ICRICT's statement on the negotiation of a UN Framework Convention on International Tax Cooperation (UN FCITC)

ICRICT
Independent Commission for the Reform of International Corporate Taxation

Why do we need a UN convention on tax?

The negotiation of the UN Framework Convention on International Tax Cooperation is a landmark opportunity to reform the outdated global tax architecture and to build a more inclusive and equitable international tax system, enabling countries to cooperate more effectively to ensure equitable taxation and to participate on an equal footing under clear, transparent rules of negotiation. It affords an opportunity to collectively address tax evasion and avoidance - by multinational enterprises (MNEs) and high-net worth individuals - and resolve gaps in global taxation arising from globalization and the digitalization of the world's economies. The efficiency of the international tax system has an important impact on the possibilities for raising domestic revenue for sustainable public financing, which, in turn, is necessary for sustainable and equitable development.

The cross-border movement of capital by financial firms, major asset owners and especially by MNEs has been an increasingly relevant feature of the global economy. While in some cases such movements are motivated by efficiency or other legitimate concerns, in other cases they are motivated by the desire to avoid or evade taxes; the latter movements undermine both global economic efficiency and equity, and may stymie the potential for growth of developing countries and emerging markets and the efforts of governments everywhere to meet the needs of their citizens.

Different national taxation norms and interstices between tax administrations create conflicts of interest among all actors, and double taxation arising from the concurrent exercise by two or more countries of their taxation rights may have an adverse effect on investments of productive or social value.

On the other hand, lack of administrative coordination between tax jurisdictions, profit shifting by MNEs and tax avoidance or evasion by individuals, results in the loss of vital tax revenue, capital flight and illicit financial flows. In today's world, zero or near zero taxation is more of a problem than double taxation. A host of jurisdictions have become known as tax and secrecy havens.

The current system of taxing MNEs' global profits based on transfer pricing supposedly using the arm's length principle has proven itself not fit for purpose in the 21st century world, where unfinished goods go across borders multiple times. This system has facilitated systemic tax avoidance by MNEs, undermining domestic resource mobilization in jurisdictions where these conglomerates make significant profits.

In addition, the past few decades have seen a rapid increase in the amount of double tax treaties signed between countries, from a global number of around 500 to more than 3,000. This network of bilateral tax treaties is skewed towards the needs of resident countries (home not only to the ultimate parent entities of multinational companies, but also, their intermediaries) as such treaties limit the taxing rights of source jurisdictions (often developing countries) restricting their ability to raise revenues.

The combination of transfer pricing and the preference of residence over source taxation in double tax treaties provides the foundation for an embedded global system of tax avoidance and a global tax regime which is complex, inefficient, and unfair.

In a similar way, globalization has opened new tax avoidance possibilities exploited by wealthy individuals around the world and for too long this has been accepted as an inevitable byproduct of capital market liberalization.

The result is that many countries' tax systems have become regressive: the super-rich have lower effective tax rates than other groups in society. This tax regressivity contributes to the rise of wealth concentration and is undermining social cohesion and the basic democratic principles of our societies.
The global design of the tax system is once again a key element of the problem here. The same limitations found in tax treaties covering payments between MNEs at source apply to the case of personal income. Further, tax treaties relating to personal wealth and income in some cases limit the possibility of extending taxresidency or applying exit taxes to individuals, in a world where golden visas are offered to high-net-worth individuals (HNWI) in connection with tax benefits in exchange for relatively modest investment.

In summary, the current design of the international tax architecture fosters tax avoidance and evasion by multinationals and the super-rich.

The negotiation of a UN Framework Convention on international tax cooperation provides a historic opportunity to revisit the recent efforts and advances in the fight to stop tax avoidance and evasion by MNEs and individuals, and to deliver more comprehensive and effective solutions which fully consider the needs and priorities of all countries.

ICRICT strongly supports such negotiation and recommends that it is developed in good faith via an inclusive process, following the already established decision-making rules of the United Nations General Assembly.

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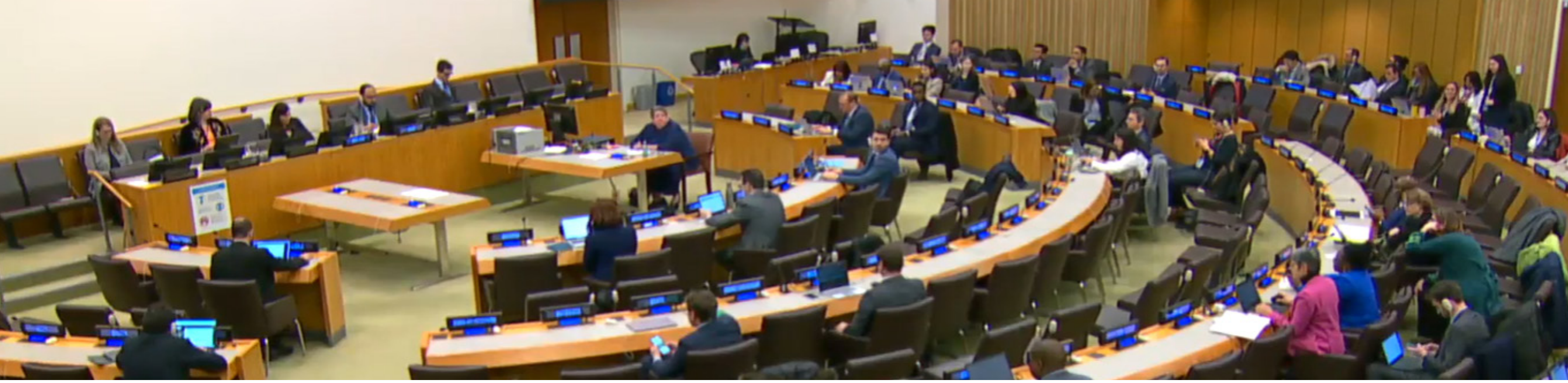


Key issues to be addressed by a UN Framework Convention on International Tax Cooperation

The Commission strongly suggests that the UN FCITC should include some basic principles and commitments:

- Equitable taxation of MNEs, based on:

    - Fair reallocation of taxing rights between countries, underpinned by the principles of unitary taxation and formulary apportionment of all profits of all multinationals across different jurisdictions.
    - The establishment of a nexus rule based on the principle of significant economic presence, whereby a taxable presence will be created in a country when a non-resident enterprise has a significant economic presence; defined as purposeful and sustained interaction with the economy of that country, including sales of goods and services by any means, including digital.
    - Coordinated taxation of windfall or excess profits.
    - The strengthening of anti-avoidance instruments and principles such as a 25% global effective minimum tax on the profits of MNEs.
    - The development of coordinated mechanisms for digital services taxes.
    - Public country-by-country reporting of MNEs' economic activities based on the robust Global Reporting Initiative standard for public reporting on tax (**Tax: 207**).

- Effective taxation of high-net worth individuals, including common principles and minimum standards for the taxation of the very rich and the super-rich, and anti-avoidance instruments such as a global minimum tax on income and wealth (both flows and stocks). This should include a commitment by all countries to ensure effective taxation of wealth as a complement to taxation of income.

- Transparency and exchange of information for tax purposes, including common principles and minimum standards for ensuring transparency of wealth ownership. This should include the creation of a **global asset register** and global standards for asset registers including beneficial ownership identification (including for trusts which obfuscate beneficial ownership), public data components and components to be shared though the automatic exchange of information among tax authorities. Transparency commitments, information sharing and administrative cooperation should also include inter alia:

    - Minimum domestic transparency commitments (e.g. inter-agency sharing of information).
    - Global administrative and judicial cooperation among jurisdictions.
    - Global access to relevant databases.

- Special and differential treatment. In the same way as is the case for trade negotiations, the principle of special and differential treatment should be part of the basis for the negotiation. Without undermining the general coherence of the tax architecture, low and middle income countries should be allowed to have more favourable treatment as well as special rights to address specific constraints.

The Convention and its protocols, as well as the negotiations that would lead to these, should be governed by the same principles and follow the approved **Terms of References** .

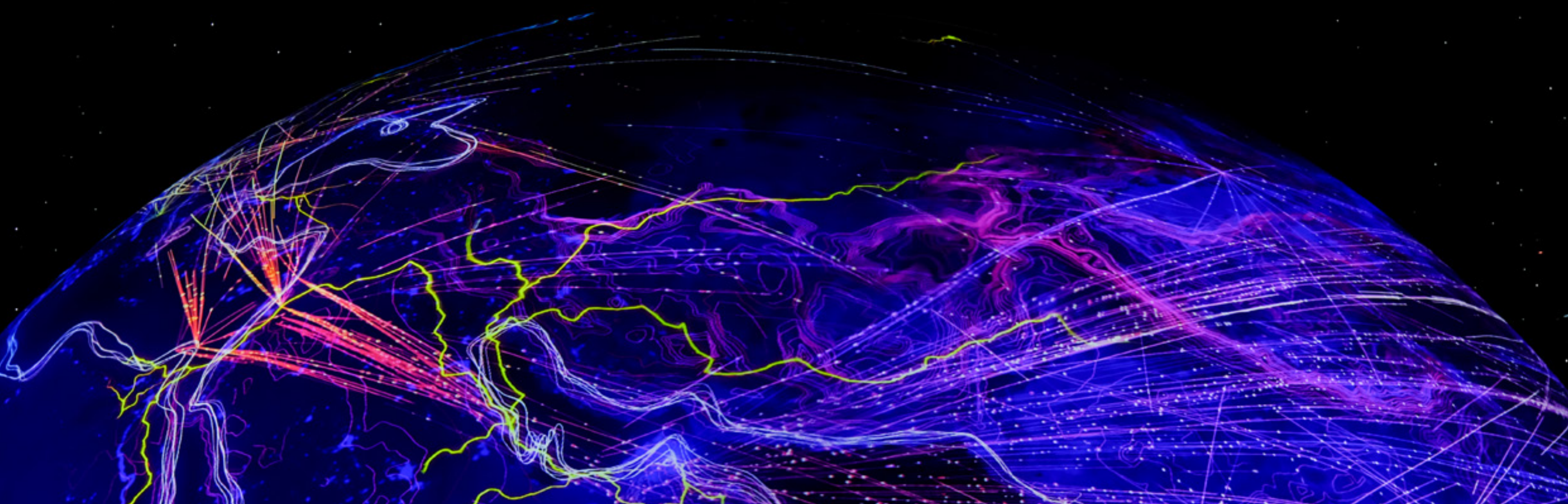
Such principles outlined above should guide the negotiations and outcomes of the UN FCITC in the first place, but also of its protocols.

Each protocol, because of its own nature, could address several of the commitments of the UN FCITC.

For instance, the following protocols could include measures that would address tax evasion and avoidance by high-net worth individuals: measures against tax-related illicit financial flows; addressing tax evasion and avoidance by high-net worth individuals and ensuring their effective taxation in relevant Member States.

In a similar way, the following protocols could include measures to address tax-related IFFs: taxation of income derived from the provision of cross-border services in an increasingly digitalized and globalized economy, taxation of the digitalized economy; measures against tax-related illicit financial flows; addressing tax evasion and avoidance by high-net worth individuals and ensuring their effective taxation in relevant Member States.

Two early protocols will be negotiated alongside the framework convention. The first agreed protocol is 'Taxation of income derived from the provision of cross-border services in an increasingly digitalized and globalized economy' and the second protocol will be chosen from a list of 4 different protocols. It is likely that the second protocol will be either on 'addressing tax evasion and avoidance by high-net worth individuals and ensuring their effective taxation in relevant Member States' or on 'measures against tax-related illicit financial flows'. For this reason, Appendices A, B and C outline the relevance of such protocols and the different measures each protocol should include.



Appendix A. A protocol to address taxation of income derived from the provision of cross-border services in an increasingly digitalized and globalized economy

Why is this protocol important?

Recognition of widespread and continued tax avoidance by MNEs led G20 leaders in 2013 to support the OECD led project on Base Erosion and Profit Shifting (BEPS), to ensure that MNEs could be taxed 'where activities occur and value is created'. The first phase resulted mainly in a patch-up of existing rules, although a system of exchange of MNEs' country-by-country reports among jurisdictions was created, albeit only accessible for tax authorities and difficult for developing countries to join. This failed to resolve the fundamental flaws in the international tax system, due particularly to the priority given to the residence principle, which had been exacerbated by globalization and digitalization. Developing countries continued to try to protect the source tax base, mainly through withholding taxes; and many OECD countries adopted similar measures, although only on digital services.

This put pressure on the negotiations, and in 2019 the G24 group of developing countries proposed a new approach for taxing MNEs where they have a significant economic presence, based on fractional apportionment. This paved the way for agreement on a 'new taxing right', a key element of the '**Two-Pillar Solution**' proclaimed in October 2021 by the OECD/G20 Inclusive Framework (IF).

Amount A of Pillar One accepts the new approach of taxing MNEs on their global profits, with a formulary allocation of taxing rights to countries where they have a minimum threshold of sales, regardless of physical presence. However, Amount A is designed to apply only to the biggest and most profitable MNEs (those with global turnover of at least $20 billion and a profit margin of at least 10%) and re-allocates 25% of only the 'residual profit' (i.e. the profit above the 10% margin) to the countries where they have sales. This would add a new layer of rules, leaving in place the current dysfunctional rules for all other purposes, while adding further complexity and generating little additional revenue.

Moreover, the OECD IF formula uses only sales for reallocation of residual profits. This disadvantages countries with relatively small domestic markets, or those with substantial exports. As rich countries consume more, the allocation of profits by sales only is likely to result in an unequitable distribution between countries. There is no economic justification for this particular formula, and in many cases, it is clearly inappropriate.

Pillar One has still not been agreed, and even if it were, it is highly unlikely to be implemented. Its adoption would require ratification of a multilateral convention by a critical mass of states, including the United States that is the headquarters of most of the largest and most profitable multinationals. Given the two-thirds majority in the Senate required for ratification, the US Congress almost certainly will not ratify it any time soon.

Furthermore, signing and ratifying Pillar One's Amount A multilateral convention requires countries to give up their autonomous taxing rights. They must commit to not implementing digital services taxes, and other measures like withholding taxes would be contested. This ties the hands of governments on what taxes they can impose in future, in return for a very limited amount of expected revenue. The taxes forgone could be an increasingly important source of revenue for developing countries in the future as revenues from digital services continue to increase, making signing on to Pillar One even less attractive for developing countries.

Based on the above limitations, ICRICT's advice to countries is to not sign the multilateral convention required to implement Pillar One but proceed to introduce alternative measures such as withholding taxes or digital services taxes.

In this context, the call to negotiate 'A protocol to address taxation of income derived from the provision of cross-border services in an increasingly digitalized and globalized economy' as part of the UN FCITC represents an important opportunity. The problem of taxation of cross-border services reveals the defects of current rules perhaps more than any other. Services generally involve a close relationship with clients and customers, especially in the era of user-generated content and data collection. Yet due to globalization and digitalization they have become increasingly easy to deliver with little or no physical presence.

Services have become increasingly important for economic development, but international tax rules favouring delivery by non-residents act as a disincentive to the growth of local services providers, particularly disadvantaging developing countries which are mainly hosts to MNEs. The spread of tax treaties favouring the OECD model has been accompanied by a widening deficit in services trade of developing countries, with a weakening of their attempts to protect their tax base through withholding taxes resulting in increasing losses of tax revenue.

Consequently, two approaches would be possible in designing a protocol under UN auspices. One would be an agreement to strengthen source taxation, mainly through withholding taxes. In fact, a model for this has already been developed by the United Nations Committee of Experts on International Cooperation in Tax (UNTC) , which includes a **Fast Track Instrument** that would facilitate the incorporation of all the provisions in the UN tax model to protect source taxation for all services. Many countries, including OECD members, have adopted digital services taxes (DSTs), which are similar in nature to withholding taxes, and both the convention and a protocol could aim to standardize these. However, this would not resolve the wider problem of protecting the source tax base, which is more acute for developing countries. The alternative, which reflects ICRICT's long-standing position, would be for the protocol to agree the principle of unitary taxation of MNEs based on formulary apportionment. This would ensure taxation of income from all cross-border services, indeed it would resolve the problem of MNE taxation in a comprehensive and effective way.

The protocol itself should include the basic principles for unitary taxation and formulary apportionment, as well as procedures for its coordinated implementation by willing states. The more detailed technical standards for application of the approach should be formulated as model rules, as has been done for the global corporate minimum tax under Pillar Two. These standards could be based on those already formulated for Amount A of Pillar One, including (i) a quantitative threshold of sales revenue to define taxable presence; (ii) rules for the adjustment of MNEs' consolidated financial accounts to define their global net profit for tax purposes; (iii) rules to define the source of sales revenues particularly for services; and rules to define and quantify the other factors to be used for apportioning rights to tax (e.g. physical assets, employees and data presence / data extraction).

Key aspects to be included in the protocol to address taxation of income derived from the provision of cross-border services in an increasingly digitalized and globalized economy

This protocol should include, but not be limited to, taxation of Automated Digital Services (ADS) and ideally the scope should cover all services.

The protocol should set rules for coordinating the taxation of income from cross-border services ensuring coherence in treatment between comparable services. Therefore, the protocol should result in:

- Fair reallocation of taxing rights between countries, underpinned by the principle of unitary taxation and formulary apportionment of all profits of all multinationals across different jurisdictions. This would require the development of a nexus rule based on the principle of significant economic presence, whereby a taxable presence will be created in the country when a non-resident enterprise has a Significant Economic Presence (SEP), defined as purposeful and sustained interaction with the economy of that country.

- Simplification of the right to tax at source payments for services, regardless of whether they may be classified as technical or professional, or delivered by an independent person or an enterprise.

- Development of coordinated mechanisms for the taxation of digital services.

- Coordinated taxation of windfall or excess profits.

- The strengthening of anti-avoidance instruments and principles such as a 25% global effective minimum tax on the profits of multinational corporations.

To achieve this, the following alternatives should be considered in a protocol to address taxation of income derived from the provision of cross-border services in an increasingly digitalized and globalized economy:

- Withholding of income taxes on a deemed profit earned or on gross payments for all services (not just digitalized services).

- Formulary Taxation of Net Income from Sales (i.e. apply global profit margin to local sales revenue).

- Formulary Apportionment.

- Digital service taxes on gross revenues should be considered as a valid solution for the taxation of Automated Digital Services (ADS).

Further, the design of a protocol on the taxation of MNEs' profits should be based on a principle of allocating taxing rights based on location of real activities; but also based on an objective of minimising profit shifting. Criteria which take into consideration the use of data to extract profit should also be considered for the allocation of taxing rights. Some possible considerations in this regard could include allocating taxing rights based on sales (with due consideration of both location of final customers and country of origin in the case of natural resources, including agriculture), employees, location of physical assets and data presence / data extraction.

Enforcement and collection mechanisms should be kept simple and easy to administer.

In addition, this protocol should also address issues such as transparency and effective international cooperation for tax matters, including:

- Public country-by-country reporting of MNEs' economic activities based on the robust Global Reporting Initiative standard for public reporting on tax (**Tax:207**).

- Extend the reach and effective implementation of the automatic exchange of information on income derived through digital platforms.

Appendix B. A protocol addressing tax evasion and avoidance by high-net worth individuals (HNWI) and ensuring their effective taxation in relevant Member States.

Why is this protocol important?

Several recent studies have highlighted the evidence on income and wealth inequality estimates in both high-, middle- and low-income countries. Income concentration of the super-rich has risen sharply, as between 1987 and 2024 the average wealth of the top 0.0001% richest households globally has increased by about 7% a year on an average net of inflation, much faster than average wealth (3% a year).

High-net worth individuals benefit from low effective tax rates, typically lower than those paid by other economic strata. Instead of being progressive, contemporary tax systems fail to effectively tax HNWIs.

In a similar way to MNEs, globalization has opened new tax avoidance possibilities exploited by wealthy individuals around the world and for too long, this has been accepted as an inevitable byproduct.

HNWIs have de-localized their wealth, diversifying it into various assets located in different jurisdictions, underneath layers of shell companies, trusts and other opaque legal arrangements that disguise the actual or beneficial owners.

Moreover, the taxation of wealth has been reduced over the past decades, contributing to increasing the income gap between the wealthiest individuals and the rest of the population. The resulting reduced effective taxation of such individuals undermines the possibility of addressing equality and redistribution, as some individuals successfully manage to escape the reach of the national States.

This also undermines trust in democratic institutions and thereby affects social cohesion. The rise of wealth concentration leads to a concentration of political power in the hands of the wealthy on the one hand, and a growing sense of economic injustice among the electorate on the other.

The global design of the tax system is again part of the problem in this case. The same limitations referred to in tax treaties for the taxation of payments between MNEs at source are applicable to the case of personal income. Further, many tax treaties limit the possibility of extending tax residency or applying exit taxes to individuals, in a world in which there is a growing tendency for some jurisdictions to offer tax residency to HNWIs, with tax benefits in exchange for investment.

Therefore, a coordinated approach to taxation of HNWIs is required to address global tax regressivity and enable countries to raise revenues and enable effective taxation of HNWIs.

An objective of North-South progressivity (as well as across-gender progressivity) and fair allocation of taxing rights must be a guiding principle in the

design of the protocol addressing tax evasion and avoidance by high-net worth individuals (HNWI) and ensuring their effective taxation in relevant Member States.

This globally agreed allocation of taxing rights should in principle take into consideration both the location of the assets and the residence of the taxpayer. In the absence of published consolidated country-by-country accounts for HNWIs (in contrast to the position for large multinational corporations) it is necessary for the relevant tax jurisdictions to share wealth data with other jurisdictions affected. In the case of small and/or poor countries in the Global South with limited administrative capacity, it may be necessary for advanced economies (and their associated low tax jurisdictions) to provide direct assistance in tax collection as well as information.

Moreover, because the wealth of HNWIs is globally created in the sense that it arises from private control over international assets and markets, there is a strong case for at least a part of the new wealth tax revenue to be applied to the provision of global public goods such as pandemic disease control, environmental resilience and economic security for the poorest. Such provision must be exercised through multilateral institutions with adequate representation of the Global South.

Key aspects that should be included in a protocol addressing tax evasion and avoidance by HNWI and ensuring their effective taxation in relevant Member States

To effectively address the issue of the effective taxation of HNWI, the protocol should be designed in a way as to:

1. Help improve transparency and information exchange to strengthen domestic initiatives by:

    - Requiring country-by-country reporting for multinationals to feature legal and Beneficial Ownership (BO) information to get a more comprehensive mapping of the ownership of listed & unlisted corporations.

    - Working towards a global reach of transparency on beneficial owners of legal entities and other legal arrangements (e.g. trusts, private foundations, etc) and their use for addressing tax evasion and avoidance (e.g. effective abolition of bearer shares; verification of BO through international cooperation; sharing of best practices on personal income tax and wealth taxation going beyond legal ownership).

    - Extend existing tax cooperation standards by: (a) Improving the effective use of the Common Reporting Standard in as many countries as possible; (b) Extending automatic exchange of information to more asset classes, working towards the creation of a global asset registry.

2. Address the following issues that have historically limited the ability of countries to effectively tax wealth:

- Methodology for the valuation of assets.
- Liquidity issues regarding tax payment.
- Identification of limitations posed by tax treaties.
- Solutions for effective taxation of trusts.

3. Move towards harmonized standards to fight the race to the bottom & unfair competition by:

- Creating guidelines to harmonize wealth valuation to facilitate the work of tax administrations in assessing asset valuation of high-net-worth taxpayers and enable countries to introduce national wealth taxes.
- Ensuring that the work of the United Nations Committee of Experts on International Cooperation in Tax (UNTC) will be incorporated to the UN FCITC and its protocols; in particular in view of the work the UNTC has done in providing countries with tools to implementing wealth taxes and wealth taxation more broadly through the **UN Handbook on Wealth and Solidarity Taxes** and the upcoming UN Sample Law on Wealth Taxes.
- Designing rules to prevent unfair tax competition, including extended exit taxes or trailing rules (extending tax residency after exiting the country), among others.
- Modifying the model tax convention and existent tax treaties in order to introduce changes in residence definition and taxing rights.
- Agreeing to a common minimum effective taxation standard for HNWI, defining threshold, tax base, and rate. This should include the design of rules for self-enforcement of a common standard.

Appendix C. A protocol on measures against tax related Illicit Financial Flows (IFFs)

Why is this protocol important?

IFFs can include flows originating from illicit activities, illicit transactions to transfer funds that have a licit origin, and flows stemming from licit activity being used in an illicit way.

The problem is systemic, as highlighted in the 2021 UN High Level Panel on International Financial Accountability, Transparency and Integrity for Achieving the 2030 Agenda (FATCI Panel) report.

Illicit financial flows include tax avoidance by multinationals and wealthy individuals, who take advantage of globalization in order to arbitrate between the tax systems of different jurisdictions, choosing the most convenient ones to minimize their tax liabilities. In addition, international vulnerability to IFFs is increased when a country's incoming and outcoming flows take place in secrecy jurisdictions.

For all the above, enhancing transparency, exchange of information and international administrative cooperation in tax matters is key, and has indeed proven to have impressive effects on tax collection. It is important to remove the barriers that limit the reach of such cooperation in the case of low-income countries. It is also important to advance on a wider use of information exchanged for tax purposes, so to address related financial crimes.

However, transparency should not be the sole aspect to be worked on. The design of the international tax architecture needs to be addressed also to support countries exercise their taxing rights and fight aggressive tax evasion and avoidance.

Key aspects that should be included in a protocol on measures against tax related IFF

ICRICT considers that the definition of IFF should be addressed by a protocol of this nature and should consider the work already developed by UNCTAD and UNODC, among others, observing that IFFs are multi-dimensional, and can include flows originating from both licit and illicit activities, including tax evasion and avoidance.

Further, the issue of measuring IFFs is also a relevant one which should also be considered in the protocol.

Therefore, some priority areas to be included in a protocol on measures against tax related IFFs, particularly those related to tax avoidance by MNEs, are:

- Fair reallocation of taxing rights between countries, underpinned by the principle of unitary taxation and formulary apportionment of all profits of all multinationals across different jurisdictions.
- Simplification of the right to tax at source payments for royalties, interest, dividends and fees for services (most common channels for profit shifting), regardless of whether they may be classified as technical or professional, or delivered by an independent person or an enterprise; and regardless of the physical presence.
- The adoption of solutions for intra-group payments as well as for the taxation of capital gains which result from Offshore Indirect Transfers (OITs) of assets.
- Public country-by-country reporting of multinationals' economic activities based on the robust Global Reporting Initiative standard for public reporting on tax (Tax:207).
- Extend the reach and effective implementation of the automatic exchange of information on income derived through digital platforms.

Further, the adoption of solutions for the valuation of intragroup trade in goods that consider effective ways of taxing exports at the country of origin in the case of natural resources (including goods), should also be considered.

In addition, and in the same way as was observed by the **report** produced by the UN FACTI Panel in 2021, ICRICT notes that some other issues that should also be addressed in a protocol on measures against tax related illicit financial flows are:

- Provide for effective capital gains taxation.
- Taxation must be equitably applied on services delivered digitally. This requires taxing MNEs based on group global profit.
- End information sharing asymmetries in relation to exchange of information for tax purposes, so that all countries can participate on an equal footing.
- Establish guidelines for exchange of information at the national level across agencies as standard practice to combat all varieties of illicit flows.
- Provide solutions for the elimination of barriers for a wider use (e.g. for anti-money laundering) of information exchanged for tax purposes.

Finally, ICRICT stresses that transparency of ownership and control of companies, partnerships, trusts and other legal entities that can hold assets and open bank accounts is critical to determining where illicit funds are moving and who is moving them. Therefore, enhancing automatic exchange of information and beneficial ownership registers should be one of the commitments resulting from this protocol.

All countries should require beneficial ownership information to be provided when they incorporate companies, and register assets, for that information to be updated regularly, and for that information to be available on the public record.

Further, it should be noted that advancing the transparency and digitalization of commercial registers , including information on financial statements, that can be used for building comparable data for the application of the arm's length principle (until another global principle replaces it), would also serve the purpose of reducing IFFs.