International tax emergency: A critical time for developing nations to speak up!

By José Antonio Ocampo
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In the face of global outrage at the low or no taxes paid by some of the world's largest multinationals, the Group of 20 appointed the Organisation for Economic Co-operation and Development a few years ago to design alternatives to end these abuses. In response, on October 9th, the OECD put forward proposals for a new international tax system which could be imposed on the world in the coming decades.

This is a major issue. In the United States, for example, 60 of the 500 largest firms—including Amazon, Netflix and General Motors—paid no taxes whatever in 2018, despite a cumulative profit of $79 billion, because the current system allows them to do so, and in a completely legal way.

These misappropriations are based on complex arrangements but a very simple principle. The multinational only pays taxes in the subsidiary where it declares its profits. This way, it shows low profits or deficits where taxes are relatively high—even if that is in those countries where the firm undertakes the bulk of its activities. And it reports high profits in jurisdictions where taxes are very low, or even zero—even if the firm has no customers there.

As a result, every year, developing countries lose at least $100 billion, hidden by multinationals in tax havens. Globally, this diverts 40 per cent of foreign profits to such havens, according to the economist Gabriel Zucman.

Constantly increasing

With the accelerated digitalisation of the economy, the amounts diverted are constantly increasing—this many institutions, such as the International Monetary Fund and the United Nations Conference on Trade and Development, have highlighted. But the most important move has come from the OECD, with its mandate from the G20 to propose alternatives to the current international tax system, including the effects of digitalisation.

After decades of inaction, the process could move forward very quickly. Following the recent publication of its proposal, the organisation will make a final one in 2020, laying the base for the new system. After that date, it will be practically impossible to influence the reform process.

That is why we need to raise the alarm for developing countries. They can no longer say that they have no voice in the process. The OECD has given them a place at the negotiating table by creating a group called the 'Inclusive Framework'. With 134 members, this is the arena where tomorrow's global tax system will be decided.

Unfortunately, despite its name, we do not play on equal terms within this 'Inclusive Framework'. Rich countries have greater human, political and financial resources, to make their views prevail. With the largest concentration of multinational headquarters, they are also those most influenced by corporate pressures—at the expense of their own citizens and the rest of the world. But by refusing to realise what is at stake, developing countries are also failing in their responsibilities.

Two pillars

The OECD reform proposal is based on two 'pillars'. The first is to establish clearly where corporate profits are generated for tax purposes. The ideal—for which ICRICT, the tax reform commission I chair, has been fighting for years—would be to treat multinationals as single firms; total profit should then be taxed where they operate, according to objective factors, such as employment, sales, digital customers and natural resources consumed.

In this field, however, the OECD's proposals are neither ambitious nor fair enough, as we explained in our latest report. The share of profits which would be redistributed internationally would be limited to the so-called 'residual' of the multinationals' total profits. Worse still, this principle would only apply to very large multinationals and the allocation of these profits would depend solely on volume of sales, excluding employment and other factors that would favour developing countries.

The second pillar is the establishment of an effective minimum corporate tax at the global level. Some developing countries fear that by abandoning the weapon of tax incentives, they will no longer be able to attract investment from multinationals. Yet the evidence that these incentives attract investment is controversial, according to IMF research.

Even more importantly, if the international community agrees on a sufficiently high rate (ICRICT pleads for at least 25 per cent, the average rate in developed countries), this would put an end to the race to the bottom which we are witnessing, with the multinationals the only winners. This measure would remove the *raison d'être* of tax havens, while ensuring that all states enjoy access to resources essential for development.

Alternative solutions

In the absence of an international consensus, some countries have chosen to find alternative solutions. This is the case for France, which will tax at 3 per cent the turnover of firms in the digital sector. Others, such as Mexico, are considering the possibility of forcing platforms such as Uber or Netflix to pay value-added tax on services provided in the country.

While it is a good initiative to tax revenues which are now escaping, it is impossible to compartmentalise the digital economy and take it as the sole objective of the reform: more and more firms are using digital technologies as part of their commercial activities. And it is not via such one-off measures that states will emerge from deficits and repeated austerity cures.

It is time for developing countries to mobilise. Increasing their fiscal resources is the only way to improve access to health and education, to pursue gender equality or the fight against climate change. If the heads of state and finance ministers of these countries continue to underestimate the importance of these debates, they will soon find themselves forced to accept a new international tax system that will not suit them. The winners will still be the same—but then it will be too late to complain.

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