Forum: General Assembly 5

Issue: Legal measures to reduce tax avoidance by transnational corporations

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Introduction

Since the emergence of systematically organized societies, taxation has been the cornerstone of all governmental functions. From medical care to military operations to public education, every state action is sourced through taxes. As per the social contract that binds responsibility among the state and its people, all citizens must pay their due taxes to the state—with which the state invests into various sectors for the benefit of all citizens. Taxes are an essential part of a country's source of funds to support infrastructure and many other positive externalities that the average citizen can take advantage of. Thus, they are essential to any functional society.

The manner by which a state taxes its citizens is left to the jurisdiction of the individual government. This was the case for many thousands of years. However, according to the United Nations Office on Drugs and Crime (UNODC), there are “three times more tax havens” now “than in the 1970s”—involving a total of over 7 trillion US Dollars. This rise in the number of transnational corporations (TNCs) has subsequently led to the rise of tax collection complications as business transactions occur across borders. Due to the existing ambiguities in international tax laws and the current inefficiency in cooperation between states in which TNCs operate, these businesses are able to legally slash their tax losses—or in some cases evade taxation entirely. As a result, nations worldwide are unable to acquire the necessary resources that are vital in supporting state organs for their citizens. Furthermore, because tax evasion is most effectively conducted across national borders, only large corporations are capable of orchestrating such feats. This prompts the furthered success and growth of existing large businesses, while suppressing smaller, local businesses—thus supporting monopolies on a global scale and promoting company acquisitions. In the end, the average citizen- people who are generally in the lower or middle classes- are hurt by the larger corporations evading or slashing taxes. The solution to this problem is to implement an international standard to which taxation can occur for businesses that work across many borders.

Due to the nature of the issue, this burden is placed upon the UNODC, which has devised the core of the international community’s devices against international. Another vital aspect of the struggle to securing taxes is the jurisdiction to indict TNCs for evading taxes. Since these corporations are operating among various different territories, each of which acts according to its own respective legislations, there is often confusion as a result of conflicting authorities. To this end, the UNODC has worked towards producing comprehensive guidelines to declutter inefficiencies.

In order to effectively achieve universal tax law compliance, all nations must reach a consensus on an international taxation standard. Taking into consideration that TNCs operate on a global scale, every nation plays the role of a stakeholder in this issue. For this reason, such an international standard must be established with the participation of all nations. If a single nation is excluded as a member state from the process, that nation will become a safe haven for TNCs seeking refuge from taxation—consequently compromising the efforts of the international community to curb such conduct. Therefore, any effort to this end must be planned and implemented unanimously.

However, such a global standard cannot be determined lightly due to the fact that each stakeholder has varying economic prosperity. For example, a More Economically Developed Country (MEDC) would have a different taxation rate as compared to that of a Less Economically Developed Country (LEDC). As such, a single international standard rate cannot be determined without certain countries being adversely affected. Yet this issue is prioritized by the United Nations in order to realize its millennium development goals. According to the United Nations Economic Commission for Latin America and the Caribbean (ECLAC), "Latin American countries lose more than 50 per cent of their income from taxes," - this has greatly impeded the United Nations' efforts to accomplish its Millennium Development Goals in all regions. Especially in developing countries, taxation is one of the crucial means by which they are able to generate resources for development. It is of paramount importance that MEDC's do not lose all economic incentives to invest in LEDC nations, but LEDC nations must also not purposefully drop tax rates on businesses to "attract" businesses from abroad through lower taxation.

Definition of Key Terms

Base Erosion and Profit Shifting (BEPS):

Tax evasion strategies that exploit varying tax laws in different nations in order to systematically shift profits to locations with low taxation rates, thus minimizing profit losses as a result of taxation.

Transfer Pricing

The maneuvering of production costs and profits among different departments of a company with the purpose of manipulating the profit margins of individual departments. Such allocation is typically employed with each departments being situated in different locations with varying taxation rates.

Tax Base

The margin of income to which taxation laws are applicable for collection. Typically, taxation laws are applied at set rates comparative to one's profit margin—so as to tap into successful businesses while supporting weaker ones. The larger the collective pool of tax bases in a nation is, the more resources there are for governments to secure.

United Nations Millennium Development Goals:

The United Nations set eight milestones in global development to be achieved by the year 2015. Such goals include: universal education, eradication of hunger, and global partnership for development. Although the deadline for these goals has elapsed, the UN has continued to push for post-term progress for the agenda through the Sustainable Development Goals (SDGs)

Double Taxation

The levying of taxes on the same income by two different countries. Double taxation can occur as a result of transnational transactions.

Tax Haven

A country where taxes are levied at considerably low rates relative to others. Tax havens are the prime grounds for tax inversions to transpire.

Background Information

International tax evasions committed by TNCs are becoming the center of discussion for the international community as more whistleblowers are stepping up and shedding light on the severity of the issue. Investigations lead by United Nations human rights, such as former UN official Alfred-Maurice de Zayas, have revealed that trillions of dollars are being safeguarded from the tax laws of governments in foreign bank accounts—resources that are essential for the combatting poverty, climate change, and all other pressing areas in need of development. The trillions of dollars that are being lost, laundered, or converted are trillions of dollars that would have otherwise gone to a country's government to support programs for education, healthcare or other public services.

Tax Havens Incentives

Despite the truth that tax havens result in businesses being allowed to maintain their wealth by paying less to governments, these tax havens exist due to the benefits these nations gain from the influx of businesses. The tax haven nations, although they levy taxes at a substantially low rate, ultimately gain more resources due to the large amount of tax bases they have available. These LEDCs have very limited sources of income due to the lack of infrastructure and variety in their economy. Yet by lowering their national tax rates, they are able to appeal to foreign businesses to base their company's operations within their nation—thus allowing them to be taxed. In addition to the obvious benefit of overall reduced tax payouts, TNCs benefit from the perks of total anonymity.

Since MEDCs are unable to benefit from the schemes of TNCs operating abroad, many attempt to track down these hidden funds and levy their respective taxes in order to lay their rightful claim to a share of the wealth. Thus in order to protect their newfound sources of income, tax havens makes it illegal in their nations to disclose any information about the workings or identities of TNCs operating within the nation. As a result, tax havens continue to reap the benefits of wide tax bases, while TNCs continue to evade taxes and sustain their wealth. From an economic perspective, it makes sense that LEDC's would want to attract foreign businesses to increase their own gross domestic products, and in a way, a country's tax policies are an issue that falls within the sovereignty of every individual state. However, MEDC's obviously do not benefit from such policies.

Logically, we would want LEDCs and their economies to take this opportunity to flourish into more economically sustainable and developed countries, but this presents a new problem: companies that used to pay billions or trillions of dollars in taxes move out to foreign countries and are no longer subject to the taxation laws in their host nations, and that money is lost for the host nation. Take a nation like the United States for example. The average rate of tax for businesses falls between 30% to 40% depending on the State. A federal tax is instated on top of an original state tax, amounting to a percentage that is the third highest in the world. In a nation where new businesses arise every year in the millions and statistically, many fall due to the fact that they cannot move forward with production due to hefty taxation. Of course, a country like Vietnam now seems a lot more attractive to the average American business owner, as the average corporate tax (excluding precious mineral businesses) is 25%. There are many other third-world countries that have corporate tax rates lower than 20%. In the year 2016, the US Treasury Department also introduced a third set of guidelines to try and stop multinationals from evading taxes, but these guidelines are still a controversy within the United States Senate and a feasible bill is far from being drafted, much less enacted upon by Congress.

Consequences of Tax Havens

Although the governments of countries that become tax havens do benefit from the sheer scale of the amassed resources from TNCs, their economies are left undeveloped. This would be a common misconception. Regardless of whether there are resources flowing into the country, the businesses native to the country suffer tremendously. This is because the TNCs establish a monopoly in the local economy. Native businesses are unable to compete against the powerful global corporations and are forced to go out of business. Native workers are deprived of high-paying occupations and are left with low-paying labor work. As LEDCs become more and more dependent on TNCs for their income, their economy falls into a quagmire of counterproductive trade. Economically speaking, trade is supposed to be beneficial to both nations in terms of producing goods with lower opportunity costs. In the case of corporations from MEDC nations coming in to local economies for LEDC nations, many times the trade balance between two countries is upset greatly. This means that there is no productive trade going on in terms of the economy, in addition to an uneven balance of trade occurring. Most MEDC's are not lacking the resources present in LEDC nations (with the exception of oil). The corporations do not have a country's interests in mind, only profit, as all businesses do. Although the profit incentive is indeed at the heart of capitalism itself, governments cannot allow the profit incentive to overtake the international relations and the policies therewith regarding two or more nations.

Importance of transparency

It is the right of every nation to establish its own respective laws and is a point that the United Nations cannot infringe upon. However, the issue of tax avoidance is not solely reliant on whether or not these tax havens are willing to abandon their heavy dependence on TNCs, but also their willingness to disclose information regarding their operations. The aforementioned benefit that these foreign companies enjoy allows them to operate in a manner that is entirely shrouded from the eyes of the international community. The pressing issue of tax avoidance cannot be addressed if such activity cannot be identified or monitored in the first place. Thus, there lies a heavy importance on the transparency of TNC activity in tax havens. In locations where such activity is shrouded under the protection of the law, whistleblowers are the sole light the international community has to identify such illicit conduct.

However, do to the commonly passed laws which punish such conduct, the truth is often buried behind borders. It is important to recognize that LEDCs have very little incentive in the short-run to expo se or reveal that certain businesses are indeed committing acts of tax evasion or otherwise. In the short-run, the businesses will indeed provide a decent source of taxation for the LEDC nation. But as with all good sustainable development, we must look at the picture in the long run. You cannot simply plant a few multinational companies in the middle of Burma and expect them to help the economy thrive in 30 or 40 years. Dependence comes quick, as LEDCs use the extra funds from taxes to build infrastructure and expand public services. But there has to be sustainability. If a road or bridge breaks down, there has to be enough money to fix it, in addition to the construction or urbanization of other rural areas. It is critical to note that businesses are volatile in nature, (thus why stocks are unpredictable at best) and reliance is a dangerous road to go down.

Take for instance the company of Nokia. If Nokia had become a major contributor to taxes in Egypt, even at low rates such as 13%, it would involve drawing in millions of dollars. Nokia essentially disappeared from the smartphone market in 2012, when Apple and Samsung really started hitting the innovative sweet spots in smartphone technology. Nokia stock prices plummeted, as most children born past its will not even recognize its name. The country of Egypt would now have a deficit in the millions of dollars. The unreliability factor of businesses in the long run must be taken into account when building resolutions and putting forth potential ideas to fix this issue.

Furthermore, the UNODC has repeatedly underscored the importance of transparency in the struggle against TNC tax evasion. One such recent action is the initiation of project Strengthening criminal investigation and criminal justice along the Cocaine Route in Latin America, the Caribbean and Western Africa (CRIMJUST), which seeks to facilitate cooperation in the investigation of international crimes across several regions.

Major Countries and Organizations Involved

The United Nations Economic and Social Council (ECOSOC)

ECOSOC is the primary UN body for addressing global economic issues, such as tax avoidance by TNCs. The committee has already convened numerous discussions on the matter and has developed a number of resolutions to work towards establishing an international standard of conduct regarding the matter.

The United Nations Committee of Experts on International Cooperation in Tax Matters

The United Nations Committee of Experts on International Cooperation in Tax Matters is a subsidiary body to ECOSOC. It is the primary instrument charged with specifically addressing issues related to the levying of taxes internationally. Its responsibilities include the convening, reviewing, and updating of the United Nations Model Double Taxation Convention.

Bermuda

According to Oxfam International, an international charity with the purpose of combating world hunger, Bermuda is ranked as the world's worst tax haven. With a 0% tax rate being levied onto TNCs, the nation is the host of numerous offshore bank accounts and hidden funds. The reason for its nonexistent tax rate is realized by the substantially high living and operating costs, which slightly offsets its benefits for foreign businesses, but is heavily outweighed by the clear appeal.

Panama

In May of 2017, financial documentations of a large panama-based law firm was leaked—revealing the involvement of numerous other businesses and high-ranking political figures. This scandal has placed Panama on the radars of various organizations, such as Transparency International (TI) and the UNODC, as a potentially potent tax haven. Furthermore the controversy has stirred people to call for increased monitoring of financial institutions in Panama, as well as stronger legal reformations to grant the capacity to deliver swift and meaningful punishment to anyone found guilty of tax fraud.

United Nations Office on Drugs and Crime (UNODC)

The United Nations Office on Drugs and Crime is the primary UN body charged with handling issues pertaining to illicit drug trafficking and fighting international crime. In regards to the agenda at hand, the UNODC is responsible for establishing the framework by which transnational tax avoidance cases are defined and handled. The UNODC has collaborated with the World Bank in the launch of its Stolen Assets Recovery Plan (StAR). This initiative aims to aid developing countries in the recovery of lost resources and reallocating them towards funding development programs.

Timeline of Events

Date	Description of Event
1979	Manual for the Negotiation of Bilateral Tax Treaties between Developed and Developing Countries was passed

1980	United Nations Model Double Taxation Convention between Developed and Developing Countries was passed
1990s	Ad Hoc Group of Experts on International Cooperation in Tax Matters recognized significant changes in international economics—such as new transfer pricing methods and online banking—and began reviewing and revising previous guidelines.
August, 2001	Revised Version of the Manual for the Negotiation of Bilateral Tax Treaties between Developed and Developing Countries; the original manual was revised in light of more aggressive tax havens emerging as a result of technological advancements in the financing sectors.
September 8, 2000	United Nations Millennium Summit; All member states at the time—191 countries—determined eight international development goals to be achieved by the year 2015.
June, 2015	United Nations Handbook on Selected Issues in Protecting the Tax Base of Developing Countries; United Nations Department of Economic and Social Affairs developed internationally standard guidelines for the international community to uphold in order to effectively address the issue of tax avoidance.

Relevant UN Treaties and Events

- United Nations Convention against Transorganised Crime, 8 January 2001, (A/RES/55/25)

ECOSOC Resolutions regarding international tax cooperation standards:

- ECOSOC Resolution (E/RES/2004/69)
- ECOSOC Resolution (E/RES/2006/48)
- ECOSOC Resolution (E/RES/2007/39)
- ECOSOC Resolution (E/RES/2008/16)
- ECOSOC Resolution (E/RES/2011/23)
- ECOSOC Resolution (E/RES/2017/3)

Previous Attempts to solve the Issue

Since the turn of the century, the ECOSOC has drafted twenty three resolutions regarding the issue of tax avoidance. Each reinforces the previous with updated, more specific guidelines on how the international community should address the issue. However, the problem persists and remains at large due to the legality of TNCs' activity. The United Nations lacks the authority to infringe upon a nation's sovereignty in regards to its taxation rates and laws, and therefore can merely suggest actions to be taken. However this has proven to have little effect as these tax haven nations have grown extremely dependent on the income of TNCs and would collapse without them.

Progress has been noted in cases where a whistleblower discloses information about the offshore funds hidden away by TNCs. Unfortunately, these cases are very rare because of the strict laws that have been put in place by many LEDCs to discourage such conduct. The compromise of anonymity for TNCs could result in the business's relocation to other tax havens which are more than willing to provide sanctuary and turn a blind eye in exchange for their resources.

Notably, the UNODC formulated the first legal instrument purposed with combatting transnational organized crimes. The UNTOC empowered the international community with the ability to efficiently forward jurisdiction from one state to another, as organized crimes attempt to evade authorities by shifting borders. As a result of the UNODC's efforts, the international community was able to indict the known tax avoidances committed by countless TNCs. However, due to the aforementioned lack of transparency enjoyed by TNCs under the sanctuary of tax havens, many corporations are left formally acquitted.

Possible Solutions

Possible solutions could include the establishment of an international body with the purpose of discussing and the authority of establishing international standards regarding tax rates including: tax rates, double taxation, and taxation transparency. Such a committee would require the unanimous participation of every nation as any solution is rendered completely ineffective with the existence of even a single tax haven. The World Bank and other organizations such as transparency international can also become involved in this process. The creation of an ad-hoc committee to deal with the issue of international taxation and the laws therewith is recommended.

Furthermore, all nations must have a voice in this committee regardless of their current economic standings. As evident in previous attempts to convene similar discussion, MEDCs and LEDCs hold drastically different stances regarding what action the international community should take in addressing the matter. However, this solution is limited by the fact that it requires immense trust by all involved parties to act in conformity with the established guidelines. Additionally, it would require some nations to yield some economic power out of goodwill. In concession of the unlikeliness of this outcome, further incentives and reasons must be suggested in order for all nations to reach a consensus.

Another interesting approach for MEDC nations to take is to place stricter regulations on companies themselves in exchange for lowering the tax rates. It is a Nash equilibrium situation that should increase the number of companies that will pay their taxes instead of seeking ways to avoid it. The first step is to lower the corporate taxes (if they are ludicrously high in countries such as the United States or the United Arab Emirates). This will firstly take the financial burden off of companies. Making tax brackets bigger at the lower levels of profit instead of just making them lower at higher levels will help smaller business grow and feel less of a financial burden on themselves. This is the first "win" situation in place for businesses. For governments, this means that there will be need for less money for lawsuits, as well as an increase in the number of companies that will pay taxes without trying to flee to other countries in order to evade doing so.

LEDC's should also set or agree to a minimum corporate tax rate so that they do not compete to have lower and lower tax rates for multinational corporations. Setting this tax floor will disincentivize LEDCs from continuously lowering their tax rates, and should create a slow in the lowering of corporate tax rates around the world. This will also push for LEDCs to compete in more economically beneficial ways, such as having safer public environments or having better infrastructure to make companies feel like their country is best for their workers, not just profits.

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Appendix or Appendices

http://www.un.org/en/databases/index.html

- United Nations portal with links to archived official documents, resolutions, conferences, reports.