United Nations

Financing for Development

**Economic and Social Council**
**Special Meeting on International Cooperation in Tax Matters**
**Trusteeship Council Chamber/Virtual, 8 April 2022**

***Official Summary by the President of ECOSOC***

1. The Economic and Social Council (ECOSOC) convened its 2022 Special Meeting on International Cooperation in Tax Matters on 8 April. The Meeting focused on critical international tax topics in the context of the COVID-19 pandemic and recovery. Participants addressed: (i) the future of corporate taxation, examining changes introduced in the 2021 UN Model Double Taxation Convention between Developed and Developing Countries (UN Model) and the G20-led OECD/Inclusive Framework initiative on a two-pillar solution to address the tax challenges of the digitalized and globalized economy; and (ii) efforts and effective ways to tackle tax-related illicit financial flows for sustainable development, with emphasis on the extractives sector.

2. The Meeting took place in parallel with the 24th Session of the UN Committee of Experts on International Cooperation in Tax Matters (4-7, 11-12 April). It brought together UN Member States and Observers, including senior officials of national tax authorities, members of the UN Tax Committee, and senior representatives of relevant international and regional organizations, civil society, business, and academia, for action-oriented exchange of views and best practices on international tax issues.

**Key messages**

i. The **rules governing the taxation of cross-border** investments and economic engagement **need to keep pace with changes in modern business and technology** to ensure effective taxation of economic activity and value creation **rules that remain workable for all countries**.

ii. As countries decide on their own path in taxing the globalized and digitalized economy, **more action is needed to ensure inclusive norm-setting**. International discussions should consider how economies in different stages of development and with diverse tax systems are affected by tax reforms; and new rules should be devised in a way that all countries can easily implement and administer them.

iii. The proposed OECD/Inclusive Framework two-pillar solution is viewed by many developing countries as complicated and not sufficiently responsive to their needs. They prefer the **simpler and more administrable approaches included in recent changes to the UN Model**, which are proposed to be implemented more broadly through a potential multilateral instrument.

iv. Beyond being a drain on public finances, illicit financial flows **destroy trust, tax morale,** and, eventually, state-building. Although multinational enterprises frequently reap large profits from mining extractives in developing countries, **tax avoidance and other illicit financial flows undermine domestic resource mobilization**; meanwhile, in many cases, the projects themselves are detrimental to the lives, labour, environment and general development of the host countries.

v. Reducing illicit financial flows depends on providing **access to information** held in other countries regarding income and capital flows. This information is particularly important for **developing countries**. Still, they **often are unable to meet technical requirements** to join international efforts and therefore **do not benefit from recent advances in tax transparency.**

vi. An **integrated approach** to tackle illicit financial flows must involve **bold policy measures** at the global level and assist national tax administrations in improving implementation, mainly via **capacity building and human resource strategy**.

vii. The UN's multidisciplinary mandate and global convening power enable it to serve as an equitable platform for all countries and stakeholders to engage with each other to form **a global pact to tackle illicit financial flows**.

## I. Introduction

3. In the current context, where multinational enterprises use innovative and complex business models, companies can sell products across borders without maintaining a presence on the ground. This has begged the question whether corporate tax regulation is keeping pace with these changes, which have only accelerated in the context of the COVID-19 pandemic. Hence the increasingly urgent call for reform of the tax rules to address the challenges presented by new business models. At the same time, there is heightened awareness that such reform must pay special attention to developing countries and their realities in order to reduce, rather than increase, global inequalities.

4. Illicit financial flows present all countries with a significant challenge to domestic resource mobilization. Illicit financial flows drain the resources needed by governments to help finance sustainable development. Countries need to increase efforts to reduce illicit financial flows, with the aim of finally eliminating them. International cooperation is critical in addressing illicit financial flows. A key area of action is embracing the transparency and information exchange mechanism. Multilateral cooperation should include support for countries in detecting and reducing cross-border tax evasion, eliminating shell companies, and strengthening anti-money laundering laws and practices.

5. Reforming international corporate taxation is a key requirement to emerge effectively from the pandemic and accelerate the transition to equitable, sustainable and resilient growth models. There is an urgent need for a new social contract between companies, governments, and citizens that includes progressive taxation as a foundation of sustainable development.

6. In an increasingly digitalized and globalized economy, it is essential to ensure an equitable distribution of revenues among market jurisdictions where economic activity occurs, often within developing countries. As countries continue to determine and evaluate the options available to them, it is important for them to consider their own specific realities and situations to achieve fair and effective tax systems.

7. This reform is critical especially in developing countries endowed with natural resources. This sector has too often been plagued by illicit financial flows and regressive taxation, contributing to the so-called "paradox of plenty," where states rich with natural resources nevertheless experience poor economic growth and an increased likelihood of violent conflict.

8. For the extractive industries to successfully contribute to sustainable development, key conditions must be met that require greater international cooperation on tax issues. First, governments need to improve environmental sustainability, transparency, inclusive decision-making and accountability. This includes investing rents from extractives in the sustainable development of local communities and populations. Second, countries need to diversify their economies and reduce dependence on revenues from extractive industries over time by exploring innovative domestic resource mobilization mechanisms.

9. The UN Tax Committee aims to help countries mobilize domestic resources for sustainable development by broadening their tax bases, strengthening tax administration, and helping curb tax avoidance and evasion. The Committee has identified new areas of work that will support domestic resource mobilization, including work streams on wealth and solidarity taxes, health taxes, and (other) indirect taxes. The current challenges that the world is facing influence the work of the Committee and how that work is conducted in order to produce targeted and practical guidance highly relevant for developing countries. The Committee has generated a wealth of tools and products to support country efforts to achieve the sustainable development goals (SDGs). Those products include updating the

provisions on tax treaties, guidance on transfer pricing, carbon taxation, and tax treatment of government-to-government aid projects.

10. The UN Tax Committee has also introduced dynamic provisions, expanding source states' taxing rights on business profits generated by non-resident enterprises in those jurisdictions. Most recently, the Committee designed and introduced a new Article 12B in the UN Model, which deals with the taxation of automated digital services. The ability to conduct business remotely without being subject to tax on income generated from such activities in market jurisdictions is one of the most significant challenges currently faced by the tax world, with important implications for sustainable development.

## II. The future of corporate taxation in a digitalized and globalized world

11. The way that multinational enterprises organize themselves is constantly changing. In the past, business models involved moving from centralized to more decentralized structures, with business functions and segments being situated in different jurisdictions. However, newer business models that take advantage of advanced technologies allow multinational enterprises to generate income in countries despite having little or no physical presence there. Under most bilateral tax treaties, the lack of physical presence prevents the source countries from taxing the relevant income. This encourages centralization in low-tax jurisdictions.

12. This reality has led to concerted efforts to reform the global corporate tax framework to keep pace with changes in modern business and technology and respond to long-standing calls by developing countries to allow effective taxation by all jurisdictions of value created within their borders. Discussions in the international tax arena have proposed approaches for consideration by countries to address the taxation of income generated without a physical presence. One approach is the two-pillar solution, as developed at the Inclusive Framework level. Another is the new Article 12B of the UN Model, developed by the UN Tax Committee to address the taxation of income from automated digital services in bilateral situations.

13. The development of the two approaches reflects increased international tax cooperation. Some participants expressed optimism regarding the role of developing countries in the negotiation of the two-pillar solution. Others underscored that not all UN Member States participate in the Inclusive Framework. For example, approximately two-thirds of least developed countries (LDCs) (making up almost half of the members of the Group of 77 and China) are not part of the Inclusive Framework.

14. This lack of representation affects the substantive results. Although the two-pillar framework recognizes the contribution of markets in value creation, developing countries continue to call for a greater allocation of revenues to those market jurisdictions. For any meaningful redistribution of tax revenues to be achieved, streamlined distributional analyses of the impact of the two-pillar solution must be undertaken. Participants observed that a significant portion of additional tax revenue will go to developed countries that are the headquarter countries of multinational enterprises instead of lower-income countries. Furthermore, the proposed minimum corporate tax rate of 15 per cent is much lower than the statutory corporate tax rates of many developing countries. For instance, most African countries have higher rates, generally ranging between 25 per cent to 35 per cent.

15. Other common challenges faced by developing countries in the tax area, such as access to information, the complexity of the proposed international tax rules, and the ability and cost of administration, have not been sufficiently addressed during deliberations over the two-pillar solution. Participants stressed that the proposed rules should not exacerbate the existing strains on technological infrastructure and human capital. Countries that do decide to adopt the new rules will need technical support in implementing them.

Financing for Development

16. Developing countries need simple and easily administrable approaches to taxing multinational enterprises, such as expanded withholding taxes. Such rules have been adopted in the UN Model and are central to the UN Tax Committee's new work stream to draft a multilateral instrument that would allow countries that want to adopt such approaches to more quickly amend multiple existing bilateral treaties that currently prevent the imposition of such withholding taxes.

17. For developing countries to participate on an equal footing in devising rules for international tax governance, they must have a leadership role in forums in which global tax policy deliberations and rulemaking take place. A principled approach would be to rotate leadership in intergovernmental tax policymaking bodies. More fundamentally, it is essential to support developing countries in enhancing their capacities, including human resource capacity, to participate effectively in international tax norm- and policy-shaping and evaluation of proposed rules reform and in the relevant forums.

18. Developing countries need to take proactive steps to ensure that they have an effective voice in international deliberations that result in norms that impact their revenue mobilization efforts. They are encouraged to leverage their collective views in international discussions, as done by the African Tax Administration Forum (ATAF) and by the Group of 24 in the discussions of the two-pillar solution. There is also the need to increase the engagement at the political level of developing countries to create political awareness of the implications of new international tax rules.

19. All in all, the Meeting noted that the shift toward strengthened international tax cooperation is promising. There is a long journey ahead to navigate, define, and implement any solutions to the changing business models. To be fair and ultimately to be effective, this process needs to systematically include the considerations of all countries.

## III. Tackling tax aspects of illicit financial flows for sustainable development

20. The COVID-19 pandemic and its impacts and the prevailing global conflicts have brought heightened urgency to efforts to ensure the financing of the SDGs. These crises have placed a strain on financial integrity and resource mobilization, both of which are key factors in eradicating poverty and inequality. Developing countries, which already faced difficulties in their resource mobilization endeavours, remain vulnerable and in need of innovative ways and stepped up support to strengthen and reform their tax systems for greater effectiveness and resilience.

21. Against this backdrop, illicit financial flows stand out in their depriving developing countries of their wealth and driving them to adopt less favourable financing options. This is particularly prevalent in the context of developing countries' extractive industries and trade in natural resources. Although multinational enterprises frequently reap large profits from mining extractives in developing countries, tax avoidance and other illicit financial flows undermine domestic resource mobilization. In many cases, the projects themselves are detrimental to the lives, labour, environment and general development of the host countries, further undermining efforts to achieve the SDGs.

22. The High-Level Panel on International Financial Accountability, Transparency and Integrity for Achieving the 2030 Agenda (FACTI Panel) has underscored the need for integrated approaches for tackling illicit financial flows. The Panel has urged countries to align in order to establish a normative framework that directly responds to illicit financial flows. A comprehensive solution is needed, premised on upholding financial integrity: a change in mind-set that focuses on the intention of the law and a whole-of-government approach emanating from political commitment at the top.

23. Much has been done in recent years to reduce the secrecy that abets illicit financial flows, for example, at the Global Forum on Transparency and Exchange of Information for Tax Purposes. In terms of technical solutions, ensuring transparency through information sharing is crucial. Participants gave

examples of some developed countries (such as Finland) illustrating how certain tools – such as real-time sharing of information, engagement of stakeholders in the private sector, whistle-blower channels and increasing capacity to manage bigger databases – have substantially contributed to tackling illicit financial flows.

24. Still, much remains to be done. A case in point is the information asymmetry that persists between developed and developing countries. Developing countries often do not have access to information held by developed countries that could aid them in addressing illicit financial flows. There is a need for further cooperation to facilitate the return of assets to developing countries.

25. Strategies to attack illicit financial flows must be tailored to the specific problematic behaviour. As participants noted, it is commonly held that such flows take two forms: those derived from criminal activity, such as human trafficking, and those related to tax avoidance and evasion. Although both forms undermine financial integrity, they need to be addressed in different ways. For example, tax auditors, who are trained to uncover tax avoidance and evasion, are not necessarily equipped to deal with illicit financial flows arising from criminal activity.

26. Furthermore, developing countries require additional support in capacity building and guidance for tackling illicit financial flows, including in specialized areas, such as the interaction between tax and financial crimes. Regarding capacity building, developing countries' tax administrations require trained personnel responsible for information sharing processes, such as Country-by-Country Reporting. Developing countries should also adopt human resources practices that enable successful career paths in countries' revenue departments to support retention in public service of officials and experts with the relevant experience. The UN Tax Committee's work on digitalization of tax administrations and increasing tax transparency supports such efforts. Developing countries also may look to regional integration for purposes of strengthened collaboration in combating illicit financial flows, sharing of best practices and mutual support.

27. Addressing illicit financial flows requires tackling the imbalance in the international financial and trade systems. Curbing such flows at national and regional levels requires confronting weak institutions that have prevented countries from exercising the necessary ownership over economic and financial flows, such as managing natural resources, particularly in the extractive industries. Development of a global pact addressing illicit financial flows would provide all countries an equal opportunity to contribute and shape normative guidance. The UN's multidisciplinary mandate and global convening power present it as the most equitable platform for all countries and stakeholders to engage with each other and to form such a global pact for tackling illicit financial flows.

## IV. Conclusion

28. Multilateral institutions are key in driving successful international tax cooperation. The role and efforts by the United Nations, the OECD, the IMF and the World Bank (separately and together at secretariat level as the Platform for Collaboration on Tax (PCT)), regional tax organizations and other stakeholders are notable. For years, they have supported developing countries in their ability to overcome the challenges and impacts of the digitalization and globalization of the economy and, as partners, improve the livelihoods of the citizens they represent. They have pushed to strengthen the capacities of public officials while fighting aggressive tax planning and safeguarding adequate flows of foreign direct investment for sustainable development. Governments, private investors, business, academia, civil society, and other key stakeholders also play a significant role in the discussions at the international level.

29. Capacity support and development is an overarching theme in order for countries to effectively deal with tax challenges from the digitalized and globalized economy and to tackle tax-related and other illicit financial flows. UN-DESA continues to reach developing countries through its capacity

development program, aptly disseminating the practical guidance developed by the UN Tax Committee in the context of wider support to help countries mobilize and manage diverse sources of financing for development, while also addressing systemic issues. Member States are encouraged to make contributions to help fund the Committee's work and UN-DESA's capacity development activities to ensure strengthened support for developing countries. These efforts will go a long way in ensuring preparedness by tax and other government officials to deal with complex issues that might result in the erosion of their tax bases.

30. The innovative and practical solutions to the challenges highlighted at the Special Meeting may counter the effects of the recent events that have slowed down efforts to mobilize domestic resources, in particular in least developed and other developing countries. Addressing the identified challenges will assist the development of fair and effective tax systems domestically and internationally for sustainable development, while also strengthening global partnerships and cooperation for achieving the SDGs in their totality.

* * * * *