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THE HEGEMONY OF INTERNATIONAL TAX REFORM

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Introduction

The economic viability of the developing world, particularly the poor economies of sub-Saharan Africa and the Caribbean, continues to escape the focus of the high-income countries of the developed world as they move forward with projects to ensure international cooperation to combat tax avoidance and to harmonize the standards for evaluating the substantive integrity of national regimes. The recent Base Erosion Profit Shifting (BEPS) project of the Organisation for Economic Cooperation and Development (OECD) has sought an overhaul of tax standards in a process that has given inadequate consideration to the particular concerns of the above-noted portion of the developing world (hereafter encompassed by the term "developing countries"). Action to include input from these nations was taken very near the end of the process, by providing an opportunity for consultation, but only after the paradigms, dictates, and core principles were adopted. Inclusiveness (a term used by the OECD itself)[2] at that late stage prevented any meaningful consideration of the significant issues facing this cohort.

The story of the OECD's development and construction of the BEPS initiatives is a replay of a dynamic manifested in environmental law. After decades of environmental degradation, and various interim accords, most nations convened in Paris in November, 2015, to prescribe goals and standards that would ensure future sustainability of the planet. These efforts followed years in which the developed nations built their economies by allowing production at home that polluted the environment or by allowing or even encouraging resident companies to shift production to poorer countries in search of the lower production costs available, in part, because of less stringent environmental regulation. In this light, it would have been inappropriate to assume that reform of standards would require that developing countries be subjected to the same requirements imposed on richer countries. To suggest that these countries take on similar compliance burdens when they had sacrificed their home environments to support production by multinationals from richer nations would seem unfair, given that this production seemed to have only reinforced the economic instability of the poorer hosts and increased the profits of the guests. Recognizing this dynamic, the UN meeting concluded with modified goals for the developing world that acknowledged capacity restraints as well as competitive disadvantages.

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Unfortunately, unlike the UN's Environmental Sustainability Project, the OECD's BEPS project of international tax reform did not significantly take note of either the competitive disadvantages faced by developing countries seeking to attract foreign capital or their diminished administrative capacity. The separate tax regimes of developed nations, including the U.S. and most OECD members, have led multinationals to exploit gaps which allow minimization of tax liability in their resident countries or shifting of profits to low-tax jurisdictions to escape or substantially reduce taxation. The ability to manipulate the disparate tax regimes to gain unintended benefits works to the disadvantage of developing countries because they tend to be pawns that in the end derive no economic advantages. For example, reliance on base-eroding techniques (such as earnings stripping or excessive payments of deductible items) and use of outdated source rules to artificially inflate foreign tax credits, enables multinationals to reduce tax liability (in the home and host country) without any significant investment in the developing country. These spillovers from the richer country regimes substantially affect the ability of the developing countries to attract investment that raises tax revenue sufficient to sustain their economies, support infrastructure, or develop a social safety network for citizens.

In developing prescriptions for tax reform, the OECD rejected an opportunity to focus on developing world needs when it foreclosed consideration of internationally-focused solutions to tax avoidance in favor of the prevailing separate country regimes. This removed the possibility of a meaningful role for developing countries in the design of strategies supporting revenue-raising and it even denied the developed world a chance to move toward a truly modern regime that could end the sophisticated tax-avoidance techniques employed by multinationals. Thus, the BEPS reform project launched by the OECD has served to shore up the separate tax regimes of the developed world and impose burdensome compliance measures without acknowledging the collateral consequences that effectively undermine efforts by developing countries to compete for much needed investment.

The vast needs of the developing world, especially after the great recession of 2008, underscore the urgency of allowing these countries a meaningful voice in international tax reform. Twenty-first century international tax reform has diminished power to conquer the challenges of the global marketplace when it ignores, minimizes, or undervalues the perspective and input of developing countries. The continued export of terrorism and the rising tide of political and economic refugees from these neglected areas of the world will shed a harsh light on efforts to ignore the importance of these nations to the economic and political stability of the remainder of the world.[3]

Part I of this article briefly examines efforts of the OECD, G20, and other dominant tax policy makers to promulgate international standards through the BEPS and other initiatives. Part II

[3] Jason Horowitz, Italian Spy Master Takes on Immigration Crisis, N.Y. Times Int'l Edition, Aug. 8, 2017 P. 2

weighs the benefits and burdens placed on developing countries by this wave of international tax reform. Part III considers multilateral proposals that take an international (as opposed to separate regime) approach to reform. The article concludes by considering international tax reform projects that take into account the needs of developing countries.

I.
Toward Internationally Accepted Standards

A brief survey of the evolution of international tax policy begins with the primacy of the capital export neutrality (CEN) principle,[4] protecting the tax base of high-income countries, like the United States, Canada, European Union members, and others. Those founding their regimes on the CEN principle proceed on the premise that multinational enterprises should locate economic activity in the region in which assets may be most productively employed. It has been the consensus of these, typically capital-exporting, countries that tax considerations (such as low tax rates) should not influence investment decisions. Application of CEN would result in application of the same tax rate to resident companies whether they operate at home or abroad. Some countries adopting this principle have a tax regime in which the worldwide income of residents is taxed by the home country and allow a credit against tax liability for taxes paid on profits from operations in foreign countries, known as the foreign tax credit. For example, the U.S. had until recently taxed certain high-income resident companies at a statutory flat rate of 35% on worldwide income, allowing a credit against U.S. tax liability for taxes paid to foreign countries on operations located abroad. Under such a system, a lower rate abroad (15%, for example) would not provide relief to the U.S. resident company because it would pay tax at the rate of 15% to the foreign country plus the 20% residual tax due the U.S. (35% minus 15% = 20%) after allowance of the credit.

Most of the so-called "capital exporting countries"[5] have adopted some variation of capital export neutrality as a governing principle in which the country of residence has the primary right to tax. One important exception has resulted, however, from the decision of most countries to allow some form of tax relief for foreign source income (income derived from business activity abroad). Before enactment of the 2017 Jobs and Tax Cut Act,[6] the U.S. allowed deferral of U.S. tax on active foreign source income of the wholly owned foreign subsidiaries of U.S. multinationals until the income was repatriated to the U.S. parent in the form of dividends or interest, dividends, royalties, or rental payments (or investment in U.S. property). Other countries have exempted foreign source income (but generally not passive investment income) from home country taxation by allowing various incarnations of a participation exemption. The

[4] Diminshed importance of these tax policy principles
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participation exemption provides for reduced taxation of certain income, usually dividends and sometimes interest, of foreign subsidiaries. In general, only 5% of the resident parent's dividend (or interest) income is subject to tax and the balance (95%) is excluded from taxation upon repatriation of these items to the resident parent. For residents of some countries, there is no tax at all on repatriated dividend income.

This departure from the application of CEN is typically described as adoption of the capital import neutrality (CIN) principle supporting the ability of resident companies to take advantage of the lower tax rates of certain foreign locales. Although it is a departure from CEN, which is premised on worldwide efficiency, CIN is typically defended as necessary to ensure competitiveness. Under CIN, resident companies operating in a foreign jurisdiction are able to lower their tax costs and enjoy the same advantage as locals and multinationals resident in countries that employ a "purer" form of CIN (often termed a "territorial tax regime") in which foreign source income is totally (or nearly) exempt from home country tax.[7]

Retaining remnants of a worldwide tax system, at the end of 2017, the U.S. Congress moved to a participation exemption that allows a one hundred percent deduction for foreign source dividends paid by U.S. corporate shareholders owning at least ten percent of the stock. At the same time, it reduced the tax rate on corporate income to a flat 21%. Anti-base eroding rules purport to provide a disincentive for U.S. multinationals to move offshore in search of lower-taxed income and limit the ability to reduce U.S. tax liability by stripping out deductible payments (reducing U.S. tax liability) to related parties resident in low-tax countries.[8] Statutory transfer pricing rules were adopted to curb certain practices allowing a shift of intangibles income offshore to related low-taxed parties.

The U.S. legislation is emblematic of the worldwide trend among developed countries to compete for investment from multinational enterprises through the "tax rate wars."[9] It also signals the end of a principled premise for tax regime design in favor of a self-centered grab for revenue while attempting to block competition.[10] CEN, CIN, and even the relatively new policy principle of capital ownership neutrality (CON)[11] have given way to an "every country for itself" approach that supports developed-world agency, but leaves no space for action by the developing world. Neither the recent U.S. tax reform initiatives nor international proposals take account of the ways in which such an approach operates to disadvantage these low-income

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[7] Dictated by capital ownership neutrality contribution/Reference to Avi-Yonah piece on Surrey and residence vs. source

[8] New §59A expands the old rules under §163(j), which limited stripping of interest only, to cover any deductible payment and depreciation deductions arising from acquisition of assets from a related foreign person.

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[10] GILTI, diverted profits tax (UK, Australia)

[11] Hines, Desai

nations which, now more than ever, have a critical need to find sustaining revenue for their economies. Economic development worldwide cannot be on a secure course when concern for the populations of these nations is shifted to the bare margins of tax policy deliberations. [Increase in worldwide GDP if women employed; developing world more productive?]

Failure to appreciate the ways in which healthy developing-world economies can advance worldwide achievement is not a recent phenomenon. Starting in the early days when nations were attempting to work together to determine ideal regime design, international cooperation amounted to a type of parenting when developing world interests were concerned. [complete source vs residence dichotomy, UN Model Convention for Developing Countries]

While there was no agreement dictating the contours of a tax base or the appropriate tax rate structure, countries began to work toward common rules relating to determination of the source of income derived by multinationals, the availability of the foreign tax credit, and procedures by which conflict could be mediated. This work, primarily supported by the League of Nations (and then the United Nations), was achieved through drafting of model tax treaties and negotiation of bilateral treaties country-to-country.[12] Creation of the OECD, in 1961, added a mechanism by which some nations could collaborate to create best practices (bilaterally and multilaterally) in the development of tax policies. Some of the work to elaborate collective standards has related to substantive rules, while other work has focused on procedural or administrative issues.

One of the major initiatives designed to promulgate common standards affecting substantive tax rules was the OECD's Harmful Tax Competition Report (HTCR), issued in 1998.[13] The HTCR criticized two types of tax regimes: 1) tax havens generally imposing no or nominal tax on income and 2) harmful tax regimes in which a country collects significant income tax revenue but its system has preferential features that subjects specified income to no or low taxation.[14] The OECD deemed these regimes harmful for several reasons. These included: distortion of investment flows, undermining integrity and fairness of tax systems, re-shaping desired level and mix of taxes and public spending, shift of tax burden to less mobile bases, and increase in administrative and compliance costs on tax authorities. Failure to condemn tax strategies which developed countries were using in their own regimes to compete,[15] signaled that the OECD's

[12] Michael Graetz article

[13] OECD, Harmful Tax Competition (1998) (hereafter "OECD, HTC"). Need to explore history here. Note Anti-Avoidance Report issued around the same time.

[14] OECD, HTC at

[15] Ireland, for example, a member of the OECD and the European Union, shifted to a 12.5% corporate income tax rate in a move designed to attract multinational businesses. In a compromise intended to appease members, the OECD blessed low tax-rate-type competition when built into the general tax scheme (i.e., the low-rate applied generally and was not limited to certain limited types of income (known as "ring-fencing"). OECD, HTC, at

real concern focused on regime-designed that allowed offending countries to attract investment from its members.

Developing countries appeared on the original so-called "black list," published by the OECD presumably in order to shame or bring notoriety, signaling that these countries failed to comply with generally accepted standards. Noting the absence of a role for developing countries in constructing international standards through the OECD, an inter-governmental organization with membership limited to high-income nations, the lists were decried by those outside the OECD as a patriarchal move to portray those listed in a bad light and in need of policing.[16]

The opprobrium resulting from assessment of country regimes as harmful (or not) led to complaints concerning the lack of participation by developing and other outsider countries in the initial construction of the standards and the expression of a preference for a focus on transparency through exchange of information. This led to the formation of a Global Forum, now comprising 139 member-nations, which focuses on assessment of transparency in tax administration and effective exchange of information in civil and criminal tax matters.[17] The standards used to review these tax systems is largely reflected in the OECD's Convention on Mutual Administrative Assistance in Tax Matters.[18] There is peer examination of the tax systems of Forum members, which accords a role to all member nations, expanded beyond the smaller OECD membership. According a voice late in the process to developing countries through membership in the Global Forum after standards had already been shaped by the OECD places into context the marginal input allowed developing countries.

Almost simultaneously with issuing the Harmful Competition Report, the OECD issued its Tax Sparing Report,[19] which condemned a practice by which many countries provided incentives for investment by their resident multinationals in developing countries. One version of tax sparing allows residents a credit against home country liability for fictional taxes on income derived in the developing country which is exempt in the source country because of tax holidays offered to certain classes of investors.[20] The OECD recommended an end to the practice of granting tax sparing credits for several reasons. Primarily, it felt that the grant of a tax sparing credit might unfairly compete with industries in the residence country (because moving operations to a host country with a zero tax rate and allowing a credit for the income derived against residence country tax would disadvantage residence country businesses subject to tax without benefit of a deemed foreign tax credit). It also contended that there was a likelihood that profits from

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17 Describe Phases of review.

18 This is based on a 2002 predecessor, the Model Agreement on Exchange of Information in Tax Matters.

19 Organisation for Economic Cooperation and Development, TAX SPARING (1998) (hereafter "OECD, Tax Sparing, at 10-11

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operations might be repatriated to a residence country that features a regime exempting foreign source income rather than re-invested in the host country.

The OECD cited several other reasons why the practice of granting tax sparing credits should be ended. Notably, however, it did not focus on the imbalance of power in the negotiation between the host country offering the tax holiday and the multinational resident in a developed country. This itself furnishes an important reason to question tax sparing, because of the dangers posed by the "race to the bottom" that may ensue if the multinational demands tax rate and other concessions that could harm the ability of the host developing country to protect an adequate revenue base or shore up other factors in the economy that could support sustainability (environment, worker rights, health care) efforts. Yet, by calling generally for reconsideration of the advisability of tax sparing credits without offering more, the OECD abdicated a duty to the developing world by failing to prescribe alternatives that could accommodate the developing world's need for revenue raising strategies. [21] Moreover, the contention that tax sparing was no longer needed because developing countries have become "economically much more sophisticated" and have reached an economic level "which is equivalent or superior to that of some [OECD] Member countries" fails to justify such a move concerning sub-Saharan or Caribbean countries which quite obviously did not hold a position of economic strength.

At the time the Report was issued, all but five OECD Member countries had tax sparing treaties with non-Members.[22] This number gradually eroded after the OECD's recommendation that members abrogate treaties allowing the practice.[23] Today, only a handful of countries, notably France, Germany, the Netherlands, and the UK, continue the practice.[24]

And Report recommendations placed developing countries in a tough spot. They were forced to fit their own regimes into a template, into which they had minimal input, which was

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[21] See, e.g., Karen B. Brown, Missing Africa: Should U.S. International Tax Rules Accommodate Investment in Developing Countries? 23 U. Penn J. Int'l Econ Law 45, 68-76 (recommending a treaty-based exemption system in lieu of a tax sparing credit for income derived from increased investment in sub-Saharan Africa with provision for environmental sustainability, worker rights, and sustainable tax rates).

[22] Only Iceland, Ireland, Portugal, Turkey and the U.S. had no tax-sparing treaties. OECD, Tax Sparing, at 68-69. The U.S. has never allowed tax sparing, although the U.S.-People's Republic of China does anticipate allowance of tax sparing credits, if they should be granted to any other country. The U.S. has firmly opposed grant of the credit.

[23] The OECD advised that the practice of granting tax sparing credits should be re-examined, with the Committee on Fiscal Affairs recommending that they should be granted only to "countries the economic level of which is considerably below that of […] member countries. The Report, however, caused countries to reconsider the practice even for needy countries. See, e.g., Kim Brooks, Tax Sparing: A Needed Incentive in Low-Income Countries or an Unnecessary Revenue Sacrifice? * Queens L. J. 505, 538 (Spring 2009) (noting that any benefit from attracting foreign investment are outweighed by the costs to the low-income country); Deborah Toaze, Tax Sparing: Good Intentions, Unintended Results, 49 Canadian Tax J. 879, 880 (indicating "tax sparing has produced only marginal economic benefits while providing opportunities for tax avoidance").

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constructed to accommodate the goals of the high-income members of the OECD. Some countries find themselves in the position of announcing acceptance of international standards, while surreptitiously doing what is necessary to attract investment even if those measures deviate from the enunciated standards.[25]

The most extensive push to develop international standards governing emerging issues in international taxation is the BEPS initiative directed by the OECD. This initiative gained momentum after meetings in 2012 led G-20 nations to recommend measures that would target a number of areas in which multinationals have gained unintended tax advantages simply by exploiting differences in countries' tax laws.[26] Areas of concern are wide-ranging and include targeting of schemes that use hybrid entities[27] to achieve double non-taxation of income, strengthening of controlled foreign corporation ("CFC") provisions to limit tax avoidance effected through off-shore subsidiaries, restricting rules allowing excessive interest deductions that erode the tax bases of residence countries of both the payer and payee, cracking down on treaty and transfer pricing abuses, and eliminating harmful tax practices.[28] The BEPS project resulted in a final report issued in 2015.[29] Connected with implementing these standards, in December, 2016, the OECD adopted a model Multilateral Instrument that will modify existing bilateral tax treaties in order to permit incorporation of many of the BEPS standards.[30]

The G-20 nations have adopted the BEPS plan, but they and other participating countries[31] are left to incorporate the proposals into their separate regimes. Implementation will require participating countries to shoulder a substantial compliance burden, including revision of internal statutory law as well as promulgation of streamlined procedures that will avoid the normally time-consuming treaty ratification procedures in place in most countries. Moreover,

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[25] See, e.g., Jalia Kangave, International Taxation: The Case of Uganda, in Taxation and Development: A Comparative Study (2017) (Karen B. Brown, editor) 280, 283 (The author notes Uganda's deference to OECD guidelines in documents and its commitment to taking steps to conform with internationally accepted tax practices, but acknowledges that "[w]hile there is no legal framework backing tax holidays, the government continues to provide them on an ad hoc basis."

[26] In particular, the OECD maintained that "[t]he current rules have revealed weaknesses that create opportunities for Base Erosion and Profit Shifting, thus requiring a bold move by policy makers to restore confidence in the system and ensure that profits are taxed where economic activities take place and value is created." OECD, BEPS Project Explanatory Statement (2015 Final Reports).

[27] Hybrid entities are those classified differently by two or more countries (e.g., an entity treated as a partnership by one and a corporation by another) with the result that the entity may pay no tax in any jurisdiction, often because of tax treaty advantages.

[28] There are 15 action areas. In its action plan, the G20 directed the OECD to develop items addressing "instances where interaction of different tax rules leads to double non-taxation or less than single taxation… [and] arrangements that achieve no or low taxation by shifting profits away from jurisdictions where the activities creating those profits take place." OECD, Action Plan on Base Erosion and Profit Shifting 10 (2013).

[29] OECD, Base Erosion Profit Shifting (October, 2015).

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[31] Need to define participating parties

because some of the proposals are controversial, implementation may not be uniform.[32] It is not easy to predict the number of additional countries that will sign on to the BEPS initiatives, in whatever form, but there is great deal of pressure on many, including developing countries, to conform.[33]

Many of the compromises made to achieve final reform recommendations reflect the participation in the negotiations by OECD members and efforts to accommodate their particular concerns. Yet, despite their involvement in the BEPS process, there is a question whether even OECD members will ultimately endorse every initiative. This is because the task of achieving consensus and conformity regarding so many complex core principles is gargantuan. The difficulty of finding agreement and buy-in is amplified considerably regarding non-OECD member countries. Non-members in the developed world have power to object to wholesale implementation, while poorer nations do not.

The past two decades have also witnessed a deluge of standard-making in the administrative arena, supplementing or even standing apart from the initiatives seeking to harmonize substantive law. In addition to the Mutual Administrative Assistance Convention, arising out of the HTC project, the U.S., the European Union, and the OECD have heightened requirements for record-keeping, information exchange, data collection, and administrative assistance. Among the most important of these have been the Foreign Account Tax Compliance Act ("FATCA") rules and the European Union-led Common Reporting Standards.[34]

The FATCA rules of primary focus in this article require financial institutions to disclose account information, obtain reliable documentation on the identity and whereabouts of the account holder, and withhold tax on payments received on behalf of U.S. taxpayers in the event appropriate documentation is not obtained.[35] Countries and their financial institutions were forced, as of the end of 2016,[36] to become "FATCA-compliant" in order to avoid the most serious consequence, which is inability to receive payments from U.S. banks and other non-bank financial institutions or entities (including those in which a U.S. person has an equity or debt interest)[37] free of the imposition of U.S. withholding tax. Compliance with FATCA also requires the automatic exchange of information regarding offshore financial accounts and assets of U.S. citizens and residents.

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[32] Not all countries are in agreement with all 15 action items

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[37] Richard Levine, Aaron Schumacher, and Shudan Zhou, A Comparison: FATCA and the Common Reporting Standard, 27 J. Int'l Taxation 42, 46 (2016) (hereafter "Levine, Schumacher, and Zhou, FATCA and CRS Comparison").

The FATCA accords did not occur without significant objection by other countries and their financial institutions. The particular concern was the unilateral “extraterritorial enforcement” of the U.S. tax law aimed at uncovering hidden assets of U.S. citizens and residents.[38] FATCA compliance was assured nonetheless because no foreign bank or non-bank financial institution could afford to lose a U.S. customer base, a result almost guaranteed if they did not comply with FATCA requirements, because U.S. banks would be forced to withhold on payments to these entities on behalf of U.S. customers or interest-holders. As of March, 2018, 113 countries were FATCA-compliant through entry into complex agreements with the U.S. Some of these agreements require the country in question to provide specified information to the IRS.[39] Others involve reporting directly by the foreign financial institution resident in these countries directly to the IRS.[40] These agreements have resulted from lengthy negotiations and place considerable burden on the signatories. So far Angola, South Africa, and many countries in the Caribbean region are considered FATCA-compliant.[41]

The OECD has developed a parallel information reporting regime, known as the Common Reporting Standard (“CRS”). CRS will eventually require the signatory nations to automatically exchange prescribed financial asset information. CRS signatories enter into Competent Authority Agreements like FATCA Intergovernmental Agreements (“IGAs”), but the CRS enforcement mechanism is different. With the absence of penalty measures like the ones available to the U.S. in the event of noncompliance, enforcement of the CAA will depend upon the internal laws of the respective parties to the agreement. As of January 1, 2018, ninety-six countries had committed to become or had become CRS signatories. Of these, nine developing countries had committed to agreements implementing CRS.[42] Notably absent from the group is the United States, which has indicated that it will not sign.[43] Perhaps because it was the first mover on the anti-tax evasion front, the U.S. is the one nonparticipant in CRS exempted from hardships resulting from non-signatory status.

In addition to agreements motivated by international reform initiatives, other bilateral and regional agreements place a burden of conformity on developing countries. These include Tax Information Exchange Agreements (TIEAs). Many countries have entered into these agreements mainly to facilitate transparency and information exchange. The U.S., for example, beefed up negotiation of TIEAs as a result of concerns that its tax treaties were being used for unintended

[38] Levine, Schumacher, and Zhou, FATCA and CRS Comparison, supra note 24
[39] These agreements are known as Model 1 Intergovernmental Agreements (“IGAs”).
[40] These agreements are known as Model 2 IGAs.
[41] Signers from the Caribbean region are Bahamas, Barbados, Bermuda, Cayman Islands, Dominica, Guyana, St. Kitts and Nevis, St. Vincent and Grenadines, Trinidad and Tobago, and Turks and Caicos.
[42] These are Antigua and Barbuda, Aruba, Bahamas, Barbados, Dominica, Ghana, St. Kitts and Nevis, Saint Martin, and Trinidad and Tobago.
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purposes by third-parties that had not participated in the negotiations. This practice became apparent in the 1990s phase of corporate inversions because the limitation of benefits provisions of comprehensive treaties like those with Barbados and Bermuda were used in connection with corporate expatriations to support stripping of earnings out of the U.S. tax base by deductible (for U.S. income tax purposes) payments that were tax-free to the newly formed parent corporation due to treaty concessions.[44] To the extent that countries hantered into comprehensive income tax conventions with developing countries, these have been criticized. While they purport to offer a benefit in the form of the alleviation of double taxation concerns, they have provided little actual incentive for investment by high-income country residents in low-income jurisdictions.[45]

II.
Burdens and Benefits

Reform proposals captured by the fifteen BEPS action items will fail to achieve the targeted mobilization against tax avoidance and manipulation if they are not accepted by the vast majority of countries, whether or not OECD members. Consequently, the OECD intends the BEPS initiatives to establish an international standard. Many of the reform prescriptions were designed with the intention of engaging so-called "third countries" (non-OECD/non-G20 nations) but are allowing input only after proposals were finalized or close to finalization.[46] Although it had no real power to bind any nation to a particular course of action, the launch of the Project in 2013 had the effect of coercing non-members to engage or react on terms not of their making.

The developing world's enthusiasm for an active role in shaping the BEPS prescriptions was evident in its demand that the Committee of Tax Experts of the United Nations ("U.N. Tax Committee") take the leadership role in charting the path. The goal was to construct a process open to worldwide approaches to taxation, such as those embodied in formulary apportionment, and similar, proposals, that seek to bridge the jurisdictional boundaries of the separate country regimes. This was the approach developing countries had in mind when they advocated for a World Tax Organization.

For years, developing countries, lacking a membership role in the OECD have urged the establishment of a World Tax Organization that would allow a broader-than-western view that would seek solutions to cross-border tax avoidance through profit shifting and other techniques

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[45] Tsilly Dagan

[46] OECD, Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance 68 (Action 5: 2015 Final Report) (2015) ("Action 5 of the BEPS Action Plan (OECD, 2013) explicitly recognised the need to involve third countries and requested the [Forum on Harmful Tax Practices] to develop a strategy to engage non-OECD/ non-G20 countries into the work on harmful tax practices.")

that consider the needs of all nations.[47] This work would have been taken up by the United Nations Committee of Experts on International Cooperation in Tax Matters ("U.N. Tax Committee"), upgraded to the status of an inter-governmental body. As an intergovernmental body, the U.N. Tax Committee, with expanded governmental representation and an adequate budget, would have been in a position to convene a "World Tax Organization," a significant counter-weight to the mostly western representatives of the OECD.[48] Under a World Tax Organization, the direction of tax reform might have questioned building the BEPS project to protect decisions made by OECD-members to support choices they had already made about the fundamentals of their own tax bases.[49]

This proposal to expand the U.N. Tax Committee was rejected at the United Nations Third International Conference on Financing and Development, held in Addis Ababa, in July, 2015, in large part because the OECD's BEPS project was underway.[50] The Conference concluded that the OECD-led process would adequately account for the concerns of developing nations. A few months later, in December, 2015, the OECD issued its final BEPS reports on the fifteen covered initiatives. The underlying premise of the final proposals for a global response to targeted types of tax avoidance (namely, exploiting gaps in different countries' tax systems that lead to non-taxation of income by any country and using various vehicles to shift income to low- or no-tax jurisdictions) was protection of the separate tax regimes of sovereign members of the OECD, the G20, and selected associates.[51] The final reports reflect an intention to involve developing nations in implementation of the initiatives, but this came long after fundamental steps to shape the project had been taken.

One of the critical issues concerning the direction of the BEPS Project, but foreclosed from consideration at an early stage, was whether tax avoidance could be better addressed by a global approach in the design of different countries' regimes. Harmonization or coordination of countries' substantive tax rules could occur in any number of ways, including one of the dominant proposals, formulary apportionment. To describe it simply, formulary apportionment

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[47] David Spencer, U.N. Tax Committee, Developing Countries, and Civil Society Organizations, 26 J. Int'l Taxation 44 (2015) (hereafter "D. Spencer, U.N. Tax Committee").
[48] Id.
[49] Id. (citing Mindy Herzfeld's observation that "[a]t the core, the concern by Western nations about upgrading the status of the U.N. Tax Committee may reflect the broader fear of the [U.S.] and the countries of the EU that as the agenda of international tax reform – and ultimately international tax rules more broadly – tilts from the West to the East, the historical system that generally favored residence or capital-exporting countries will also tilt to favor source countries." In Tax Analysts, May 2015).
[50] United Nations, Countries reach historic agreement to generate financing for new sustainable development agenda (Press Release, 15 July 2015) (The newly adopted Addis Ababa Action Agenda "calls for strengthening support for the work of the UN Committee of Experts on International Cooperation in Tax Matters to improve its effectiveness and operational capacity…").
[51] OECD, Action Plan on Base Erosion and Profit Shifting 9 (2015); OECD, OECD/G20 Base Erosion and Profit Shifting Project: BEPS Project Explanatory Statement (2015 Final Reports) 4 (2016).

would require all countries to agree to allocate the income of multinational enterprises under an agreed formula. The method proposed by Reuven Avi-Yonah, and others, is designed to eliminate the abilities of businesses to shift income across countries through legal and accounting techniques by allocating income on a worldwide basis.[52] The worldwide income derived by each business activity of a multinational group (based on the functions performed by the related parties) would be determined by subtracting worldwide expenses and allocating the net result based on a global accounting system among all countries in which the activity was conducted.[53] An estimated market return on tax-deductible expenses ("routine" income) would be allocated to the country in which the expenses were incurred and the remainder of the income ("residual" income) would be allocated based on the group's relative sales into each country.[54] While the proposal is not perfect, it aimed to address the ability of multinationals to artificially shift income and ownership of intangible property. This type of income manipulation occurs in transactions between multinationals resident in high-income countries, like the U.S., in transactions involving developing countries, a problem which current transfer pricing methodology has not been able to combat, particularly in natural resource mining.

While formulary apportionment may not be the final answer to the problem of international tax avoidance through income shifting, it provides an example of one of the worldwide approaches that would involve developing countries in the tax regime design process. Nevertheless, as early as 2013 when it formulated its action plan, the OECD noted that "there is consensus among governments that moving to a system of formulary apportionment of profits is not a viable way forward."[55] It did not note which governments had reached such a conclusion, nor did it detail the consequent failure to adopt a path that could seriously take developing country interests into account. Given its repeated emphasis on the necessity of buy-in by all countries to the BEPS initiatives, it is hard to understand why the OECD would relegate the input of developing countries to after-the-fact participation.

The OECD's failure to seek developing country input into the design of BEPS has caused it to miss an opportunity to guide a path to international tax reform that addresses the ability of developing countries to support sustainable economies. Although left with a peripheral role in tax design, developing countries are nonetheless expected to take on significant burdens to achieve a label of "compliant" with an increasing burden of standards that shore up the regimes of high-income countries.

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[52] Reuven Avi-Yonah, Kimberly A. Clausing, and Michael C. Durst, Allocating Business Profits for Tax Purposes: a Proposal to Adopt a Formulary Profit Split, 9 Fla. T. Rev. 497, 507-509 (2009).
[53] Id., at 508.
[54] Id. at 508-509.
[55] OECD, Action Plan on Base Erosion and Profit Shifting 14 (2013).

III.
BEPS Action Five and Harmful Tax Competition

The OECD opted to design the BEPS project without significant input by developing countries, but it committed to modifying the resulting initiatives in ways that would take into account the diminished capacity of these nations to implement many of the provisions. The burden of complying with constructing thin capitalization rules and transfer pricing standards that may not operate well with existing domestic law and the administrative burden of constructing country-by-country reporting rules, uncovering financial information of multinationals and administering a multilateral treaty instrument designed to supplement existing treaties is likely to work a hardship on resource-strapped low-income or medium-income countries. Other BEPS initiatives introduce standards that are incompatible with known interests of developing nations.

Action Five of the BEPS Project[56] relates to harmful tax practices and builds upon the work the OECD initiated when it issued the 1998 Harmful Tax Competition Report, described above. It targets all harmful tax regimes and is not limited, as in the case of the 1998 Report, solely to geographically mobile activities, such as financial and other service activities, and includes providing intangibles. Action Five indicates a resolve not to consider global tax design when the introduction notes that the initiative is “not intended to promote the harmonisation of income taxes or tax structures generally within or without the OECD.” While the report does not purport to “dictate to any country what would be the appropriate level of tax rates,” it has the effect of countenancing the competitive moves of many developed countries (including most recently, the U.S.) to compete by lowering tax rates in their separate regimes to attract foreign investment.

The common wisdom in recent years among developed countries, strapped for revenue after the great recession of 2008, appears to be that lowering corporate income tax rates attracts multinationals.[57] While Ireland was the first mover in the 1990s to a 12.5% maximum corporate income tax rate when most others were 30% or higher, other countries have countered with their own rate reductions.[58] The United Kingdom, Japan, Canada, and others have reduced their top statutory tax rates in recent years and the United States has moved to a 21% flat tax rate, down from the 35% maximum rate, as described above. This type of competition for investment does not violate Action Five principles because it classifies a tax regime as “harmful preferential” only if the rate reduction applies only to particular activities, often known as “ring-fenced” regimes. A rate much lower than that existing in other countries is not harmful so long as it applies generally to all corporate income.

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[56] OECD, OECD/G20 Base Erosion and Profit Shifting Project, Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance (Action 5: 2015 Final Report) 9, 15-16 (2015) (hereafter “Action Five”).
[57] Karen B. Brown, Taxation and Development – Overview, in Karen B. Brown (ed.), in TAXATION AND DEVELOPMENT (2017)
[58] CBO, International Comparisons of Corporate Income Tax Rates 2 (Summary Table 1) (2017).

This definition of harmful tax regime sanctions the tax rate competitive strategies of developed countries, but it does not address one of the major issues in developing countries -- the ability to offer tax incentives to foreign investors. The G20 Development Working Group, the OECD component charged with engaging with developing country issues, noted that, while the topic was outside of the BEPS mandate, the use of tax incentives was a top concern.[59]

Developing countries frequently find themselves pressured to offer incentives to attract foreign investment.[60] As noted above, one approach has been to offer a "tax holiday" to attract a given business activity of a multinational. An initial loss of revenue caused by a drastically reduced corporate income tax rate could be justified if the developing country obtains other advantages in return, such as employment of local workers and improvements to infrastructure, such as roads, schools, housing, and electricity or other utilities. There is a danger, however, that the grant of a tax holiday could lead to a "race to the bottom" in which developing countries are pressured to lower tax rates beyond sustainable levels due to competition from similarly situated countries and the greed of tax-cost-conscious multinationals concerned with the bottom line. The move of most high-income countries to a territorial tax regime enables resident multinationals to benefit from these incentives. If the home country will never tax earnings derived by a wholly owned foreign subsidiary, and freedom from taxation is not dependent upon compliance with minimum safeguards designed to protect the environment, health and working conditions for labor, and economic viability of the local economy, developing countries will continue to be pawns in the quest by multinationals to push rates as close to zero as possible. The pressure on developing countries to reduce tax rates or to provide multinational-friendly tax rules is one of the "spillovers" from the tax regimes of developed countries.[61]

When developing countries do seek to impose a significant tax on the extraction of valuable natural resources they possess. The example of mineral-rich developing countries in sub-Saharan Africa is instructive. These countries depend upon revenue from corporate income taxes imposed upon multinationals engaged in mining these natural resources in order to fund social, governance, transportation, power and other infrastructure needs essential to their constituents. One of the profit shifting techniques of these companies is to structure operations, including capitalization, so that excessive interest deductions are allocated to the higher-tax mining income and that interest is paid out to components of the group in low- or no-tax jurisdictions. While the developing country could strengthen its interest deduction rules

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[59] OECD, Part 1 of a Report to G20 Development Working Group on the Impact of BEPS in Low Income Countries 14 (2014).

[60] See, e.g., Jalia Kangave, International Taxation: The Case of Uganda, *in* TAXATION AND DEVELOPMENT – A COMPARATIVE STUDY 277, 283 (Karen B. Brown ed., 2017).

[61] International Monetary Fund, Spillovers in International Corporate Taxation: IMF Policy Paper 11-12 (The IMF defines a spillover as "the impact that one jurisdiction's tax rules or practices has on others." It notes the special importance of allocation of the rights to tax income to low-income countries as source countries and the "recipients of capital inflows," but not investors in business activities outside their borders. Because developed countries, as capital exporters, maintain the right to tax their resident multinationals, this may operate to the detriment of developing countries because these countries are not concerned with the 'fair' international allocation of tax revenue and powers across countries.

in an attempt to restrict this type of earnings stripping, the options presented under Action Four (Interest Deductibility) of the BEPS Final Reports are not easy to implement and they may not mesh with the income tax scheme in place. The multitude of acceptable regimes acknowledged in the report means that multinationals will be subject to a variety of rules in various jurisdictions,[62] and that developing countries may be susceptible to pressure to enact rules that are most favorable to existing industries. The OECD's decision not to adopt a global solution to apportioning income and deductions of multinationals serves as a missed opportunity to either enact rules that operate on a worldwide basis or to eliminate this type of manipulation by denying any interest deduction at all.[63]

Multinationals conducting mining activities in sub-Saharan Africa continue to use transfer pricing to shift income to lower-tax jurisdictions. In addition to using loans to finance exploration and development costs, these companies rely on transfer pricing techniques to lower profits when procuring machinery and support services from related parties and in sales of mined products to related parties.[64] Implementation of a common and less complicated rules, such as through adoption of formulary apportionment, would provide relief to developing countries. The absence of a legal structure to enact the complex transfer pricing rules promulgated by the OECD and the lack of an administrative structure (and auditors) to perform the audit and evaluation of the aggressive methodologies used by multinationals ensure that sub-Saharan nations will not be equipped to defeat this type of sophisticated tax planning.

[62] Lee A. Sheppard, BEPS Action 4 (Interest Deductibility), 80 Tax Notes Int'l 116,
[63] Id. at 118 ("The drafters of the final report went out of their way to preserve interest deductions for multinationals, missing the opportunity to attack the most widely used tool of tax planning with a straightforward disallowance rules.")
[64] Alexandra Readhead, Preventing Tax Base Erosion in Africa: A Regional Study of Transfer Pricing Challenges in the Mining Sector (Natural Resource Governance Institute, 2016).

IV.

(The Promise of) Tax Reform