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Some states are more equal than others

Rich countries design the international tax system by themselves. This leaves developing nations in the position of rule-takers

The Charter of the United Nations lays out that the UN is founded on the basis of sovereign equality of all its member states – implying all states have equal rights and duties as equal members of the international community. In September 2011, the Human Rights Council adopted resolution 18/6, which was even extended twice for a period of three years each, in 2014 and 2017, on the promotion of a democratic and equitable international order. The resolution affirms that such an order will foster the realisation of human rights for all, and that everyone is entitled to it.

It's interesting, then, that a group of rich, developed countries voted against this resolution each time – making one question whether countries like Germany, Japan, Switzerland, the UK and US stand against democracy, equity and human rights, or against all countries being able to realise these values.

The hilarious neo-colonialism that marks our age is probably most noticeable in the design and architecture of the international tax system. The foundations of this century-old arrangement – comprising a loosely coordinated system of bilateral tax treaties – were laid when most businesses and corporations were primarily national, international economic flows consisted of trade and portfolio investment, and multinational corporations (MNCs) were in their infancy.

A shift to global models

The world has since witnessed a steady financialisation of capital, removal of trade barriers, integration of national economies and markets, and technological developments – all of which resulted in a shift from country-specific operating models to global models and integrated supply chains. As MNCs grew in dominance in the world economy, the global

value chains they coordinated came to account for about 80 per cent of global trade. Consequently, the international tax system has effectively cracked along its fault lines to lay bare the systemic extractivism it has historically enabled.

Following the global financial crisis of 2007-08, the hegemony of the World Bank and the IMF was replaced by that of the G20 and OECD over shaping norms of international finance and taxation. The G20 has at best paid lip service to issues such as tax havens, tax abuse by MNCs and the global elite and secrecy in the global financial system. With infrequent meetings and a crowded agenda, the G20 most often delegates its already incoherent and inconsistent efforts on international tax reforms to the OECD.

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Norm-setting institutions also include an extended web of lesser-known technocratic bodies including the Financial Action Task Force, Bank of International Settlements, Basel Committee on Banking Supervision and International Accounting Standards Board, most of which are linked with one another directly through funding agreements and reciprocal membership. These bodies are mostly exclusively comprised of developed countries and are headquartered in the Global North, leaving most of the world's developing countries as well as the world's population looking in from the outside.

This democratic deficit in the architecture of the global financial system raises critical questions about these institutions and the constituencies they represent. The undemocratic, unrepresentative and opaque nature of the global financial system ensures that it works in favour of developed countries at the cost of their developing counterparts. Further, there is a glaring lack of transparency and accountability in its agenda-setting and functioning, allowing for a revolving door between these bodies, the global elite and corporate lobbies.

By the rich, for the rich

There is no doubt, then, that the reforms propagated by these institutions are deliberately unambitious in their design and patchy in their implementation, and end up excluding developing countries from reaping benefits from new standards.

To be fair, the G20 and OECD did design a key transparency tool to address cross-border tax evasion and the abuse of a porous financial system by wealthy elites: the Automatic Exchange of Financial Account Information in Tax Matters. This standard aims to create a global network of exchange to allow financial information to flow between countries automatically and regularly, allowing states to have actionable evidence regarding their citizens' assets abroad.

However, the OECD designed the standard without meaningful consultation of low-income countries, resulting in a system of exchange designed by rich countries for rich countries. Many prerequisites for the standard are impossible to realise for countries without large tax administrations or technical capacity. The standard also ensured a loophole whereby countries would be able to pick and choose the partner countries with which they would exchange information. Obviously, then, why would Switzerland ever agree to exchange information with Bangladesh? High-income countries thus receive most of the information they need but share very little – meaning low-income countries receive next to nothing.

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This happens in a context where cash-strapped countries in the Global South would benefit hugely from information from developed countries, which are home to most financial capitals where the elite park their illicit wealth. Thus, despite the OECD congratulating itself on more than 100 jurisdictions committing to the standard, there is nothing global or automatic about the standard on Automatic Exchange of Financial Account Information.

Time to pass the mic

The OECD's Base Erosion and Profit Shifting (BEPS) project is a similar case. It claims to equip countries with domestic and international instruments to address the exploitation of gaps and mismatches in tax rules that allow corporations to artificially shift profits to low- or no-tax locations. But developing countries weren't included at all in the various stages of policy development. Instead, the OECD invited 14 developing countries to meetings at the end of the project, once the lack of representation had been widely criticised. More than 100 developing countries had no space to be involved in decision-making and were only invited to provide comments to public hearings and participate in regional consultations.

Moreover, the BEPS project did not even scratch the surface of the main concern faced by developing countries: a skewed allocation of taxing rights, which prevents developing countries from taxing MNCs —despite the fact they create value in these nations. The arm's-length principle of transfer pricing failed to witness a resolution. This principle says the value of a transaction between related entities must be the same as if the entities are unrelated. But MNCs regularly abused it to shift profits from countries where they create value to low-tax jurisdictions.

What the BEPS project did extremely well, though, was to complicate an already complex international tax system by adding thousands of pages of guidelines. The OECD is now developing toolkits for 'low-capacity developing countries' to help them implement myriad international tax rules (that they had no role in designing) through an 'inclusive framework'. It seems nobody told the OECD they wouldn't need an 'inclusive framework' if they didn't work so hard to exclude most of the world from norm-shaping in the first place.

Being at the table is crucial to having developing countries' voices heard, and their concerns and priorities shape the agenda of international taxation. Building capacity, increasing technical knowhow and expanding tax administration departments are not solutions on their own. Developed countries and the global elite who benefit from this broken international tax system need to stop speaking on behalf of developing countries and just pass the mic.



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