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Combatting tax avoidance, the OECD way? The impact of the BEPS Project on developing and emerging countries' approach to international tax avoidance

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8 The normative debate around the BEPS Project

What should we make of the findings? Is it a good thing that the countries studied in this research project go to some lengths to implement the BEPS Project? Or is it positive that they do not adopt everything too closely? What does it mean for the interpretation of the BEPS Project as a whole? Should one view the association of developing countries to the project as positive? The purpose of the following section is to review the normative debate on the BEPS Project, and assess where the findings of the preceding chapters could feed into the debate.

Scholars and organizations concerned with tax policy in developing countries have voiced scepticism about the BEPS Project from the onset.[1] Critics question the narrative of cooperation that is used by political leaders to advertise the BEPS Project. Hearson, for example, says that "If the North-South dimension is not surfaced as an important axis of conflict between states, the tools of tax cooperation will continue to deprive lower-income countries of revenue, even though they are being recast as weapons to help all states in the fight against tax avoidance and evasion."[2]

Critiques are formulated with different levels of vigour, though, and are rooted in different conceptions about how alternatives could have looked like. This section reviews and classifies the different critiques and explains when and how knowledge about the way countries deal with the BEPS Project in practice, such as the findings from this study, matters to the concerns expressed and where more research still needs to be carried out.

8.1 Inclusion in the decision-making process

The starting point in the critical literature on the BEPS Project is the lack of participation of developing countries in the process that produced the policy outcomes.[3] Authors highlight that only very few countries beyond the OECD Member States participated: the non-OECD G20 members (India, Indonesia, Russia, China, Argentina, Brazil, South Africa, Saudi Arabia), as

1 For a summary of criticisms, see also Oei, "World Tax Policy in the World Tax Polity? An Event History Analysis of OECD/G20 BEPS Inclusive Framework Membership," 9–10.

2 Hearson, *Imposing Standards*, 30.

3 Mosquera Valderrama, "Legitimacy and the Making of International Tax Law: The Challenges of Multilateralism," 2015; Oguttu, "Tax Base Erosion and Profit Shifting in Africa-Part 1: What Should Africa's Response Be to the OECD BEPS Action Plan?"

well as accession candidates Colombia and Latvia.[4] Only in June 2016, several months after the final reports were published, all other countries were invited to implement the outcome and join the Inclusive Framework to discuss remaining issues and monitor implementation.[5] This procedure was heavily criticized and led campaigners in developing countries to popularize the slogan that developing countries were "not at the table, but on the menu".[6] As discussed in section 4, most parts of the BEPS Project originated indeed in the tax policies of OECD member countries, with the exception, however, of some transfer pricing policies inspired by India and Argentina, and the country-by-country reporting proposal (see also section 5).

A possible objection to the critique could be that participation and occasional influence from countries from the Global South represents an improvement compared to how tax policy norms were developed in the past, when there was no involvement at all from developing countries. Shay and Christians state that the decision to invite developing countries to the BEPS Project was partly driven by a desire to respond to past criticism.[7] Moreover, it is not self-evident what OECD members would gain from the fact that non-member countries (except maybe from other countries with MNE headquarters such as China, India, Brazil, and countries that facilitate profit shifting) implement BEPS standards. Most developing countries do not act as locations that facilitate profit shifting out of OECD member countries, and whether other countries defend themselves against tax avoidance should be primarily their concern. Consequently, one could view the Inclusive Framework more as an open offer to non-OECD members which they are free to accept or reject.

However, a contradiction of this interpretation is the fact that developed countries (although not through the OECD) appear to have coerced some developing countries to committing to the BEPS Project by including commitment to implement the BEPS minimum standards as one of the criteria of the EU list of non-cooperative jurisdictions.[8] The force of the critique also depends somewhat on the actual burden that committing and implementing the BEPS minimum standards would represent for developing countries. The relation between the EU list of non-cooperative jurisdictions and the BEPS minimum standards is further discussed in section 8.3.

4 Mosquera Valderrama, "Legitimacy and the Making of International Tax Law: The Challenges of Multilateralism," 2015, 4.

5 OECD, "About the Inclusive Framework on BEPS."

6 Christensen, Hearson, and Randriamanalina, "At the Table, Off the Menu? Assessing the Participation of Lower-Income Countries in Global Tax Negotiations."

7 Shay and Christians, "Assessing BEPS: Origins, Standards, and Responses," 38.

8 Oei, "World Tax Policy in the World Tax Polity? An Event History Analysis of OECD/G20 BEPS Inclusive Framework Membership"; Mosquera Valderrama, "The EU Standard of Good Governance in Tax Matters for Third (Non-EU) Countries"; Dourado, "The EU Black List of Third-Country Jurisdictions."

In sum, the analysis of the process of standard production seems to speak in favour of the BEPS Project's interpretation as "imposition" of policy preferences by some countries on others. However, the process is only one side of the argument. The fact that most developing countries did not participate is not sufficient on its own to argue that the BEPS Project is "bad" for developing countries. Usually, commentators do not go as far as suggesting that the non-inclusive decision-making process would be a sufficient reason to reject the outcome altogether.[9] With hindsight, the BEPS Inclusive Framework, which since 2016 reunites all countries that have committed to implement the BEPS Project and that participate in the monitoring process, has become the platform to discuss further reforms, especially concerning the taxation of the digital economy and the global minimum tax proposal (BEPS 2.0). In these discussions, even if fundamental obstacles to meaningful participation and representation remain,[10] a formal possibility to influence the outcomes exists for developing countries.

Finally, it is important to distinguish whether the outcome of the BEPS Project was just not "good enough" for developing countries or whether it actually makes things worse. For that it is necessary to consider the critiques regarding the content of the Project's outcome.

8.2 Critiques about the content

Critiques regarding the BEPS Project's content from the perspective of developing countries are raised from different standpoints, some of which acknowledge that international tax avoidance by MNEs is a policy problem for developing countries, whereas others negate this. Some critiques even suggest that international tax avoidance may be an opportunity for developing countries.

8.2.1 Administrative resource intensity

The main strand of critiques generally acknowledges that international tax avoidance may indeed be a policy issue that developing countries would have an interest in addressing. However, critics argue that the way advocated by the BEPS Project is not adequate due to the expected amount of administrative resources required to implement the solutions. Most developing countries' tax administrations and ministries face a relative

9 Mosquera Valderrama, "Output Legitimacy Deficits and the Inclusive Framework of the OECD/G20 Base Erosion and Profit Shifting Initiative"; Oguttu, "Tax Base Erosion and Profit Shifting in Africa–Part 1: Africa's Response to the OECD BEPS Action Plan."

10 Christensen, Hearson, and Randriamanalina, "At the Table, Off the Menu? Assessing the Participation of Lower-Income Countries in Global Tax Negotiations."

scarcity of resources. Lennard, chief of the UN Tax Committee, explained with regard to developing countries' assessment of solutions to deal with the digital economy: "They feel that when things get really complicated, they are the ones who bear the cost of the complications because of their limited resources and limited information."[11] Brauner argues that "The post-BEPS discourse focuses on anti-abuse. This focus will never be in favour of the source country. Poor countries obviously have less ability to use their enforcement powers than richer countries."[12] With regard to BEPS Action 6, for example, the BEPS Monitoring Group, a consortium of civil society activists and academics, criticized that countries need to engage in exchange of information procedures if they want to enforce the suggested treaty anti-abuse clause and that transfer pricing rules have been made more complex.[13]

How authors further develop their critiques varies depending on the assumptions that are made regarding how countries would deal with that situation. In essence, if countries simply do not use the standards (i.e., they do not implement them or they implement but do not enforce them), then they would remain with the problem of tax avoidance. If countries choose to fully implement the standards and build up resources for enforcing them, then this may crowd out policymaking and administrative activity in other areas that are more important. If, however, countries choose to adopt different solutions for the issue of international tax avoidance, critiques fear that this could have negative consequences, for example double taxation (because the other state does not recognize the legitimacy of the solution adopted and does not provide a credit for the tax levied) and consequently less genuine foreign investment, disputes with other countries, or a negative reputation, or diplomatic issues that could lead to problems in other policy areas because the solution is not recognized as "internationally acceptable" practice.

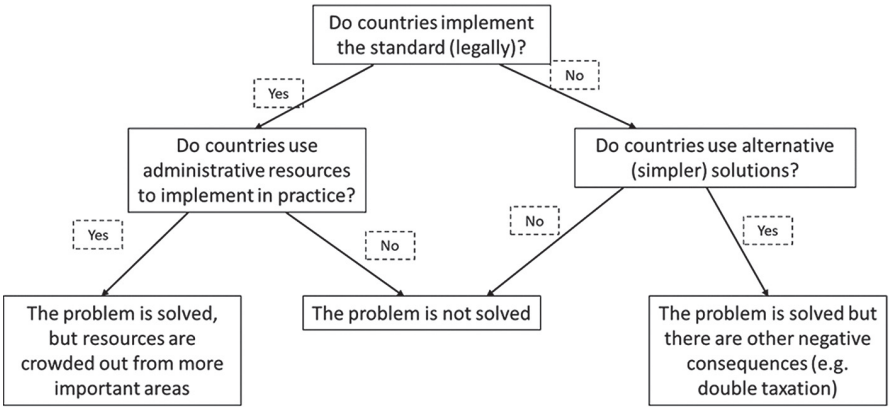
Figure 17 summarizes these arguments. The next sub-sections explore them in more detail.

11 Lennard quoted in Finley and Smith, "Article 12B Doesn't Create a New Taxing Right, U.N. Official Says."

12 Brauner, "International Tax Policy: Between Competition and Cooperation."

13 The BEPS Monitoring Group, "Overall Evaluation of the G20/OECD Base Erosion and Profit Shifting (BEPS) Project."

Figure 17: Critiques derived from the administrative resource intensity of the BEPS Project's solutions, dependent on countries' decisions



Source: the author

8.2.2 Crowding out action in other areas

The "crowding out" critique goes that if developing countries attempt to implement the outcome of the BEPS Project, scarce resources of policymakers and administrators may be diverted from other issues where these may be more productive in terms of tax revenue generation or improvement of the tax system more generally. Consequently, engaging with the BEPS Project could even lead to less tax revenue generation.

There are different versions of this critique: Authors diverge for example with respect to whether attention should instead be directed to different types of international tax avoidance by MNEs than the types addressed in the BEPS Project or on other tax policy issues altogether. Some suggest that developing countries should direct more resources to other tax issues such as redundant tax incentives, evasion of personal income tax, bringing the informal economy into the tax net, or reducing corruption in the tax authority.[14] Hongler, for example, states that: "[…] the BEPS Project should have, for instance, contained a specific action on BEPS in the poorest states on this planet, i.e., how to mobilize domestic resources in these states."[15] He references levying taxes on commodity extraction or improving tax administrations as potential areas that the BEPS project could have addressed.

14 Mosquera Valderrama, "Output Legitimacy Deficits and the Inclusive Framework of the OECD/G20 Base Erosion and Profit Shifting Initiative"; Hongler, *Justice in International Tax Law – A Normative Review of the International Tax Regime*.

15 Hongler, *Justice in International Tax Law – A Normative Review of the International Tax Regime*, 465–66.

Monkam et al. wrote in 2018 that some countries were neglecting the implementation of exchange of information of taxpayer information since staff was focused on BEPS.[16]

In all the four countries studied, interviewees mentioned other issues that were not addressed in the BEPS Project as important priorities for the government, such as the taxation of indirect transfers of assets, issues related to legal certainty in domestic dispute resolution procedures, tax incentives, evasion in the informal sector or improving policy in other taxes than corporate tax. However, over the last years, all countries introduced measures that also related to these issues. Colombia and Senegal, for example, introduced a provision to tax indirect transfers.[17] India had already done so in 2012.[18] Colombia commissioned a report in 2021 to evaluate its tax incentives.[19] In addition, the relative importance of the issues addressed in the BEPS reports vs. other issues is difficult if not impossible to quantify with current methods and data available. Other issues may not necessarily be easier to solve.[20] However, it remains a possibility that scarce resources are distracted from other potentially more productive work. This could be even more the case in countries with less developed administrations than in the countries studied.

A potential reply to the crowding out argument would be that administrative capacity does not necessarily need to remain static. The OECD offers specific capacity building programs through its "Knowledge Sharing Alliance"[21], the "BEPS twinning programme" whereby one developed country tax administration works together with a developing country tax administration,[22] and the "Tax Inspectors Without Borders" program, which is implemented jointly with the United Nations Development Program.[23] A concern raised by the critiques towards capacity building programs, though, is that these may not be sustainable, if highly educated tax administrators are subsequently recruited by private sector law and accounting firms that are able to offer higher salaries.[24] In all countries (except Nigeria),

16 Monkam et al., "Tax Transparency and Exchange of Information (EOI): Priorities for Africa," 7.

17 Cabrera, "Taxing the Indirect Transfer of Colombian Assets"; République du Sénégal, Loi n°2019-13 du 8 juillet 2019 portant loi de finances rectificative pour l'année 2019, pt. Titre II, 65.

18 Vasudevan and Nagappan, "Indirect Transfer Taxation in India: From Vodafone to Cairn."

19 Comisión de Expertos en Beneficios Tributarios, "Informe de La Comisión de Expertos En Beneficios Tributarios."

20 Scholars argue, for example, that not too much revenue should be expected from efforts that aim at reducing the size of the informal economy in developing countries: Gallien, Rogan, and Van den Boogaard, "The World Bank and IMF Are Using Flawed Logic in Their Quest to Do Away with the Informal Sector."

21 https://www.oecd.org/knowledge-sharing-alliance/ksa-pilot-project-beps.htm

22 OECD, "Background Brief. Inclusive Framework on BEPS," 15.

23 http://www.tiwb.org/

24 Sheppard, "De-FANGed International Taxation, Part 3," 395.

I interacted with former tax administration officials that had started a career in the private sector. In particular in Colombia, interviewees from both public and private sector criticized the lack of independence of the tax administration in designing career paths that would allow it to better retain talents.[25]

Other versions of the "crowding out" critique explicitly negate the significance of the phenomenon of base erosion and profit shifting for tax revenues in developing countries.[26] This is generally contradicted by empirical studies.[27] These studies are not free of problems, however, and generally suffer from a lack of fine-grained data. The results from this research show that in BEPS is a problem for developing countries. But how big it is and how it looks like is highly context specific. It depends for example on the degree to which a country has already adopted policies akin to OECD countries, whether it has signed many tax treaties, and to what extent it has dismantled foreign exchange regulations. In particular in countries that still have stricter protectionist policies in place, it is likely that international tax avoidance is a lesser issue or manifests itself differently.

In short, whether the "crowding-out" critique applies is highly context-specific. Countries should certainly evaluate carefully whether they should implement recommendations from the BEPS Project, but the evidence from this study suggests that they generally do so – and do not blindly implement policies while neglecting other important areas.

8.2.3 Not endorsing simpler solutions

Criticizing the resource intensity of the solutions proposed by the BEPS Project begs the question whether fighting international tax avoidance could be achieved through simpler ways. Critics claim that this is indeed the case. Oguttu for example argued that "This one-sided approach of addressing BEPS by patching up (or strengthening) current anti-avoidance legislation (that some capital-importing countries do not have or do not have the capacity to implement) is not the only solution to addressing global BEPS concerns."[28]

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25 CO15, CO01

26 Rocha, "The Other Side of BEPS: 'Imperial Taxation' and 'International Tax Imperialism,'" 194.

27 Johannesen, Tørsløv, and Wier, "Are Less Developed Countries More Exposed to Multinational Tax Avoidance? Method and Evidence from Micro-Data."; Cobham and Janský, "Global Distribution of Revenue Loss from Corporate Tax Avoidance: Re-estimation and Country Results."

28 Oguttu, "A Critique of International Tax Measures and the OECD BEPS Project in Addressing Fair Treaty Allocation of Taxing Rights between Residence and Source Countries: The Case of Tax Base Eroding Interest, Royalties and Service Fees from an African Perspective," 327.

For Oguttu, the failure to strengthen taxing rights for source countries was the central problem of the BEPS Project. She regretted that "certain practical measures (such as withholding taxes) that may be more suitable for African countries in addressing BEPS" were not given more attention.[29] Echoing this critique, some scholars advance that profit shifting due to transfer mispricing of imports, as well as concerns about excessive interest deductions, can be mitigated in a simple way if a country imposes higher withholding taxes on royalties, interest, and technical and management services.[30] With regard to treaty shopping, only relying on the principal purpose test to combat treaty shopping may not be sufficient if the test is too difficult to apply. Instead, terminating or re-negotiating individual treaties to reduce the beneficial character that incentivizes MNEs to "treaty shop" may be more effective. However, the BEPS Action 6 report stresses that treaty termination should only be considered as measure of last resort.[31]

A common criticism of BEPS Action 13 on country-by-country reporting is that the same aim could have been achieved with less resources if companies had simply been obliged to make the report public, instead of building a system to exchange reports among tax authorities accompanied with the obligation to introduce procedures to ensure the confidentiality of the information.[32] In sum, many authors point out that potentially simpler methods to deal with international tax avoidance issues than those endorsed in the BEPS Project are available. The BEPS Monitoring Group regret that better and more effective alternatives of two kinds have not been explored, namely formulary apportionment and "full inclusion" CFCs (an idea which in principle resembles the Pillar 2 minimum tax proposal).[33] Brauner argued with respect to the work on CFC rules that it may create a distraction if it forestalls broader discussions about business income apportionment.[34] Arguably, these broader discussions have been postponed, but have not been entirely prevented, since the discussion about Pillar 1 and Pillar 2 is exactly about these topics.

The discussion of countries' responses to transfer pricing and treaty shopping show indeed that other solutions are available, from withholding taxes over simpler transfer pricing methods to discretionary enforcement

29 Oguttu, "Tax Base Erosion and Profit Shifting in Africa–Part 1: Africa's Response to the OECD BEPS Action Plan," 27.

30 Balabushko et al., *The Direct and Indirect Costs of Tax Treaty Policy: Evidence from Ukraine*; Beer and Loeprick, "Too High a Price? Tax Treaties with Investment Hubs in Sub-Saharan Africa," 114.

31 OECD, *Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, Action 6 - 2015 Final Report*, 94; Marian, "Unilateral Responses to Tax Treaty Abuse: A Functional Approach," 1161.

32 Knobel and Cobham, "Country-by-Country Reporting: How Restricted Access Exacerbates Global Inequalities in Taxing Rights."

33 The BEPS Monitoring Group, "Overall Evaluation of the G20/OECD Base Erosion and Profit Shifting (BEPS) Project."

34 Brauner, "BEPS: An Interim Evaluation," 23.

practices. But does the BEPS Project really prevent countries from adopting them?

Minimum standards or maximum standards?

One might object to the criticisms mentioned above that countries are always free to introduce those simpler alternatives if they consider them as more suited to their needs. The first BEPS report released in 2013 notes that "Of course, jurisdictions may also provide more stringent unilateral actions to prevent BEPS than those in the co-ordinated approach."[35] Moreover, knowledge about alternatives is generally available: The UN, for example, publishes the UN Model Tax Convention, which suggests higher withholding taxes at source,[36] or the UN Practical Manual on Transfer Pricing for Developing Countries, which includes discussions of the practices by India, Brazil, China, and Kenya, among others, which do not necessarily follow the OECD approach.[37] Regional organizations such as CIAT and ATAF have published guidelines, as well, that include non-standard practices used by countries.[38]

One might also object that what the BEPS Project offers is better than what previous standards promoted by the OECD offered. After all, it recommends stronger and sometimes simpler measures in certain areas than previously. For example, BEPS Action 10 can be read as a certain acceptance of the so-called "Sixth Method" to calculate transfer prices in commodity transactions.[39] This method, which calculates arm's-length-prices in commodity transactions based on prices publicly quoted on international exchanges was first developed by Argentina, and then gradually adopted by other Latin American countries.[40]

Everything else being equal, having an anti-treaty-shopping clause in a tax treaty may potentially protect source taxing rights better than nothing at all. And even if tax authorities did not have the resources to use the

35 OECD, *Addressing Base Erosion and Profit Shifting*, 9.

36 United Nations, Model Double Taxation Convention between Developed and Developing Countries 2017.

37 United Nations, "Practical Manual on Transfer Pricing for Developing Countries (2017)"; Hearson, "UN Transfer Pricing Manual: What Brazil, India and China Do Differently."

38 CIAT, "Cóctel de Medidas Para El Control de La Manipulación Abusiva de Precios de Transferencia, Con Enfoque En El Contexto de Países de Bajos Ingresos y En Vías de Desarrollo"; African Tax Administration Forum, "Suggested Approach to Drafting Transfer Pricing Legislation"; African Tax Administration Forum, "Suggested Approach to Drafting Transfer Pricing Practice Notes."

39 Christensen, Hearson, and Randriamanalina, "At the Table, Off the Menu? Assessing the Participation of Lower-Income Countries in Global Tax Negotiations," 16–17; CIAT, "Cóctel de Medidas Para El Control de La Manipulación Abusiva de Precios de Transferencia, Con Enfoque En El Contexto de Países de Bajos Ingresos y En Vías de Desarrollo," 40.

40 CIAT, "Cóctel de Medidas Para El Control de La Manipulación Abusiva de Precios de Transferencia, Con Enfoque En El Contexto de Países de Bajos Ingresos y En Vías de Desarrollo," 39.

anti-treaty shopping clause in tax audits, it could have a deterrent effect on private actors. Finally, even though accessing country-by-country reporting data was made difficult for developing country tax administrations, prior to BEPS it would probably have been difficult for most of them to obtain similar information on MNEs headquartered in foreign countries at all.[41]

As a consequence, the critique would be stronger if it could be shown that the BEPS Project not only failed to recommend simpler (and in the context of limited resources more effective) solutions to the issue at hand, but if it actively prevented more effective actions that developing countries could realistically undertake. There are indeed a number of arguments to support such a view.

First, the purpose of the BEPS minimum standard related to dispute resolution (Action 14) has the purpose of limiting countries' ability to interpret treaties in a manner that would be too "creative", i.e., too different from what is considered internationally acceptable practice and it does not provide a country with resources to better enforce international tax avoidance.[42] India's Action 14 Peer Review Report features complaints by peer countries about the Indian tax authority's approach regarding the burden of proof in permanent establishment disputes.[43] Tørsløv et al. criticize policies that ease dispute resolution processes on grounds that they increase time administrations spend with correcting simple errors that redistribute income among high tax countries but do not affect MNE's tax burden globally. They claim that "by making it easier to correct transactions with other high-tax countries, mutual agreement procedures increase the opportunity cost of correcting transactions with low-tax countries. This allows tax-planning firms to shift more income to tax havens".[44] They conclude that there would be large savings of administrative resources if they just adopted a simpler approach (such as a formula) for allocating income and concentrating efforts on evasion. However, the evidence in section 6 suggests that beyond India Action 14 might have until now not been very effective in facilitating mutual agreement procedures.

Second, not elevating simpler rules as global standards makes it more costly for countries to enact them because frictions with other countries tax systems are higher. For example, formulary apportionment or alternative transfer pricing systems may more effectively prevent profit shifting strategies, even if adopted unilaterally. At the same time, however, they would likely increase possibilities of double taxation if other countries do not

41 Brauner, "Serenity Now! The (Not So) Inclusive Framework and the Multilateral Instrument," 19.

42 Pires de Oliveira, "Action 14 of the OECD/G20 Base Erosion and Profit Shifting Initiative: Making Dispute Resolution More Effective – Did Action 14 'Piggyback' on the Initiative?"

43 OECD, *Making Dispute Resolution More Effective – MAP Peer Review Report, India (Stage 1)*, 2019, 52.

44 Tørsløv, Wier, and Zucman, "Externalities in International Tax Enforcement: Theory and Evidence," 24.

adopt the same approach and do not grant tax credits if taxes were imposed in another jurisdiction based on such simpler rules.[45] Moreover, since tax treaties constrain countries to the arm's-length-principle, countries may be forced to run two parallel systems (one for investors from treaty countries and one for investors from other countries) with correspondingly high administrative costs for countries and investors.[46] In practice, the fact that countries do adopt simplified approaches, especially when considering how audits are actually conducted, could be seen as evidence that developing countries are not too concerned about these negative effects. Nevertheless, satisfactorily evaluating the argument would involve research that focusses on the countries from which investment originates. To what extent residence countries grant tax credits in cases where countries adopt such alternative solutions is an intriguing research question that could not be answered in the context of this study but that may be crucial for evaluating policy options for developing countries.

Third, a policy recommendation that is recognized as standard (even though strictly non-binding) may have the effect of legitimizing specific policies while delegitimizing alternatives, making it politically more costly for a government to use an alternative than in the absence of a standard. Political costs of using alternatives may increase both in the relation with other countries (e.g., in tax treaties) and in the domestic arena. Even though the revised version of the OECD Model Convention does not fundamentally change the allocation of taxing rights, countries are free to deviate from the Model Convention in their bilateral negotiations. Moreover, developing countries can argue that the UN Model Convention, which provides for more source taxing rights, should be used as basis for the negotiation. However, given that the BEPS Project endorsed a PPT (but a re-negotiation of source taxing rights only under specific conditions), it may be more difficult politically to undertake a more general re-negotiation with the partner country. By delegitimizing a shift to more source taxing rights, the political resources necessary to obtain such a deviation may increase for countries. The case of the attempted renegotiation of the Colombia – Spain double tax treaty could be interpreted in such a way (see section 0).

Implementing alternative solutions in the presence of a policy which is labelled as "standard" or "best practice" may also be associated with higher political costs in the domestic arena. A government might be in need to explain to other constituencies why it would not stick with an internationally agreed best practice and political adversaries might use the deviation to obtain other concessions. For example, domestic constituencies that benefit from less enforcement of international tax avoidance may find in the international standard an additional argument to convince the government

45 OECD, *OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2022*, 36.

46 Dagan, *International Tax Policy : Between Competition and Cooperation*, 176.

to abstain from blunter solutions as the evidence reviewed in section 5.5.5 suggests.

A common point among the critiques introduced until now is that they generally do not negate that international tax avoidance is an issue that developing countries should potentially address (if administrative resources permit it). The two other types of critiques of the BEPS project that are introduced in the following sections depart from that assumption.

Forcing developing countries to do something about BEPS although they may want to tolerate it for purposes of foreign investment attraction

One critique points out that the adoption of anti-avoidance measures by developing countries could lead to less investment because the tolerance of international tax avoidance may fulfil a similar function as tax incentives targeted at foreign investors. Rocha, for example, argued that some developing countries tolerated treaty shopping to enlarge their treaty network without negotiating treaties with all countries and may therefore not want to police treaty shopping.[47]

One may object that if countries are worried about a loss of competitiveness due to the introduction of anti-avoidance measures, they could simply provide statutory tax incentives for foreign investors or reduce statutory rates. Indeed, several authors and international organizations have hypothesized an inverse relationship between the fight against BEPS on the one hand and tax competition for real investment on the other.[48] However, proponents of the hypothesis acknowledge that "the substitutability between the statutory tax rate and instruments affecting avoidance opportunists that are constrained in BEPS-type fashion is likely to be less than perfect."[49] For example, a government might not be able to grant statutory incentives or tax reductions to foreign investors because of opposition in the parliament. Tolerance of avoidance would then achieve the desired result by circumventing this opposition. While such a strategy may at times be rational from the point of view of advancing specific economic goals, it should be pointed out that this is problematic from the point of view of democratic theory, since arguably a matter (granting a tax benefit) that would require parliamentary approval is decided without such approval.

An objection to this type of critique is that, as shown in section 3, the minimum standards of the BEPS Project do not even require countries to enforce international tax avoidance more than previously in order be considered as compliant. The architecture of the BEPS Project is rather geared towards ensuring that countries do not facilitate the erosion of

47 Rocha, "The Other Side of BEPS: 'Imperial Taxation' and 'International Tax Imperialism,'" 196.

48 Cui, "What Is Unilateralism in International Taxation?," 263; Keen, "Competition, Coordination and Avoidance in International Taxation," 220; Hong and Smart, "In Praise of Tax Havens: International Tax Planning and Foreign Direct Investment."

49 Keen, "Competition, Coordination and Avoidance in International Taxation," 223.

other countries' tax bases and that countries do not adopt too stringent approaches. For example, the standard on treaty shopping only requires countries to introduce an anti-avoidance rule if the other party requests it.[50] Since conduit jurisdiction would most likely not actively request this from a developing country source country, a developing source country without a regime for conduit companies would probably not be obliged to introduce a principal purpose test in any treaty that it has signed with a conduit jurisdiction. Moreover, the peer review of Action 6 does not aim at assessing whether a country is actively enforcing treaty shopping once an anti-avoidance clause has been introduced.[51] In a similar fashion, the minimum standard in Action 13 aims at ensuring that countries where large MNE's headquarters are located are supplying the countries where "their" MNEs operate with country by country reports (CbCRs). However, whether a country that received a report actually uses the information obtained is not assessed.[52]

Often the original argument charted above take their inspiration from India's policy with respect to the Mauritius treaty.[53] As discussed in more detail in section 0, tolerance of treaty shopping was a strategy that the Indian government ran for more than a decade and that at least a part of the Indian tax policy community considered as successful. However, this case study also showed that within India this policy was very controversial and that there is no clear evidence whether it was beneficial or not. The BEPS Project may have contributed towards shifting the balance in favour of a policy change, but the case study also showed that this was likely not the only factor.

Tolerating tax avoidance for the purpose of investment attraction may no longer be possible if because of the BEPS Project, all countries that are currently facilitating different forms of international tax avoidance had to close down the enabling tax regimes. However, this does not seem to be the case. The Netherlands, which was frequently used in treaty shopping

50 "Countries commit to adopt in their bilateral treaties measures that implement the minimum standard described in the preceding paragraph if requested to do so by other countries that have made the same commitment and that will request the inclusion of these measures." OECD, *Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, Action 6 - 2015 Final Report*, 19.

51 On the contrary, the terms of reference for the peer review contain the express statement: "If a jurisdiction is not itself concerned by the effect of treaty-shopping on its own taxation rights as a State of source, it will not be obliged to apply provisions such as the LOB or the PPT as long as it agrees to include in a treaty provisions that its treaty partner will be able to use for that purpose." (OECD, "BEPS Action 6 on Preventing the Granting of Treaty Benefits in Inappropriate Circumstances – Peer Review Documents," 12.)

52 On the contrary, the standard contains safeguards regarding the confidentiality of information received and regarding the use of the information.

53 van Weeghel, "A Deconstruction of the Principal Purposes Test"; Rocha, "The Other Side of BEPS: 'Imperial Taxation' and 'International Tax Imperialism'"; Baistrocchi, "The Use and Interpretation of Tax Treaties in the Emerging World: Theory and Implications."

structures,[54] has communicated that it would notify a treaty partner country about the lack of substance of a conduit company but would leave it up to the partner country to enforce the case.[55]

In sum, the arguments exposed in this section only hold if countries do more than what is strictly required to implement the minimum standards, since none of the more binding instruments of the BEPS Project requires countries to effectively enforce anti-avoidance measures or effectively levy more tax revenue. There is evidence that many countries do indeed more, but whether this should strictly be considered as effect of the BEPS Project is less clear.

Preventing developing countries from using tax haven features to develop themselves
Some (typically small) developing countries, such as Mauritius, Cayman Islands, etc. have developed offshore financial centres with laws that – among others – facilitated international tax avoidance strategies by MNEs as part of a strategy to develop their economy. For these countries, often labelled as "tax havens", the facilitation of tax avoidance or tax evasion elsewhere may be an important source of tax revenue.[56]

By agreeing to reforms through committing to the BEPS Project, such as introducing and monitoring substance requirements for companies that benefit from low tax rates, and agreeing to the insertion of anti-avoidance rules in tax treaties, these countries may lose economic activity and tax revenues. Particularly in light of the fact that developing offshore financial centres was sometimes among the development recommendations by international institutions such as the World Bank,[57] demands to reduce the offshore industry can be criticized from a development angle. Irish wrote in 1982 that "[Haven activities give the tax havens a measure of economic self-sufficiency they might not otherwise attain."[58] In addition, countries without corporate income tax need to spend administrative resources on monitoring substance requirements, although countries may have legiti-

54 Lejour, Möhlmann, and van 't Riet, "The Immeasurable Tax Gains by Dutch Shell Companies"; Weyzig, "Tax Treaty Shopping: Structural Determinants of Foreign Direct Investment Routed through the Netherlands."

55 Gerritsen and Kuipers explain: "The policy of the Netherlands is rather straightforward, however. When submitting a corporate income tax return, Dutch conduit companies that have invoked a tax treaty should indicate whether they fulfil the list of minimum substance requirements. If this is not the case, the Dutch Ministry of Finance will actively notify the treaty partner that the Dutch company has indicated that not all substance requirements were met in a particular year. It is then up to the source country to decide if and how this information is used. The Dutch Ministry of Finance believes it is not up to them to deny treaty benefits." Gerritsen and Kuipers, "The Post-BEPS Advantages of the Netherlands," 30–31.

56 Irish, "Tax Havens," 490–91.

57 Sharman, *Havens in a Storm*, 24.

58 Irish, "Tax Havens," 481.

mate reasons not to have a corporate income tax.[59] Most of the countries that are affected by these rules have a high GDP per capita today and thus no longer count as "developing countries", but whether their economies would survive a closing down of the tax avoidance business depends on how much the country has succeeded in diversifying its economy. In addition, by agreeing to the BEPS Project's standards, other developing countries may be prevented from attempting the same development path that offshore financial centres have taken in the future. Since this research focused on countries that have not tried to adopt such paths, this study can neither confirm nor refute this type of argument.

8.2.4 General objections to the critiques

Leeway provided by standards

When one considers only the strictly binding parts of the BEPS Project, i.e., the actions that countries need to undertake to be in compliance with the minimum standards and which are monitored by a peer review process, the strong concerns about the BEPS Project's content voiced by the critiques surveyed in the preceding section may not be valid. Adopting arbitration clauses in tax treaties, for example, is not part of the Action 14 minimum standard. Countries are not forced to adopt transfer pricing rules in domestic legislation, nor are they forced to sign (more) tax treaties with other countries, which may oblige countries to use the arm's-length-standard. Countries are not even forced to include a principal purpose test in their treaties with offshore jurisdictions, i.e., they do not need to effectively protect themselves from treaty shopping if they do not want to. While the lack of bindingness of the measures built into the process may affect the effectiveness of the BEPS Project in achieving its objectives, this flexibility may actually alleviate some of the concerns that were noted above.

Next to the flexibility in terms of the bindingness of the standards, there is flexibility in the timing of implementation. The case studies show that there have been important delays in compliance with some of the BEPS minimum standards, for example with respect to the introduction of country-by-country reporting or the ratification of the MLI. One interviewee from the Nigerian tax administration explained when comparing the 2015 BEPS Action plan with the more recent BEPS 2.0 Project: "Previous work has also been complex, however more of it could be managed because most of those you are allowed to develop your capacity and implement those you want to implement. That's the difference."[60]

59 E.g., if revenue needs can be covered through other taxes.
60 NG13

Simple solutions not necessarily better policy

Another objection could be that administratively simple solutions are not necessarily better policy and that the recommendations by the OECD are technically good in achieving desirable policy objectives, such as equitable treatment of different taxpayers, levying taxes on bases that best represent concepts such as "net income", or achieving capital import- or export neutrality. Many of the quotes in section 5 suggest that stakeholders in both private and public sector often consider approaches to tax avoidance that follow a finely delineating logic as good policy, and that only the timing of adaptation to these approaches is an issue.

Developing countries as residence countries

Finally, the critiques raised view developing countries mainly in their role as source countries, i.e., as recipients of investment, and criticize the BEPS Project's policies with regard to how they could affect developing countries' ability to tax or to forgo taxing foreign-owned multinational companies.

This makes sense since low-income countries are predominantly importers of foreign direct investment. Emerging economies such as India, Brazil, South Africa, but also smaller middle-income countries such as Colombia or Vietnam, are predominantly capital-importing countries, as well, but the imbalance is slowly reducing. Often, these countries already register a significant amount of outward investment primarily directed towards countries of the same or lesser level of development, and often undertaken by state-owned companies. In China, the probably most advanced among the group of emerging economies, the outward investment stock has started exceeding the inward investment stock in 2016,[61] it therefore already shares more characteristics with Western European countries or the United States, with consequences for its international tax policies.[62] All the developing and emerging economies that are in the focus of this dissertation, however, still have a significantly higher level of inward compared to outward investment.[63]

Nevertheless, even though the level of inward investment is higher than the level of outward investment, issues related to the taxation of outward investment are not necessarily irrelevant for developing countries. If it is accurate that the measures proposed in the BEPS Project strengthen taxation by residence countries, implementing them could still be beneficial for developing countries. While it is a debated question whether taxing foreign

61 UNCTAD Foreign direct investment: Inward and outward flows and stock, annual: https://unctadstat.unctad.org/wds , accessed on 02/09/2021

62 Hearson and Prichard, "China's Challenge to International Tax Rules and the Implications for Global Economic Governance."

63 Colombia, India, Nigeria, and Senegal had ratios of inward/outward FDI stock of 3.2, 2.5, 14.9, and 8.0 respectively in 2020. This means that in Colombia, for example, inward FDI stock was more than three times as important as outward FDI stock.

MNEs at high or low rates is beneficial from the capital importing country perspective,[64] the case for preventing avoidance by wealthy residents is clearer. For example, there is evidence that wealthy residents of Colombia and India made use of round-tripping structures to, for example, avoid capital gains tax upon sale of their business and defer personal income taxation.[65] According to a Colombian tax advisor, the CFC rules introduced in 2019 would contribute to reduce incentives to engage in this type of avoidance structure.[66]

8.2.5 The possibility to cherry pick

Overall, when it comes to policy recommendations, scholars do not suggest developing countries to abstain altogether from participation in the BEPS Project. Instead, they recommend participation, while cherry-picking the elements that are adequate. Oguttu notes that "there is a need for African countries to be associated with the OECD BEPS project, as it has the potential to put an end to tax avoidance by MNEs and so help to raise corporate tax revenues."[67] Rocha's overall advice is that: "Countries that have a sufficiently strong international tax policy can "cherry-pick" what is interesting for them in the Project and discard whatever recommendations seem inappropriate. Thus, the BEPS Project is an opportunity to participate in and engage in a high-level international taxation debate that is happening worldwide. However, for countries that are exposed to pressures from developed countries and do not have a well-formed international tax policy, it seems that the BEPS Project also poses a threat." If developing countries are indeed able to cherry pick, then a part of the criticism is less valid.

The evidence collected here suggests that countries indeed do not uncritically take over the results. To solve problems, they do not only rely on what the BEPS Project suggests. This is illustrated by the responses adopted to treaty shopping, which go beyond what was suggested by the BEPS Project in those countries where treaty shopping was a bigger problem.

On the contrary, developing countries may be able to free ride to a certain extent on the work financed by OECD member countries, as production of standards and policy recommendations is not costless.[68] Developing

64 Wallerstein and Przeworski, "Capital Taxation with Open Borders"; Margalioth, "Tax Competition, Foreign Direct Investments and Growth: Using the Tax System to Promote Developing Countries."

65 CO14, CO16, Jaiswal, "Foreign Direct Investment in India and Role of Tax Havens."

66 CO16

67 Oguttu, "Tax Base Erosion and Profit Shifting in Africa-Part 1: What Should Africa's Response Be to the OECD BEPS Action Plan?," 526.

68 Participation in the IF is connected to a fee, but the fee has not been set to recover the costs of the initial policy work.

countries could make use of the BEPS Project's policies but in a simpler and stricter way. They may help policymakers in pushing stricter measures through against domestic interests that do not want stronger measures.

One could object though that only non-OECD countries with market power are able to effectively cherry-pick. Based on the evidence of the case studies one could cautiously conclude that this is indeed the case, since in their approaches to transfer pricing, the legislated deviations from OECD practice have been somewhat more important in India and Nigeria than in Colombia and Senegal. Colombia, which faced the additional pressure of being an OECD accession candidate, probably went furthest in adhering to the OECD approach. However, when considering how rules are applied in practice, one could conclude that deviating from the ability to deviate from international standards is not limited to big and powerful developing countries. Because of its size and importance for MNEs, India may even have disadvantages since MNEs might exercise more pressure on the tax administration to conform.

Nevertheless, all countries studied in detail seem to have a relatively high policymaking capacity allowing them to evaluate which responses are in the national interests and which not. This may not be given for any country, in particular not for least developed countries.

8.3 The EU list of non-cooperative jurisdictions and the BEPS minimum standards

One of the main weaknesses of the critiques suggested until here is thus that the BEPS Project generally does not create many obligations for developing countries. However, as mentioned above, the fact that the BEPS Project elevates certain rules as standards has inspired the European Union to back them with strong incentives.

One of the goals of the EU is to coordinate policy of its Member States, both internally and externally, i.e., policies concerning the relation of Member States among each other and with third countries. With regard to the relations of Member States with third countries in the field of direct taxes, the EU's key documents are the 2012 "Recommendation to Parliament and Council on measures to encourage third countries to apply minimum standards of tax good governance" and the 2016 "External Strategy for Effective Taxation".[69] They lay out the general strategy of promoting "good tax

69 European Commission, "Communication from the Commission to the European Parliament and the Council on an External Strategy for Effective Taxation"; Mosquera Valderrama, "The EU Standard of Good Governance in Tax Matters for Third (Non-EU) Countries"; European Commission, "COMMISSION RECOMMENDATION Regarding Measures Intended to Encourage Third Countries to Apply Minimum Standards of Good Governance in Tax Matters."

governance" in other countries with the purpose of ensuring a global level playing field. The most important tool that gives this goal political force is the list of non-cooperative jurisdictions in tax matters, maintained by the Council's Code of Conduct Group and the defensive measures that member states apply against jurisdictions on the list.[70] The main criteria that affect whether a country will be considered as non-cooperative are adoption of three types of policy standards: Exchange of tax information, fair taxation (similar to the OECD's definition of "harmful tax competition"), and the minimum standards of the Base Erosion and Profit Shifting (BEPS) project.[71]

The list of non-cooperative jurisdictions has been criticized by academics, civil society groups, as well as by those countries that have been placed or could be placed on the list. Critiques raise different arguments: Too high administrative burden of complying with the criteria, lack of transparency of the process, political influence on the process, as well as hypocrisy (arguing that EU Member States should be on the list).[72] Quantitative studies argue based on the timing, a few countries may have joined the Inclusive Framework and committed to implement the BEPS Minimum Standards mainly because of the threat of being included on the list.[73]

The investigation of this dissertation can neither support nor refute these claims since all countries studied decided to adopt the BEPS project before any pressure was exercised by the EU. Nevertheless, the theoretical analysis of sections 3 and 4 suggests another argument: there is a lack of consistency between the Code of Conduct's objectives, the criteria that assess whether a third country's policy run counter these objectives, and the defensive measures that Member States are encouraged to apply against non-compliant third jurisdictions.

The stated aim of the list of non-cooperative jurisdictions is to "tackle tax fraud, evasion and avoidance" and to address "external challenges to EU countries' tax base".[74] The criteria for jurisdictions to be part of the list of non-cooperative jurisdictions is largely based on compliance with policies that are originally developed within the working parties of the OECD.

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70 Council of the European Union, "COUNCIL CONCLUSIONS on the Criteria for and Process Leading to the Establishment of the EU List of Non-Cooperative Jurisdictions for Tax Purposes."

71 Council of the European Union.

72 Yearwood and Nicholls, "The European Union's Economic Substance Rules in Commonwealth Caribbean Jurisdictions: What Is the Purpose?"; Koutsouva, "The European Union's List of Non-Cooperative Jurisdictions for Tax Purposes"; Mosquera Valderrama, "The EU Standard of Good Governance in Tax Matters for Third (Non-EU) Countries"; Fowler, "Will the EU Really Blacklist the United States?"; Langerock, "Off the Hook: How the EU Is about to Whitewash the World's Worst Tax Havens."

73 Collin, "Does the Threat of Being Blacklisted Change Behavior? Regression Discontinuity Evidence from the EU's Tax Haven Listing Process"; Oei, "World Tax Policy in the World Tax Polity? An Event History Analysis of OECD/G20 BEPS Inclusive Framework Membership."

74 https://www.consilium.europa.eu/en/policies/eu-list-of-non-cooperative-jurisdictions/

This is not surprising, given the large overlap of membership between OECD and EU. However, while the OECD does not attempt to enforce its policies upon third countries beyond persuading them that these constitute good policies and peer reviewing their efforts once they have signed up to them, the EU encourages its member states to adopt defensive measures and exercises pressure by publishing a list of non-compliant countries.

Defensive measures may be appropriate to the extent that non-compliance by third countries could lead to tax losses for EU Member States and to the extent these measures prevent such losses. In fact, many countries both within and outside the EU have for a long time maintained national tax haven lists and applied less favourable tax rules to transactions with taxpayers that are resident in jurisdictions on the respective lists (for example France, Italy, and Spain).

If another country offers a low-tax regime (without appropriate substance requirements) or fails to exchange information on potentially non-compliant taxpayers of another jurisdictions, defensive measures such as withholding taxes or limitations on deductions to limit potential tax losses for EU countries that could arise when EU residents make use of such third countries' tax provisions make sense: If appropriately designed, such measures can adequately disincentivize businesses and individuals from taking advantage of foreign tax regimes with the purpose of avoiding tax in the EU and restore the tax revenue lost to the EU. However, the Code of Conduct should not uncritically take over criteria, where non-compliance poses threats of a different nature. This is the case of most of the BEPS minimum standards.

As argued in section 3.3, some of the BEPS Minimum Standards are aimed at states that facilitate the erosion of tax bases elsewhere (mainly Action 5 and Action 6), but Action 13 (appropriate use and confidentiality criteria) and Action 14 are rather about ensuring that countries' responses to tax avoidance do not lead to double taxation or "over-taxation". The EU may have an interest in these objectives (for example avoiding competitive disadvantages for EU businesses), but the type of defensive measures contemplated may not be appropriate and not even effective in reaching these objectives.

Moreover, there is a mismatch between rhetoric about the list and its content. While the list of non-cooperative jurisdictions is presented as tool to fight tax avoidance and tax evasion,[75] its mechanism only partly aims at that goal, since some aspects of the BEPS Minimum standards arguably aim at ensuring that other countries do not levy too much tax in an inappropriate way on multinationals.

75 Council of the European Union, "COUNCIL CONCLUSIONS on the Criteria for and Process Leading to the Establishment of the EU List of Non-Cooperative Jurisdictions for Tax Purposes."

With regards to Action 6, even though if a third country fails to comply there could be a legitimate concern for the EU, the defensive measures proposed by the EU list are not appropriate. If a country refuses to introduce an anti-abuse rule in a treaty with an EU member state, the treaty itself would likely prohibit the application of the defensive measures. The power to apply withholding taxes, for example, is usually permitted only up to a certain level by the treaty and specific deduction limitations may be contrary to the non-discrimination article.

Finally, compliance with the Action 13 minimum standard on country-by-country reporting may become redundant for the EU when MNEs operating in the EU are required to publish them. Before that, the EU should take the fact into account that for the purpose of combatting tax avoidance compliance is much more relevant by those jurisdictions that host many MNE headquarters. Outside the EU this concerns mainly USA, China, Japan, India, and Canada.

It needs to be acknowledged that no country is or was listed on the EU blacklist only because of a failure to commit to implement the BEPS Minimum Standards. Countries on the list all have different shortcomings as well.[76] Indeed, as shown in section 3, for developing countries, peer reviews on actions other than Action 5 have often been postponed, and where reviews have been conducted these typically refrain from stating in clear terms if a country is non-compliant. It should also be noted that most countries on the UN's list of least developed countries are by definition excluded from the EU's listing exercise.[77]

Nevertheless, a failure to commit to BEPS is specifically mentioned in the Code of Conduct's reports, and the EU Council requested this commitment in letters sent out to third jurisdictions.[78] In addition, far-reaching reforms are planned for the future (although these seem to be currently blocked by Hungary and Estonia).[79] Since 2019, the Code of Conduct has sought commitment by member states to give more "teeth" to the Standard, by emphasizing that member states should apply a minimum amount of defensive measures. A resolution adopted by the European Parliament in January 2021 "Stresses the importance of BEPS minimum standards in the screening of third countries, in particular Actions 5, 6, 13 and 14; stresses the importance of identifying other BEPS standards to be included as listing criteria;"[80]

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76 Council of the European Union, "The EU List of Non-Cooperative Jurisdictions for Tax Purposes – Letters Seeking Commitment on the Replacement by Some Jurisdictions of Harmful Preferential Tax Regimes with Measures of Similar Effect."

77 European Commission, "Scoreboard of Indicators: Methodology," 2.

78 Council of the European Union, "The EU List of Non-Cooperative Jurisdictions for Tax Purposes. Compilation of Commitment Letters Received from Jurisdictions."

79 Van Gaal, "Hungary and Estonia Blocking EU Tax Reform."

80 European Parliament, "Reforming the EU List of Tax Havens: European Parliament Resolution of 21 January 2021 on Reforming the EU List of Tax Havens (2020/2863(RSP))," para. 16.

Before the Code of Conduct Group starts seriously assessing compliance with the BEPS Minimum Standards, the EU Council and the European Parliament should reconsider whether and to what extent BEPS standards should indeed remain part of the exercise. Similarly, before including new tax policy standards such as those currently developed in the Inclusive Framework under the "Two Pillar" framework,[81] a similar analysis like the one in the preceding paragraphs should be carried out.

81 In the 2021 Global Tax Symposium, Benjamin Angel, the Director General of EU TAXUD, mentioned that this might be considered. See https://www.youtube.com/watch?v=Cw-12dsGec8&list=PLrARaVLmTNT9oxSqNGubUZ92_k8YGUFBq at 4:18:00