AUCMUN

INDEX - ECOSOC'S STUDY GUIDE

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Topic A: The adaptation of a global minimum corporate tax to discourage tax avoidance

"This is more than just a tax deal, it's a reshaping of the rules of the global economy," (The Guardian)

Welcome letter

Distinguished delegates of the Economic and Social Committee,

We are honored to welcome you to join the Economic and Social Committee, and aim to build with you an enriching and fruitful debate.

The Covid-19 pandemic has changed the international relations field forever. Higher collaboration between states has proven to be key to the wellbeing of the citizens. Furthering this trend some administrations have proposed to apply a common corporate tax in order to lower the amount of tax avoidance that is harming the states.

Major changes have affected the economic and social situation that the world is in right now. In this committee, we aim to discuss the effects of these changes and plan the best changes for a bright future.

Now we will proceed to introduce the chairpersons board for this committee:

Cèlia is a third year student of audiovisual and mathematical engineering at Universitat Pompeu Fabra. She participated in her first MUN when she was in high school and joined UNSA Barcelona in 2019 in her first year of University. She is especially interested in women rights, cybersecurity, access to healthcare and egalitarianism. She is excited to participate in AUCMUN as a chair, as she thinks that MUNs are a great way to implicate the youth in international politics and human rights. She believes that tax justice is key in order to guarantee that the human rights prevail.

Diego is a second-year Governance, Economics and Development student at Leiden University College in The Hague. He is a very passionate and open individual, and the field of economics has a special place in his heart. He also has tremendous love for Latino music and a borderline obsession for Real Madrid, he is your go-to person for random facts about anything. Moreover, while serving as one of the chairs of ECOSOC at AUCMUN 2022, his goal is to ensure that as many delegates as possible can have an enjoyable time at the conference, while creating life-long friendships in the process. As an Econ fanatic, taxation is definitely one of his favourite topics to bring up in casual conversations, so he is thrilled by the opportunity to chair at ECOSOC this year.

Introduction to the committee

The United Nations (UN) charter established the Economic and Social Council as one of the main six organs of the UN, its founding can be traced to the United Nations Charter article 61 to 72. This institution is the leading intergovernmental institution to achieve development in the economic, social and environmental realms. It has fifteen specialized agencies, eight functional commissions and five regional commissions under its jurisdiction.

It is made of 54 rotating members and more than 1600 non-governmental institutions with observer status.

As soon as the UN was created as a result of the international disaster caused by the second world war, ECOSOC focused on the reconstruction of the countries most damaged by war: Western Europe and Japan.
In the 1960s the ECOSOC committee focused on the decolonization process and the unequal distribution of resources between the South and the North.
In the 1980s the approach of ECOSOC changed to tackle the issues that arise with globalization.
In our current times, ECOSOC started to have a bigger role on the peacebuilding missions as it understood the correlation of social and economic issues with human rights.

This Commission has gone through several reforms since its establishment in 1945. The most important ones are:

- The 2005 Reform: ECOSOC is now established as a platform for high level engagement between UN member states and the international financial sector, the private sector and civil society. The start of annual revisions upon development goals, especially the Millennium Development Goals.
- The 2013 reform: UNGA resolution 68/1 passes, strengthening the role of ECOSOC in the identification of future challenges, pushing innovation and being a main actor in the development of economic, social and environmental sustainable development.

Concepts

The tax gap describes how much tax should have been raised in relation to how much tax is actually raised. Can be caused by mainly two factors:

- lack of enforcement by law
- lack of compliance due to the high cost of bureaucracy

MNEs: multinational enterprises (MNEs)
BEPS=Base Erosion and Profit Shifting-> shift profits from higher-tax jurisdictions to lower-tax justisdictions, thus “eroding” the “tax-base” of the higher-tax jurisdictions.
CIT= Corporate Income Tax

History

a. General history about corporate taxation

This is the era of **multinational corporations**. Today, there are many companies that are more powerful as compared to entire nations. The following example (Figure 1), clearly shows how Microsoft’s market cap is higher than most countries’ real GDP! Only a handful of countries, such as the United States, France or Italy, can pride themselves over a higher real GDP than Microsoft’s market cap. Therefore, sometimes to hold back an MNE’s power, countries decide to impose corporate taxes that are relative to the company’s net income. However, corporations do not look favourably upon corporate taxes. Nonetheless, they still have to pay their share in most parts of the world. Additionally, most people believe that taxing corporations, within reasonable limits, is fair and contributes to a just system.

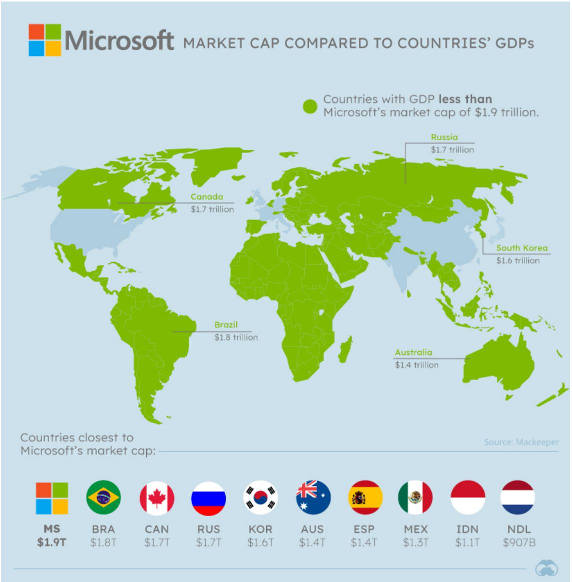

Figure 1: Microsoft's market cap (Wallach, 2021)

The history behind corporate taxation, dates back to a long time ago, and one can see its progress through the following timeline:

1-. The United States first introduced the corporate tax in the year 1894. However, the tax was not taken well by American corporations, who immediately challenged it in court. The tax could not sustain for very long and was repealed within one year since it was found to be unconstitutional. (Juneja, 2022)

2-. The corporate tax was reintroduced in the year 1913. However, this time the legislators were careful. Hence, they kept the tax rate abysmally low at 1%. This continued for some time. However, the government slowly started raising tax rates over time. Within a decade, the tax rate has grown to 15%! This was commendable given the fact that the American public has generally been averse to any form of taxation. (Juneja, 2022)

3-. The corporate tax rate in America saw a major jump during the World War 2 period. During this period, the tax rates rose sharply and remained high till the 1960s. This was a period when national security was a priority for the American government. Hence, people agreed to higher rates of taxation. During this period, corporate taxes were the single highest contributor to the American budget. Corporate taxes contributed close to 20% of the total revenue of the United States government. This is the period when the American tax rate had peaked. The tax rate was highest in 1968 when it was over 50%! (Juneja, 2022)

4-. The corporate taxes in developed nations was then reduced. For the most part, America was charging tax rates between 30% and 40%. This was also the case with all other developed western economies. In fact, the tax history of most developed western economies is remarkably similar. They were generally charging taxes between 30% and 45%. Germany was the only other developed western nation where the peak tax rate for corporations was below 40%. Till 2018, the total corporate tax collected in America had reduced to 9.9% of the total revenues and accounted for 2.2% of the gross domestic product. (Juneja, 2022)

5-. Meanwhile, other developing nations, where countries were choosing to relocate, had tax rates that were closer to 20%. (Juneja, 2022)

b. The history behind the global minimum corporate tax

"The fight against BEPS was said to be important as BEPS opportunities not only threatened the integrity of the corporate income tax (hereinafter, CIT) by creating unintended competitive advantages and distorting investment decisions (raising, therefore, fairness and efficiency issues, respectively), but, most importantly, also damaged voluntary tax compliance systems, for all taxpayers, including individuals." (Sacchi, 2020)

With the Globalization Process that started the last century the economies of different sections of the world became interdependent. Previous advantages and disadvantages along with the ability of the country to take advantage of the current situation have resulted in a highly unequal world.

In 1968 Nobel prize winner Gary Becker theorized about the economics of crime and the models of tax evasion. He concluded that the levels of tax evasion were directly proportional to the detection probability and the punishment by law. In recent studies it has also been shown that when companies or individuals are more knowledgeable about the use of the taxes they are less likely to commit fraud. This problem would then take a long time until the first proposal for a global corporate income tax.

The history of corporate income tax as such begins in 1992. In 1992 a minimum corporate tax rate was proposed on a regional scale for the European Union member states. The proposal was made by the Ruding Committee in 1992, a European Commission expert panel led by Onno Ruding. The committee's proposal, of a 30% minimum tax, was however not implemented. (Wier, 2020)

“The BEPS project, promoted by the G20, was launched by the OECD in 2013, with the objective of countering certain structures and arrangements being exploited by multinational enterprises (hereinafter, MNEs) to eliminate or significantly reduce their global tax burden in a manner inconsistent with the tax policy objectives of existing international tax standards.” (Sacchi, 2020)

Then, in January 2019 the OECD formed a group called Inclusive Framework that has since been exploring a minimum tax rate among its member states. Since January of 2019, the Inclusive Framework issued the Policy Note on Adressing the Tax Challenges of the Digitalisation of the Economy. Two pillars were agreed:

A first pillar **Pillar One** which it is said to treat with the **tax challenges derived from the digitalization of the economy**, beyond BEPS, focuses on revisiting profit allocation and nexus rules, and therefore, may derive in an international reallocation of taxing rights.

Pillar Two: The Global Anti-Base Erosion (GloBE) proposal

Meanwhile, a second pillar, **Pillar Two**, and the focus of the present chapter, is supposed to deal with BEPS “remaining” issues. In effect, it is considered that the initial measures recommended under the BEPS action plan, either already implemented or in the way of being so, have left unresolved some BEPS issues.

“Pilar Two sets out what has been named “the GloBE proposal” which, as mentioned, intends to address remaining BEPS risks by representing “a systematic solution designed to ensure that all internationally operating businesses pay a minimum level of tax”.” (Sacchi, 2020)

This proposal aims to set rules that address the ongoing risk from structures that allow MNEs to shift to jurisdictions where they are under very low taxation.

There are three main technical designs present in GloBE:

A. The use of financial accounts to determine the tax base under GloBE proposals and solutions to address the time difference.
B. The extent to which MNEs will be able to mix high-tax and low-tax income taxes and determine the effects on the resulting tax rate.
C. Stakeholders experience that might be relevant.

There are 4 main GloBE proposals, which are:

1. an income inclusion role: it would tax the income of a foreign branch or entity if such income was subjected to a tax below the minimum rate.
2. undertax payment rule: operating by denial of a deduction or an imposition source-based taxation for a payment to a related party of the payment was not subjected to a tax above the minimum rate
3. switch over rule:permit a residence jurisdiction to switch from an exemption to a credit method where the profits attributable to a permanent establishment (PE) or derived from immovable property (which is not part of a PE) are subject to an effective rate below the minimum rate;
4. subject to tax rule: complement the undertaxed payment rule by subjecting a payment to withholding or other taxes at source and adjusting eligibility for treaty benefits on certain items of income where the payment is not subject to tax at a minimum rate

Current Situation

The OECD, which has steered the negotiations, estimates the minimum tax will generate $150 billion in additional global tax revenues annually. Taxing rights on more than $125 billion of profit will be additionally shifted to the countries where they are earned from the low tax countries where they are currently booked. Economists expect that this global minimum tax rate deal will encourage multinationals to repatriate capital to their country of headquarters, giving a boost to those economies. However, various deductions and exceptions baked into the deal are at the same time designed to limit the impact on low tax countries like Ireland, where many U.S. groups base their European operations. In october 2021 the finance minister of the G20 endorsed the measure of establishing the minimum corporate tax at 15%. Nonetheless, questions remain about the U.S. position which hangs in part on a domestic tax reform the Biden administration wants to push through the U.S. Congress.
The agreement calls for countries to bring it into law in 2022 so that it can take effect by 2023, an extremely tight timeframe given that previous international tax deals took years to implement.

“However, in most cases, it is also fair to recognise that these MNEs were benefiting from disparities between national tax systems and of, both, outdated domestic legislation and international standards, not breaching, strictly speaking, any statutory rule.” (Sacchi, 2020)

In January 2019, the Inclusive Framework issued a Policy Note on Addressing the Tax Challenges of the Digitalisation of the Economy.1 Under this Policy Note, the Inclusive Framework agreed, on a without prejudice basis, to undertake work on the following two pillars:

“The OECD/G20 Inclusive Framework on BEPS (hereinafter, IF) has been working on addressing direct tax challenges derived from the digitalization of the economy under a two-pillar approach: Pillar One deals with the international allocation of taxing rights while Pillar Two, with “remaining/unresolved” base erosion and profit shifting (hereinafter, BEPS) issues.” (Andrea Riccardi) “Establishing a programme of work on a “without prejudice” basis, compromising to find a global consensus based solution by the end of 2020.“

Bloc Positions

Over 136 countries have signed the global minimum tax rate of 15%, these countries represent 90% of the global economy. There are Kenya, Nigeria, Pakistan, and Sri Lanka that have not yet signed the agreement but are included in the negotiations

Ireland, Estonia, and Hungary all recently gave their approval after initially staying out of the agreement in July 2021.

Western Nations

Within the most developed countries in the world there are many different takes when it comes to the best taxation rates.

European Union

After the Covid 19 pandemic there was a shift in the economic policies established by the EU. In 2008 the wealthiest eu countries implemented an aggressively austere politics in order to tackle the financial crisis.

The agreemest discussed in this SG is complementary to the EU own tax agenda.

United States of America

"The USA wants to raise its corporate tax rates from 21% to 28%, they fear that such a move will lead to large-scale profit shifting by US multinationals to low-tax jurisdictions like Ireland, with rates as low as 12.5%, and that a minimum global corporate tax rate will prevent such a shifting. Tax avoidance by high-tech companies has been a concern for a long in the US, where the top multinationals avoid taxes by shifting profits to low-tax jurisdictions." (Helmore, 2021)

Biden deal:
"The Biden administration had sought a 21% corporate tax rate floor but a 15% rate still represents a win for the US heading into next week's COP26 climate conference in Glasgow in 2021. It sets a minimum rate of 15% on the profits of large businesses, which will raise additional revenue for most governments and shift the tax burden to where companies sell to consumers, not where they are based. International corporations will have less scope to deploy tax avoidance schemes." (Helmore, 2021)

A deal, Biden said, would "eliminate incentives to shift jobs and profits abroad, and ensure that multinational corporations pay their fair share here at home. This international agreement is proof that the rest of the world agrees that corporations can and should do more to ensure that we build back better." (Helmore, 2021)

Developing nations:
"Defining developing countries as those which are neither OECD nor G20 members. However, even under such criterion, we must note that a wide spectrum of different degrees of economic development can be distinguished." (Sacchi, 2020)
It is worth asking what role have developing economies played in the design of the BEPS action plan? Unfortunately, "not much", may be the answer. (...) BEPS project "was led by the OECD and G20 and focused on their priorities"(Lassourd, 2022)

Developing countries in particular rely more heavily on corporate income tax revenue, and given the economic toll of the ongoing COVID-19 pandemic over the past 2 years, these governments need to find resources to finance better physical and digital infrastructure.
Firstly, offshore investment centres such as the Cayman Islands, Bermuda, or the British Virgin Islands will have no reason to continue to offer reduced or zero income tax rates to multinational companies. Some countries are already planning to change their headline corporate tax rate. This could make them less attractive for MNEs, possibly leading to a “reshoring” of taxable profit to other countries. (Lassourd, 2022)

Relations with SDGs

It relates to the Sustainable Development Goal number 17, especifically 17.1 which calls upon governments to “strengthen domestic resource mobilization, including through international support to developing countries to improve domestic capacity for tax and other revenue collection.”

Further Reading

https://www.youtube.com/watch?v=Y1r7YKu_xMQ

-CNN video that gives a great overview of the issue in question.

https://www.youtube.com/watch?v=_dgNT_Y27hk

-Analysis by the IMF of the global corporate minimum tax.

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