big multinationals such as Google and Starbucks have not paid their fair share of taxes – even in rich nations – have gone from a trickle to a flood. It is now common knowledge that tax dodging affects both industrialised and developing countries alike. Thankfully, tax now takes high priority on regional, national and multilateral policy agendas – a significant step forward. But we still haven't found a global solution to this most global of problems. International tax rules are in dire need of reform, but to be effective, developing countries need to be involved in shaping them.

Several new initiatives outside of the UN system are being set up to deal with issues of international tax. Many of these are initiated and led by the Organisation for Economic Co-operation and Development (OECD), whose expertise and capacity in tax matters is unmatched among multilateral institutions.

The OECD is a "club of the rich", comprising 35 industrialised nations. It cannot claim neutrality. In 2013, the G20 mandated the OECD to come up with a series of reforms to international tax rules through its base erosion and profit shifting (BEPS) project. 2000 pages of decisions were duly made without the participation of the majority of developing countries. This was clearly not a democratic process.

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This is not to deny the OECD the right to initiate a debate. But many of its members also insist on keeping important negotiations on international tax within the OECD. They consider decisions made in OECD fora to be "global" standards, despite the organisation's limited membership. And OECD-led initiatives are used to justify rejecting proposals to bring tax related issues into the UN, which would

allow all countries to negotiate and shape the tax agenda on an equal footing.

Transparency: leading by example

When it comes to fighting tax dodgers, there needs to be an intergovernmental process in which the public has access to negotiating documents, procedures, positions of governments and decisions. Only a transparent intergovernmental process can ensure the negotiating positions of governments are in the public interest, and allow people to hold governments to account for what they commit to and what they don't. Opaque and closed-door processes leave the doors open for rich countries to exercise a disproportional influence on negotiation positions, shaped by vested interests. A reform of international tax rules will only benefit all.

A case in point is the OECD base erosion and profit shifting (BEPS) package. BEPS refers to tax avoidance strategies that exploit loopholes in tax rules to artificially shift profits to low or no-tax locations. The package fails to address some of key issues in international tax, such as race-to-the-bottom tax competition between countries, and whether income or profits resulting from international activities are taxed where the income is earned (the source country) or where the legal person who earned the taxable income is nominally based. The BEPS package employs the "arm's length principle", whereby all parties to a transaction are treated as independent and on an equal footing. It's supposed to guard against related companies artificially distorting the price at which a trade is recorded, but in practice is often ineffective. It still gives multinationals too much leeway to decide where in the world to shift their profits.

Far preferable would be a system of "unitary taxation", where a corporation is taxed based on its worldwide income, rather than on its income in the country of the tax authority. The tax bills would then be apportioned according to real world factors such as where a company's workplace is based, where its assets are held, and which countries' resources it relies on to do business.

An example of this is the Common Consolidated Corporate Tax Base (CCCTB), proposed by the European Commission in 2011 as a single set of rules multinational companies could use to calculate their taxable profits in the European Union. The tax base of the whole corporate group would be identified, with no regard for sleights of hand when it comes to transactions between its affiliates. Rather, taxable profits would be apportioned in a way that reflects the firm's real activity in each

country. Since the original proposal was deemed too "ambitious" to implement in one fell swoop, the Commission is now looking at implementing a similar policy in stages.

The same approach to CCCTB should be used internationally. It would help minimise tax competition between states and hamstring attempts by multinationals to avoid tax by shifting income from high tax countries to affiliates in jurisdictions with low rates of tax.

As indicated above, the BEPS package is not a negotiated outcome agreed by the majority of UN member states. The OECD has now created a so-called "Inclusive Framework" open to all jurisdictions for implementing the BEPS outcomes and setting standards "in respect of remaining BEPS issues". All members have to agree to these standards, which means that tax havens such as Jersey and the Isle of Man also have a significant say. Since these territories' interest lies in protecting their status as tax havens, their consent will surely lead to any proposals to crack down on dodgy profit shifting being watered down. Such proposals would, in the words of the independent BEPS Monitoring Group "be harmful for all, as weak coordination of the international tax system undermines every country's ability to apply effective tax rules to multinational enterprises, and hence its sovereignty".

Tackling tax evasion with such watered down legislation is like attempting to seal off loopholes with a sieve. Providing capacity building for developing countries to operate rules which are defective will not prevent tax dodging.

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Tax evasion and avoidance happens not because of a lack of capacity to collect revenue. Rather, they are a deliberate business strategy of multinationals and wealthy individuals, supported by a network of enablers such as banks, audit firms, legal advisors and secrecy jurisdictions.

Finding a global solution to global tax evasion and avoidance will undoubtedly be a difficult, messy and protracted process. But transparency, and the involvement of all countries, are paramount, as is UN involvement.



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