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Durst is also the author of the forthcoming book *Taxing Multinational Business in Lower-Income Countries: A Problem of Economics, Politics and Ethical Norms*, which *Tax Notes International* will serialize in six installments over the coming months. The book explores a topic that has been highly controversial in recent years: the use by multinational companies of “base erosion and profit shifting” tax planning structures to reduce their tax liabilities in countries where they conduct business, including the world’s lower-income developing countries. In this installment, which is Chapter 1, the author provides an introduction to BEPS and an overview of the book.

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Motivation for This Book

As the 2008 financial crisis sparked widespread public anger toward the world’s large companies, investigative news reporters and nongovernmental organizations revealed that the world’s multinational business groups were routinely avoiding hundreds of billions of dollars of corporate income tax each year in the countries where they conduct business.¹ Multinationals were accomplishing this by shifting profits from countries where they earned their income to zero- and low-tax countries where the groups often appeared to conduct little if any business activity. The profit-shifting payments were not being made secretly; to the contrary, tax agencies around the world had for many years been aware of them. However, under the system of international tax laws that has been adopted by virtually every country of the world, and has been coordinated globally by the Organization for Economic Cooperation and Development, a Paris-based organization consisting mainly of the world’s wealthiest governments,² countries’ revenue-protection agencies could not prevent the income-shifting.

The reports by news media and by nongovernmental organizations tended to focus on the effects of tax avoidance in two different

¹ See, e.g., Christian Aid, “False Profits: Robbing the Poor to Keep the Rich Tax-Free,” (2009); ActionAid, “Calling Time: Why SABMiller Should Stop Dodging Taxes in Africa” (2010; updated 2012) (reports by nongovernmental organizations); and Charles Duhigg and David Kalinowski, “How Apple Sidesteps Billions in Taxes,” *The New York Times*, Apr. 28, 2012; Jesse Drucker, “IRS Auditing How Google Shifted Profits,” *Bloomberg.com*, Oct. 13, 2013; and Hugo Duncan and Tamara Cohen, “Starbucks ‘Treats Tax Like a Church Collection Plate’: Treasury Chief Secretary Attacks Coffee Chain,” *Daily Mail*, Dec. 9, 2012 (news articles).

² OECD member countries include Australia, Austria, Belgium, Canada, Chile, the Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Israel, Italy, Japan, Korea, Latvia, Luxembourg, Mexico, the Netherlands, New Zealand, Norway, Poland, Portugal, the Slovak Republic, Slovenia, Spain, Sweden, Switzerland, Turkey, the United Kingdom, and the United States.

groups of countries. Media reports generally emphasized the effects of profit-shifting on wealthier industrialized countries. Following the financial crisis, the governments of many of these countries were experiencing fiscal shortfalls. Some especially widely noted news reports focused on well-known U.S. companies, including Starbucks, Amazon, and Google, that were earning large revenues from sales in the United Kingdom while paying little if any corporate tax there.³

The reports by nongovernmental organizations, on the other hand, focused on the effects of profit-shifting from the world's poorer developing countries. These countries typically face a chronic shortage of public infrastructure to meet people's most basic human needs, in areas like the supply of clean drinking water, health care and primary education. The nongovernmental organizations argued that by depriving countries of the financial means to build infrastructure in these and other areas, corporate tax avoidance was effectively perpetuating widespread personal suffering. One report, for example, suggested that if corporate tax avoidance were to be eliminated, the deaths of tens of thousands of children annually might be prevented.⁴

Some of the media and NGO reports acknowledged that the profit-shifting they were

describing generally was "legal," in the sense that it was permissible under the tax laws of the countries that were involved. Nevertheless, the authors of the reports made no attempt to conceal their belief that the tax avoidance reflected moral failure on the part of a number of politically powerful actors: the multinational companies that engaged in the avoidance; the lawyers, accountants and other tax professionals who advised them; the OECD and other intergovernmental groups that had perpetuated ineffective tax laws; and national governments that seemed content to retain those laws on their statute books despite their apparent failure to contain revenue losses.

The media and NGO reports generated a strong public reaction, especially in the economically developed world. Parliamentarians in some countries conducted inquiries at which legislators were highly critical of the world's most prominent multinational corporations. In one widely reported instance, for example, a senior U.K. Member of Parliament criticized U.S. multinationals Starbucks, Amazon, and Google as having fallen short of basic ethical standards in engaging in tax-avoidance practices, notwithstanding that the avoidance appeared legally permissible. "We are not accusing you of being illegal," the M.P. declared, "we are accusing you of being immoral."⁵

In response to these developments, in 2012, the finance ministers of the G20 group of countries⁶ directed the OECD to conduct a multi-year inquiry into the phenomenon of what the OECD labelled "Base Erosion and Profit Shifting," or "BEPS." Senior officials of both the G20 and the OECD expressed the view that BEPS-style tax planning around the world was eroding public confidence in national and global economic institutions, and should no longer be tolerated. The OECD began its study of base erosion and profit shifting in 2013, promising a thorough reassessment of the body of international tax laws

³ See, e.g., the article from the *Daily Mail* cited at note 1 *supra*, and the BBC report cited at note 5 *infra*.

⁴ Christian Aid, "Death and Taxes: The True Toll of Tax Dodging" (2008) at 2. The report claims that if tax revenues lost in developing countries to two forms of corporate behavior – "legal" avoidance of the kind addressed in this book, and certain criminal tax avoidance consisting of the falsification of trade documents – could be recovered, "then the lives of 350,000 children under the age of five would be saved every year – including 250,000 babies" (emphasis in original).

The quantitative analysis of the Christian Aid study has been criticized, and the report may substantially overstate the revenue losses that countries experience from corporate tax avoidance. See Clemens Fuest and Nadine Riedel, "Tax Evasion, Tax Avoidance and Tax Expenditures in Developing Countries: A Review of the Literature," Oxford University Centre for Business Taxation (2009); and Maya Forstater, "Can Stopping 'Tax Dodging' by Multinational Enterprises Close the Gap in Development Finance?" Center for Global Development (2015).

Moreover, it must be remembered that increased corporate tax revenues alone will not necessarily improve social well-being in a country. It is also necessary that the revenues be used to meet unmet social needs, rather than being misappropriated through corruption and inefficiency. See, e.g., Timothy Besley and Torsten Persson, "Why Do Developing Countries Tax So Little?" 28 *Journal of Economic Perspectives* 99, 113 (2014). This book will include reminders of a number of places that effective tax policy represents only one among many requirements for the alleviation of poverty in the world's poorest countries.

⁵ See, e.g., BBC, "Starbucks, Google and Amazon Grilled Over Tax Avoidance" (Nov. 12, 2012).

⁶ The G20 countries include Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, Republic of Korea, Mexico, Russia, Saudi Arabia, South Africa, Turkey, the United Kingdom, and the United States.

that the OECD historically had been responsible for articulating and maintaining.

Although the OECD draws its membership from the world's wealthiest countries, the OECD acknowledged that revenue losses from base erosion and profit shifting were affecting developing countries especially acutely. The OECD therefore invited developing-country governments to participate in the BEPS studies. In addition, intergovernmental organizations active in the field of international development, including the IMF, the World Bank, and the United Nations, collaborated with the OECD and produced several extensive analyses that focused particularly on the situation of developing countries with respect to corporate profit shifting.

In late 2015, the OECD issued final reports from its BEPS studies, recommending a number of legislative and administrative measures that governments might take to curtail the shifting of income by multinational groups. In addition, a consortium of intergovernmental organizations, including the OECD, the World Bank, the IMF, and the United Nations, pledged to join in a sustained program of technical assistance, to help the world's developing countries implement the BEPS recommendations and otherwise improve the performance of their tax systems.

This book seeks to provide a critical, and in some ways novel, assessment of base erosion and profit shifting as it affects the world's lower-income countries,⁷ and of the current efforts of the OECD and other international organizations to curtail the phenomenon. I write this book from the belief that the advocacy of NGOs and others, described above, performed a valuable service in bringing the tax situation of lower-income

⁷ A note is in order about the use by this book of the term "lower-income" countries. It might be possible instead to use the term "developing" countries, but this term is used popularly to describe countries at many different levels of per capita income, some of which are relatively wealthy by global standards. The World Bank uses the terms "low-income" (per capita income of \$1,005 or less for fiscal year 2017-18); "lower-middle-income" (per capita income of \$1,006 to \$3,955), "upper-middle-income" (per capita income of \$3,956 to \$12,235) and "high-income" (per capita income of at least \$12,236). I use "lower-income" to denote countries falling roughly within the low- and lower-middle-income groups. (For the World Bank classification, see World Bank, "World Bank Country and Lending Groups.") It should be recognized that each World Bank category includes countries of widely varying levels of per capita income and social conditions, so that my use of the term "lower-income" inevitably encompasses countries that differ from one another in many important ways.

countries to greater public attention. I believe as well, however, that the problems of corporate taxation in lower-income countries reflect a longstanding, complex, and stubborn mix of political and economic influences, and that the post-2008 public exposure represented only the beginning of a still incomplete process of understanding the roots of the problems that have been identified. As will be discussed below, largely through the OECD's BEPS process, progress has been made toward improving the performance of the corporate income tax in lower-income countries, but the process of reform has only begun. The BEPS process has to date been unable to address some of the most central difficulties faced by lower-income countries, and some of the fundamental political and economic causes of those difficulties have not yet been sufficiently aired and confronted.

The Book's Fundamental Argument

This book addresses three fundamental questions:

- Would curtailing base erosion and profit shifting in lower-income countries be in the interest of the people of those countries, especially in facilitating the alleviation of poverty?
- What are the political and economic roots of BEPS-style corporate tax planning?
- What policies might lower-income countries realistically pursue to reduce their vulnerability to base erosion and profit shifting?

With respect to the first of these questions, the book concludes that BEPS-style tax planning does properly demand the continuing attention of policymakers around the world. The world's poorer countries are chronically short of the public revenues needed to combat persistent severe poverty, and as a practical matter the income generated by multinational companies within those countries represents one of the few realistically accessible sources of additional public funding, at least for the foreseeable future. There are limits, of course, to the extent that lower-income governments should seek to increase corporate tax revenues above current levels: at some level of increased corporate taxation, the social costs of reduced inbound

investment will override the social benefits of generating additional revenue. As will be discussed in Chapter 2, however, profit-shifting has become so pervasive in lower-income countries that corporate tax revenues today are almost certainly below socially optimal levels.

Therefore, curtailing BEPS-style tax avoidance should increase the likelihood of gains in social welfare for people in lower-income countries. This is not to say that increases in government revenues will lead inevitably to improvements in social conditions; many obstacles, including corruption and other shortfalls in governance, can obstruct the path between the collection of revenues and their successful use in promoting social well-being. Nevertheless, enhanced revenues should make badly needed social improvements more feasible than they are today, and for this reason curtailing tax avoidance in lower-income countries appears to represent a desirable policy goal.

With respect to the political and economic roots of BEPS-style tax planning, the conceptual core of this book consists of an historical interpretation of the phenomenon. The history of profit-shifting is a remarkably long one: all the techniques by which multinational groups currently use subsidiaries in zero- and low-tax countries in avoidance planning were already in use within a few years after the end of World War II, when the cessation of hostilities and wartime technological innovations permitted a flowering of cross-border trade and investment. I argue in this book that BEPS-style tax avoidance can be understood most usefully not primarily as a product of corporate wrongdoing, but rather as a consequence of the longstanding desires (i) of taxpayers to minimize their liabilities, and (ii) of the governments of countries at all levels of economic development to encourage investment by offering companies full or partial exemptions from corporate taxation.

To some extent, countries offer investors tax exemptions through explicit means, for example by enacting laws permitting “tax holidays” for investments in new businesses, or tax exemptions for starting businesses in economically disadvantaged areas within a country (“special economic zones”). All governments, however, face some degree of political resistance to the use

of explicit tax exemptions to attract investment, on grounds that the governments are showing excessive largesse to corporate interests. I argue in this book that the techniques that multinational companies employ to avoid taxes through the use of zero- and low-tax subsidiaries, and the international system of tax laws that protects the avoidance from successful challenge by revenue authorities, evolved as a means by which companies could obtain, and governments could tacitly provide, *de facto* exemptions from taxation with less political visibility than is entailed in explicit tax incentives.

My interpretation of base erosion and profit shifting as reflecting not only the desire of multinational companies to avoid taxes, but also the desire of governments to facilitate that avoidance to encourage inbound investment, raises the question whether the recommendation that the international community take steps to curtail the avoidance incorporates an undesirable element of paternalism. After all, if governments of lower-income countries have tolerated high levels of avoidance for many years, on the view that the resulting encouragement of investment outweighs the potential social value of increased investment, what standing do NGOs, journalists, tax scholars, and international organizations like the OECD, IMF, and World Bank have to encourage lower-income governments to try to curtail avoidance?

An answer to this question is found, I believe, in the nature – indeed, in the elementary mathematics – of international tax competition. If lower-income countries did not see themselves as competing with their neighbors to attract inbound investment, they presumably could drive a tougher tax deal with investing multinationals, increasing the amount of corporate tax revenues closer to socially optimal levels. But in fact, virtually all countries are eager to attract inbound investment, and whatever level of taxation a country might be willing to offer a potentially investing multinational, one or more other countries often will be willing to offer a lower level of taxation. The result is in effect a kind of auction, a “race to the bottom,” in which governments perceive little practical alternative but to permit investing companies to engage in some measure of tax avoidance.

In view of all this, it seems clear that a successful mix of policy initiatives to enhance corporate tax revenues in lower-income countries will need to include measures by which countries can to some extent be shielded from the pressures of tax competition. There really is only one way in which market competition, of which international tax competition is a species, can be mitigated, and that is by some degree of coordination among market competitors. Thus, for example, if lower-income governments could bargain with multinational groups not individually but instead as a bloc, they could in theory obtain agreement on a level of corporate taxation that would optimally balance the competing goals of raising public revenues and maintaining a favorable environment for investment. Currently, little coordination of tax policies is in effect among lower-income countries, and given persistent pressures of tax competition, the degree of coordination that is possible is likely to remain limited for the foreseeable future. Nevertheless, it seems unavoidable that lower-income countries will need to achieve some degree of additional policy coordination, especially on a regional basis, if they are to implement policies to better shield themselves from BEPS-style tax avoidance.

And achieving this degree of enhanced market coordination is unlikely to occur without assistance and encouragement from parties in addition to lower-income countries themselves. We see today the inevitable result of leaving lower-income countries to counter the presence of tax competition without the support of outside intervention: the race to the bottom continues to operate largely unimpeded, leading to very high volumes of corporate income-shifting. Better results will require more effective political counterweights to the forces of international tax competition; and those counterweights will need to be provided not only by the world's lower-income countries themselves, but also by other politically empowered groups that are involved in the international tax lawmaking process.

In other words, it seems inescapable that substantial increases in corporate tax revenues for lower-income countries will require political acceptance, and even proactive political support, from multinational companies and the governments of their home countries. This will

involve the willingness of business interests, acting in concert, to refrain from exercising the full measure of economic power that tax competition affords them in their dealings with lower-income countries. In doing so, companies will need to be motivated not only by economic but also by normative goals. Essentially, a political consensus will need to be reached that current corporate tax laws and practices generate revenue at levels below those that can support socially desirable programs for the alleviation of poverty. Companies would therefore acquiesce in measured and predictable measures to increase the tax bases of lower-income countries for the same reason that they cooperate in, for example, international efforts to prohibit child labor or harmful environmental practices.

As will be discussed later in this book, the idea that multinational companies should voluntarily acquiesce to laws that limit their exercise of economic power in the tax context is bound to elicit political opposition. Asking companies' partial, voluntary forbearance from tax competition could be seen as an interference with global market mechanisms, which to some may be objectionable in itself. In addition, self-restraint by companies in the reduction of their tax liabilities could be seen as effecting a redistribution of income from the shareholders of multinational companies to the populations of lower-income countries, which also may meet opposition. Nevertheless, some degree of forbearance on the part of business interests, from taking full advantage of the opportunities presented by tax competition, seems to me indispensable if the performance of the corporate tax in low-income countries is to be meaningfully improved.

I need to defer detailed comment on the third question that this book addresses, of the specific corporate tax policy initiatives which might prove most useful to lower-income countries, until forthcoming chapters have provided additional background. Even at this preliminary stage, however, one common-sense prerequisite for effective international tax policies can be mentioned. Above all else, successful policy initiatives must be far less complicated than those that currently govern the taxation of cross-border trade and investment around the world. Later chapters of this book will argue that today's

international laws have evolved over decades to generate rather than reduce complexity and unpredictability of application, and that this tendency has greatly impaired efforts both to enforce the law, and to reform it legislatively, in countries around the world. The undue complexity of current law is problematic in countries of all levels of economic development, but the difficulties posed are especially serious for lower-income countries, which have limited resources to support both tax administration and legislative analysis.

There will be limits to the simplification of international tax laws. The many different kinds of business transactions engaged in by multinational companies often are inherently complex and therefore require a certain irreducible amount of complexity in the tax laws. Moreover, the enactment of tax laws typically requires political compromise, and compromise often results in legal provisions that, because of ambiguity, can be difficult to apply. Nevertheless, current international tax rules have evolved toward obscurantism as an end in itself. A new generation of international tax laws should be judged in significant part by the simplicity and transparency of their structure.

The main policy recommendations of this book all will involve simplification. For example, when examining the OECD's recent BEPS process, I will focus on two initiatives that the OECD has either recommended or addressed sympathetically in its work: proposals to simplify the manner in which tax authorities may apply "transfer pricing" rules,⁸ and rules placing quantitative limits on the amount of interest payments that corporations are permitted to deduct. These BEPS-related initiatives represent well-conceived attempts to reduce the complexity of current laws and can, I think, offer lower-income countries meaningful practical benefits.

I would extend the principle of simplification, however, beyond the policy initiatives that have figured during the recent BEPS discussions. In

⁸"Transfer pricing" laws govern the question whether the different companies within multinational groups deal fairly with one another (on an "arm's-length" basis), so that income is not shifted artificially to affiliates in low-tax jurisdictions. Transfer pricing laws have become especially complicated over the years; they are discussed in some detail in chapters 3 and 4.

particular, in Chapter 5, I will explore the possibility of a relatively simple statutory "overlay" that a country might place atop the more complex body of existing international-tax rules, to ensure that reasonable minimum levels of tax revenue can be collected even from companies that engage heavily in profit-shifting. Precedent for these kinds of overlays is provided by the "alternative corporate minimum taxes," based on gross revenue (turnover) rather than net income, that some developing-country governments have been applying for decades. Revenue yields from the minimum taxes could be calibrated so as to generate significant benefits to lower-income countries while remaining below levels that would be expected unduly to discourage inbound investment.

As will be discussed in Chapter 5, the minimum-tax approach has potential drawbacks and limitations. Among other things, its use of gross revenue as a base poses some economic disadvantages, particularly in placing some taxpayers at risk of taxation even in the absence of profits. Also, implementation of the minimum tax could, like all potential measures that would increase tax revenues, be impeded by pressures of tax competition. In addition, more must be learned about countries' experiences to date with the alternative corporate minimum tax; given that it has been in use for many years, surprisingly little research is available on how it has performed in practice. Nevertheless, under current political and economic circumstances, more widespread use of the tax may offer promise for lower-income countries, and it should be given careful consideration in international reform efforts. This book will suggest how minimum-tax proposals might be effectively researched and developed and, possibly, implemented by more countries on an internationally coordinated basis.

This Book's Intended Audience

I hope that this book will be useful to both specialists in the field of international taxation and, probably more importantly, to non-specialists who generally are conversant with questions related to public finance and international development, but who are not familiar with the complexities of international tax laws and practice. The body of laws that protects

the institution of base erosion and profit shifting has survived for more than sixty years in part because it is protected by an impressive layer of verbal camouflage. The legal guidelines and other official documents that memorialize the current system reach remarkable heights of verbosity and circumlocution, raising forbidding obstacles to newcomers who desire to approach the system and understand it. Professional insiders, therefore, have enjoyed a near-monopoly on policymaking in the field of international corporate taxation. Non-initiates will need to be able to see through the law's protective covering of complexity and gain an understanding of how the tax laws function in practice, if the range of actors who can participate effectively in policymaking is to be widened. Therefore, although I try in this book to avoid oversimplification, I also try to avoid the unnecessary use of specialized terminology. I try to summarize legal rules and corporate business transactions in relatively straightforward language, with technical details consigned to footnotes.

There is a limit, however, to the extent that the discussion in this book can be simplified (at least by me). Even if spurious complexity is pushed aside, corporate income taxation, especially in the international setting, remains an intrinsically complicated topic. I have therefore found the effort to keep this book accessible to non-specialists challenging, and I am certain that at best, I have succeeded only partially in doing so. Non-specialists (and maybe even specialists), therefore, are bound to encounter prickly tangles of verbal complexity in journeying through this book. For this I apologize and hope that the rewards of the trip outweigh any pain experienced along the way.

For those international tax specialists who might read this book, let me express the hope that you will find the discussions stimulating and useful, even though much of the analysis that I present is likely to be familiar to you. We who make careers in the tax field tend to spend much of our time and intellectual energy probing the law's minute complexities. We can focus so intently on relatively confined, technical topics that we risk losing sight of the overall political, economic, and ethical matrix in which we work. I

hope that even the most sophisticated international tax specialists will find this book helpful in gaining insights into the broad policy implications of the work that we do, and of possibilities for applying our expertise in new and helpful ways.

The Forthcoming Chapters

This book develops its argument in five chapters that follow this introduction:

Chapter 2 is entitled "Tax Competition and International Tax Planning." The chapter will examine the basic economic dilemma faced by lower-income countries with respect to the corporate tax, describing the tradeoff raised by the conflicting desires for enhanced public revenues and to encourage inbound investment. The chapter will explore the central policy question raised by tax competition in lower-income countries: namely, whether it can be said with confidence that increasing corporate tax revenues in lower-income countries is likely to promote social wellbeing. Given the ever-present tradeoff between raising corporate tax revenues and promoting investment, there almost certainly are potential levels of corporate taxation that would be so high as to generate net damage to social well-being in lower-income countries. Currently, however, evidence seems persuasive that because of the influence of tax competition, acting largely through the mechanism of BEPS-style profit shifting, effective rates of corporate taxation in lower-income countries are far below socially optimal levels. Therefore, policies that would reduce the incidence of profit-shifting from lower-income countries should on a net basis be expected to increase social wellbeing in those countries.

Chapter 2 also will offer an historical overview of BEPS-style corporate tax planning, describing the origins of the phenomenon in the years following World War II and its remarkable durability over more than six decades. I will argue that BEPS practices arose largely because they permitted both multinational companies and governments to afford companies *de facto* tax reductions on income derived from cross-border investment, but to do so in a relatively nontransparent manner. Chapter 2 will offer what I hope will be a reasonably accessible, but not

overly simplified, explanation of the mechanics of tax avoidance based on profit-shifting, outlining four basic transactional formats that are present in virtually all BEPS-style planning structures.

Chapter 3, entitled “The Evolution of Porous International Tax Laws,” will survey the various principles of international tax law that are intended ostensibly to control profit-shifting among members of multinational groups, but which instead have evolved over decades to insulate profit-shifting from successful legal challenge by national tax administrations around the world. The discussion in Chapter 3 will focus in large measure on the “arm’s-length principle” that underlays international “transfer pricing” law, as that law is codified in guidelines issued by the OECD and followed by national governments around the world. Transfer pricing laws are supposed to provide tax authorities the means of limiting, to economically reasonable levels, the amounts that companies can deduct for payments made to foreign affiliates. Chapter 3 will argue, however, that today’s arm’s-length transfer pricing rules contain obvious conceptual and technical anomalies that excessively limit their usefulness to tax authorities in many real-life tax audits. Chapter 3 will review the historical development of the OECD’s transfer pricing laws in an effort to pinpoint the political origin of those parts of the rules that are most problematic in the developing-country setting.

In addition to transfer pricing laws, Chapter 3 will explore other areas of tax law that are important to an understanding of base erosion and profit shifting. These include “controlled foreign corporation” rules, by which governments sometimes have sought to prevent their home-based multinationals from availing themselves of profit-shifting avoidance techniques in countries where the multinationals conduct business. In theory, CFC rules offer a means by which the home countries of multinationals could, by coordinating their legislation, effectively end BEPS-style avoidance by prohibiting their multinationals from participating in it. In fact, however, there has been little if any collaboration among capital-exporting governments to prevent their multinationals from engaging in tax avoidance around the world. Governments instead have feared that by

subjecting their home-based multinationals to effective CFC legislation, they might place those multinationals at a competitive disadvantage with respect to multinationals based in other countries, where effective CFC legislation is not in effect. As a result, although many countries maintain CFC rules on their statute books, the rules tend to be riddled with exceptions and other vulnerabilities, so that BEPS-style avoidance has been permitted to flourish despite the existence of these laws.

In its discussion of CFC rules, Chapter 3 will address a recently prominent variation on the CFC approach, the minimum tax on companies’ foreign income (the global intangible low-tax income, or “GILTI,” tax) that is included in recently enacted U.S. tax reform legislation. Chapter 3 will consider whether the enactment of the GILTI tax by the United States may trigger what amounts to an international revival of the CFC approach, which might to some extent reduce the pressures of international tax competition on lower-income countries.

Chapter 3 also will examine the remarkably permissive laws that for decades have permit companies operating around the world to deduct, from their taxable incomes, interest that they pay on obviously tax-motivated loans extended by zero- and low-tax affiliates. Chapter 3 will consider why historical attempts to control profit-shifting through interest payments generally have failed, and examines recent efforts by some countries – which during the BEPS process were endorsed by the OECD – to adopt more effective legislation to limit loan-based corporate tax avoidance.

Chapter 4 will build on Chapter 3’s examination of the legal and political foundations of base erosion and profit shifting by assessing the extent to which the OECD’s recent BEPS efforts offer practical promise for the curtailment of corporate profit-shifting from lower-income countries. I will argue that inevitably, the BEPS process was heavily affected by durable political pressures, from various quarters, to retain the historically evolved structure of international corporate tax law. The BEPS project has therefore refrained from recommending fundamental revisions to the legal principles that currently govern international corporate taxation. In

particular, in the BEPS reports, while the OECD has devoted considerable critical attention to the difficulties posed historically by “arm’s-length” transfer pricing laws, the BEPS recommendations leave some of the most important problems of current law unaddressed.

I nevertheless argue in Chapter 4 that the BEPS project has generated a number of policy recommendations that offer the prospect for significant improvement in the generation of corporate tax revenues in lower-income countries. First, in an effort to reduce profit-shifting through the payment of interest on loans from affiliates, the OECD has recommended that countries adopt rules disallowing interest deductions that exceed a specified percentage of the borrowing company’s net income. A number of relatively wealthy countries already have adopted limitations of this kind; they are relatively simple to administer and probably could lead to significant revenue gains in lower-income countries that are willing to adopt them. In addition, notwithstanding the BEPS reports’ hesitancy in addressing some central shortcomings of transfer pricing laws, I believe that plans of the OECD and other donor groups to provide technical assistance in simplifying the administration of transfer pricing rules – particularly the “transactional net margin method” under the existing OECD guidelines – offer some practical benefits for lower-income countries and should be pursued. Similarly, I argue, the plans of the OECD and other organizations to engage in “capacity building” in the area of transfer pricing administration, while limited in their potential effects by remaining deficiencies in underlying laws, nevertheless offer promise for net benefits in lower-income countries and should be pursued.

I argue as well in Chapter 4 that the OECD’s recommendations for improving the performance of international tax treaties offer limited, but still significant, potential benefits to lower-income countries.

Finally in Chapter 4, I consider the extent to which various developments related to but not part of the BEPS process might reduce demand for BEPS-style tax planning among multinational groups, thereby reducing the pressures of tax competition on lower-income countries. These

developments include growing concerns by multinational companies regarding the reputational effects of BEPS-style tax planning; actions within the European Union to limit member countries’ participation in tax planning structures; and the recently enacted GILTI tax in the United States, which may reduce U.S. groups’ tax benefits from overseas profit-shifting arrangements.

Chapter 5 seeks to build on the analysis of prior chapters by suggesting a program of potentially useful policy instruments for lower-income countries. My recommendations are based on the overall assessment (which I believe generally underlies the BEPS studies) that the problem of profit-shifting is extraordinarily complicated, politically as well as technically, and that meaningful progress against it is likely to arise from a combination of incremental legal reforms, rather than a “big fix” consisting of a fundamental re-design of the prevailing system of international tax laws. In accordance with this view, Chapter 5 will consider how countries might best implement the OECD’s recommended initiatives that will have been discussed in Chapter 4: (i) limitations on interest deductions; (ii) simplification of transfer pricing methods; (iii) capacity-building, mainly in the area of transfer-pricing enforcement; and (iv) the adjustment of national policies relating to income tax treaties.

In addition, Chapter 5 considers the potential benefits and limitations of the use, by additional countries, of an alternative corporate minimum tax (ACMT) applied at a low rate (for example, 1 percent) applied to a taxpayer’s gross revenue (turnover) rather than its net income. Because no deductions are allowed under a turnover-based tax, a turnover-based tax would be immune from avoidance through BEPS-style deductible payments of any kind, including not only royalties and service fees but also interest. Moreover, as will be explained in Chapter 5, a turnover-based ACMT also should be effective against tax planning based on the undervaluation of products shipped from a country, including natural-resource and agricultural products. Further, the relative simplicity of a minimum tax suggests that it might be well-suited to coordinated implementation among groups of

countries, thereby to some extent relieving pressures of tax competition.

Chapter 5 will conclude by offering brief comments on the taxation of some industries that often are of great importance to the economies of lower-income countries. These include natural resource extraction, electronic commerce, mobile telecommunications, and banking and insurance. There has been a great deal of specialized study of taxation of these industries, and this book cannot attempt to discuss them in detail. Nevertheless, Chapter 5 will offer a brief explanation of the special problems that taxation of these industries present, as well as ways that have been considered to alleviate these problems.

Chapter 6 will conclude this book with observations on the possibility of generating the political will, among the various interested actors, that will be needed to implement even limited measures to curtail profit shifting as it currently affects lower-income countries. Today's virtually universal use of BEPS-style tax planning among multinational companies reflects the operation over many decades of two mutually reinforcing kinds of competition: competition among countries to attract business investment, and competition among multinational businesses to minimize their tax burdens in countries where they operate. Together, these two kinds of competition have constrained corporate tax receipts in lower-income countries at levels that seem significantly lower than would be socially optimal.

In light of the persistence of both kinds of competition, it seems inevitable that meaningful

enhancements of corporate tax revenue in lower-income countries will require a supportive consensus among the major stakeholders in the global corporate tax system. These include businesses and business organizations, the national governments of both industrialized and developing countries, intergovernmental organizations like the OECD, IMF, World Bank, and United Nations, and regional associations of developing-country governments. What is needed is, essentially, an extension of the recent BEPS negotiations, but with a focus specifically on the needs of lower-income countries.

Chapter 6 will consider, from an ethical perspective, both the desirability of this kind of effort and the likelihood that support for it can be gathered from both the governmental and private-sector actors who would need to implement it. Does there exist a moral duty to assist lower-income countries in improving the performance of their corporate tax systems, even at the financial expense of both the governments of other countries and multinational companies themselves? Further, if a duty of this kind exists, who specifically bears the responsibility of seeking to implement it, and in what ways? No piece of writing, including this book, can pretend to answer questions like these definitively, or to all readers' satisfaction. Nevertheless, I hope that the observations offered in Chapter 6 will prove helpful to those who seek to build a pragmatic policy framework for improving the performance of corporate income taxation in lower-income countries. ■