Emerging Globalities and Civilizational Perspectives

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Redefining Global Governance

A Tax, Trade and Investment Perspective in the EU and beyond

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Emerging Globalities and Civilizational Perspectives

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This series documents the range of emerging globalities in the 21st century at the national, transnational and trans-civilizational levels of analysis. “Globality” refers to a global condition where people located at any point on Earth are aware of being part of the world as a whole---the world as a single interacting entity. Social interactions occur among actors belonging to different societies, different social strata and different cultural traditions so that the condition of “globality” is experienced in many different ways.

Examples of emerging globalities are social movements generated from the unfulfilled promises of neoliberalism and feelings of discrimination and marginalization of lower social strata; cultural otherization or the blaming of economic problems of certain geographical areas on a low level of cultural development; insecurities generated by technological risks, epidemics, and global terrorism; uncertainties generated by processes of transnational governance, outsourcing, unbalanced trade and massive migrations; biology-machine interfaces and impacts of non-human organisms and technologies on human consciousness and action; long-term threats of global warming, climate change and depletion of bio-diversity; increasing exploitation and marginalization of less industrialized regions.

We state that globalization entails encounters and often clashes among people and nations of different civilizational traditions. Hence, one of the exploratory questions of these volumes will be the extent to which negative or problematic globalities are reactions to failed promises and unrealized ideals of civilizational and national traditions and/or perhaps attempts to revive those traditions. Our notion of civilizational tradition takes inspiration from the classical works of Spengler and Toynbee, Benjamin Nelson, Vytautas Kavolis, Roland Robertson, Johann P. Arnason, Jeremy Smith, and others; a tradition which is in sharp contrast with the civilizationism recently promoted by authoritarian leaders with hegemonic ambitions. The volumes in this series aim to extend the inter-civilizational focus of classical civilizational thinkers from the analysis of the origins and development of civilizations to the fostering of contemporary inter-civilizational dialogues; the intent is to facilitate an international rapprochement in the contemporary atmosphere of global conflicts.

The volumes will reflect the diversity of theoretical perspectives and captures some of the novel thinking in social sciences, economics and humanities on intra- and inter-societal processes; the attention to novel thinking will extend to emerging policy formulations in dealing with threats, risks, insecurities and inequities and to strategic thinking for a sustainable global future. The historical perspective will also be an important component of analysis together with the avoidance of West-centric perspectives. The intended readership of this series is not just an academic audience but also policy decision-makers and the public at large; accessibility of language and clarity of discourse will be a key concern in the preparation of these volumes.

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Introduction to Volume

The Common Global Governance Challenges of Tax, Trade, and Investment

The interconnected nature of the global economy ensures that there are no clear boundaries between the realms of tax, trade, and investment law. Instead, every nation state confronts a bewildering mix of policy choices across these regulatory areas as well as various constraints on the ability to achieve national policy priorities. Every cross-border business or investment decision accordingly involves navigating a web of overlapping regulatory regimes characterized as much by conflict as coordination.[1]

Following geo-political and socio-economic distinctions among states established decades and even centuries ago, today's dominant trends in transnational institution building and standard and rule-setting across tax, trade, and investment reflect deeply inconsistent historical and contemporary aims and capacities of political leaders. The confluence of both interdependence and incompatibility among tax, trade, and investment law institutions and instruments around the world produces constant conflict and renegotiation regarding the terms of cross-border cooperation across states. The way we understand and resolve these conflicts among regulatory areas and across states deeply impacts the livelihoods of individuals around the world as international agreements direct and shape the movement of goods, services, and capital. The rise of digital giants such as Amazon and Google

[1] These national interests and overlapping regulatory regimes can raise protectionism and/or disputes in tax, trade, and investment. This topic has been discussed extensively in literature, see, for instance, Chaisse J, Dimitropoulos G. Domestic Investment Laws and International Economic Law in the Liberal International Order. World Trade Review. 2023;22(1):1–17. doi: https://doi.org/10.1017/S1474745622000404. See for an analysis of these interlinkages and public international law, special section Asia Pacific Law Review including introductory article by Julien Chaisse & Irma Mosquera (2022): Public international law, international taxation and tax dispute resolution, Asia Pacific Law Review, DOI: https://doi.org/10.1080/10192557.2022.2102585, accessed 4 June 2024.

has only underscored the complexities involved as both companies and nation states use and manipulate rules and standards to achieve sometimes congruent and sometimes incongruent goals.

As a result, understanding the complexities of the intersecting fields of tax, trade, and investment law is crucial. Policymakers, legal practitioners, academics, and business leaders must navigate through these challenges to strike a balance between competing interests, achieve equitable outcomes, and promote sustainable development. The goal of this book is accordingly to introduce and explore these complex interactions and to analyze how the convergence of these three key international legal areas influences global patterns of economic development and shapes the way nations compete and collaborate on the world stage.

This book contributes to enhancing interdisciplinary exchange regarding the common global governance challenges of tax, trade, and investment. These governance challenges are the result of the shifting of power to tax from the national to the international level as has been described, among others, by Rixen et al in *Global Tax Governance: What It Is and Why It Matters*.[2] Scholars, countries, and organizations have addressed the topic of global governance from national, regional, and international perspective.[3] In addition, the European Union plays a key role in global governance by introducing harmonizing legislation and guidance, including the EU Standard of Tax Good Governance into economic, trade, and strategic partnership agreements.[4] Further, current developments in international tax law such as the 2013 Project initiated by the OECD to tackle base erosion and profit shifting (BEPS)[5] have been regarded by countries and organizations as an example of how to achieve consensus in multilateral tax settings that may shape and inform trade and investment governance.[6]

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[2] P. Dietsch, and T. Rixen, T., "Global Tax Governance: What It Is and Why It Matters," in P. Diestsch and T. Rixen, eds, Global Tax Governance: What is Wrong With It and How To Fix It (Rowman & Littlefield/ECPR Press, 2016), 3.

[3] The topic of global tax governance has been addressed by the editors of this book elsewhere. See, e.g., Mosquera Valderrama, Irma, "Global Tax Governance," in Florian Haase, and Georg Kofler (eds), The Oxford Handbook of International Tax Law, Oxford Handbooks (2023; online edn, Oxford Academic, 23 Oct. 2023), https://doi.org/10.1093/oxfordhb/9780192897688.013.59, accessed 4 June 2024.

[4] See Chapter 15 of this book and also Mosquera Valderrama, Irma. 2019. "The EU standard of good governance in tax matters for third (non-EU) countries". Intertax. Vol 47(5).

[5] The BEPS Project has been initiated by the OECD with the political mandate of the G20, and it has currently 15 Actions including 4 Minimum Standards, 10 Best Practices, and 1 Multilateral Instrument. As of June 2024, more than 145 tax jurisdictions have committed to implement the 4 Minimum Standards and more than 100 jurisdictions have signed and ratified the Multilateral Instrument. See Chapter 3 of this book.

[6] "The main argument is that the BEPS Project shows that despite tax sovereignty, solutions to the problems of taxation can be addressed throughout multilateral settings developed by the OECD and the G20. Therefore, other organizations that are struggling with seeking multilateral solutions in areas such as trade and investment can also follow the BEPS model to achieve global consensus, for instance, at the WTO and UNCITRAL level". However, the current UN discussion for a Framework Convention to achieve truly and inclusive multilateralism has raised new questions on

Contribution of this Book

One contribution of this book is the study of the interlinkage between this shifting of power in global governance and how this shifting of power has been addressed from a tax, trade, and investment. Therefore, in this book, we revisit the conceptual foundations of global governance and re-examine the roles played by different actors including the United Nations, regional international organizations, the OECD, non-governmental organizations, and multinational corporations in achieving global governance.

A vital part of the production of the book was a weeklong workshop, *Redefining Global Governance: A Tax, Trade and Investment Perspective in the EU and Beyond*, organized in June 2023 at the Lorentz Center in Leiden, the Netherlands.[7] As the title of the workshop and this book suggests, while acknowledging the role of the EU, beyond dominant debates which focus on the perspectives of developed countries, we sought to engage experts in more balanced policy discussions taking into consideration the unique concerns of developing countries. Over the course of five days, 28 participants from different parts of the world came together in person to discuss edge-cutting global governance issues including: tax evasion and avoidance, sustainable economic development, the role of technology, national security, digitalization, dispute settlement, and policy convergence.

Several of the book chapters were presented at this workshop in their early forms. In light of the discussions that took place during this workshop, we invited scholars at the early and later stages of their careers and with different backgrounds in tax, trade, and investment law, to contribute to this book. The result is a comprehensive book with 19 chapters addressing four overarching themes. The themes are divided into four parts.

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the success of these multilateral solutions. See Mosquera Valderrama, I. (2024). How Can Regional Cooperation Help the Enhancement of Regional Economic Development and Strengthen the Voices of Developing Countries in Global Tax Negotiations?. The Journal of World Investment & Trade, 25(2), 201-236. https://doi.org/10.1163/22119000-12340323 at 228, 235, accessed 4 June 2024.

[7] The organization of this workshop was supported by the Lorentz Center and the Netherlands Institute for Advanced Studies (NIAS). This workshop and the open access funding for this book were also supported by the GLOBTAXGOV Project (2018–2023) funded by the European Research Council (ERC) under the European Union's Seven Framework Programme (FP/2007–2013) (ERC Grant agreement n. 758671) and the EU Jean Monnet Chair EUTAXGOV funded by Erasmus+ Programme (Grant agreement n. 101047417).

A report of the workshop is available at the GLOBTAXGOV blog at https://globtaxgov.weblog.leidenuniv.nl/files/2023/08/Redefining-Global-Governance_Scientific-Report-31-July-2023.pdf accessed 4 June 2024.

Short Summary of the Chapters of this Book

Part I, **The Tax, Trade, and Investment Governance Landscape,** introduces readers to the complex governance aspects of tax, trade, and investment regimes. It examines the challenges states face when navigating conflicting policy choices and demonstrates how national policies intersect or conflict with international obligations. The five chapters in this part explore governance issues, including the struggle of lower-income states to have their concerns addressed in international arenas and the interplay between national tax and investment policies.

Chapter 1 "Introduction to Part I" introduces this Part and provides an overview of the themes reflected in its chapters. In Chapter 2, "A Survey and Critique of International Tax Governance Reform", Karen Brown explores the governance problems faced by lower-income states in international tax policymaking, highlighting the dominance of the OECD and advocating for more inclusive global tax governance. In Chapter 3 "International Tax and Investment Policy: Navigating Competing Demands", Katharina Kuhn examines the challenges national policymakers face at the intersection of tax and investment policy, including the trade-offs between attracting foreign direct investment and complying with international tax best practices. In Chapter 4 "The Tax Carve-Out Clause in International Investment Law", Paloma García Córdoba discusses the evolving relationship between taxation and international investment agreements, focusing on the language and purpose of tax carve-out clauses and their impact on the relationship between investment law and tax law. Sharon Waeytens closes out this Part with Chapter 5 "Tax and Trade and Investment Instruments in Sustainable Development Goals Achievement", which explores how tax, trade, and investment policy instruments can contribute to achieving the Sustainable Development Goals and the importance of policy coherence in this process. Together, these chapters provide a comprehensive overview of the legal, social, economic, and distributive aspects of contemporary international economic law and policy.

Part II, **Global Tax Governance: Transparency, Fairness, and Regulation,** presents an analysis of the link between global tax governance and converging tax, trade, and investment regimes. It highlights the influence of these regimes on evolving international governance structures and emphasizes the foundational pillars of transparency, fairness, and regulation in promoting equitable economic practices worldwide. Through detailed examinations of beneficial ownership transparency, treaty shopping, and tax policy fairness, this part underscores the importance of creating a coherent and fair international tax system that enhances global economic stability.

Julien Chaisse provides an introduction to this Part in Chapter 6 "Introduction to Part II". In Chapter 7, "Competition and Complementarity of EU and FATF Beneficial Ownership Transparency Orders", Leyla Ates, Andres Knobel, Florencia Lorenzo, and Markus Meinzer analyze the relationship between the European Union and the Financial Action Task Force regarding beneficial ownership transparency, assessing collaborative or competitive efforts to improve transparency. In

Chapter 8 "Dealing with Treaty Shopping Across the Tax, Trade, and Investment Regimes", Frederik Heitmüller examines the practice of treaty shopping within and across tax, trade, and investment realms, focusing on policy synchronization and multilateral approaches to manage this issue effectively. In Chapter 9 "Hidden Dynamics and Hierarchies in Tax Policy: A Critical Assessment of Fairness in OECD, EU, and UN", Ezgi Arik analyzes different conceptions of fairness by intergovernmental organizations and highlights the need for a globally recognized definition of fairness in international tax policy. In Chapter 10 "Transparency and Transformation: Rethinking Tax Governance in the Mining Sectors of Tanzania and Kenya", Anne Wanyagathi Maina focuses on tax transparency in the mining sector, evaluating global initiatives and national reforms to improve governance and combat corruption in the extractive sector.

Part III, **Interactions and Overlaps Between Tax, Trade, and Investment Policies,** focuses on the interlinkages among tax, trade, and investment policies using case studies and examples of relevant legal texts to illustrate how these interactions play out in practice. It explores how international investment agreements can affect tax policy and the potential for duplicative disputes across double taxation conventions and investor-state dispute settlement provisions. The part also discusses unique cases, including a trade-based side agreement between Australia and India that overrides a double tax convention, which provide rich detail regarding the complexities and potential conflicts in these intersecting legal fields.

Frederik Heitmüller provides an introduction to this Part in Chapter 11"Introduction to Part III". In Chapter 12, "The Interaction Between IIAs and DTCs: Potential for Overlap and Reform Proposals", Javier Garcia Olmedo discusses investor-state dispute settlement (ISDS) cases related to tax measures, examines the overlap between investment treaties and double tax conventions, and proposes potential reforms. In Chapter 13, "The Intersection of Treaties on Tax and Trade: A Case Study of Australia and India", Sunita Jogarajan and Tania Voon analyze a unique trade discussion between India and Australia, focusing on a side agreement that appears to override an existing double tax convention and examining the implications of this override for international trade and investment policy. In Chapter 14, "The Legal Transplant of EU Standards in Taxation: A Case Study of the ACP Post-Cotonou Agreement", Irma Mosquera and Filip Debelva discuss the Post-Cotonou Agreement, highlighting the potential legal transplant of EU standards and the compatibility of its provisions with existing tax, trade, and investment agreements.

The fourth and final part of the book, **Reforming Global Governance,** addresses ongoing reforms in global governance at the international, regional, and domestic levels. It explores challenges for policy coherence arising from the persistent popularity of tax incentives, including in furtherance of green transition goals, as well as proposed designs and prospects for better decision-making through new regional (particularly African and Latin American) and international governance structures, including the rationale and likely impacts of the elevation of the United Nations in international tax law-making. Through these discussions, it outlines the potential pathways for future reforms in global governance that take a holistic approach to

address tax, investment, and trade issues while considering the differences between developed and developing countries.

Irma Mosquera opens this Part with an introduction in Chapter 15 "Introduction to Part IV". In Chapter 16, "Optimizing Policy Synergies: The Role of Tax Incentives in International Trade and Investment", Julien Chaisse examines the impact of tax incentives on trade and investment, providing insights into designing tax incentive regimes that balance international legal frameworks with national policy objectives. In Chapter 17, "Tax, Trade and Investment for Green Transition", Suranjali Tandon addresses the need to balance tax incentives and carbon pricing to encourage a green transition, analyzing instruments such as the EU's Carbon Border Adjustment Mechanism and the Inflation Reduction Act. In Chapter 18, "Breaking the Cycle of Domination in Global Tax Governance: Africans Defying Asymmetries and Seizing Opportunities", Lyla Latif discusses the role of African nations in global tax governance, highlighting their proactive participation in international tax discussions and advocating for equitable treatment. And finally, closing out the book, in Chapter 19, "Decision-Making in a Proposed African Union Tax Governance Structure", Afton Titus argues for creating an institutional structure within the African Union to address international tax challenges and coordinate policies to deal with these challenges effectively.

Concluding Remarks and Main Findings

Throughout these twenty chapters, this book demonstrates the difficult trade-offs today's policymakers continue to face in articulating and achieving domestic and international economic goals. It explores how political leaders grapple with a lack of coherence across global regulatory areas that has been forged and facilitated through a history of policy divergence and incoherence as well as deep and persistent inequities among states. A key theme throughout the book is the struggle of lower-income states to address their concerns in global regulatory arenas through decades of institution building around cross-border coordination that has consistently been characterized by policy designers and architects as projects that sought prosperity for all. Consequently, many chapters take issue with the continued dominance of highly developed countries, which is especially prominent in international tax policymaking, and call for a reconstitution of governance structures to include meaningful input across disparate socio-economic regions.

The chapters of this book contribute to policymaking at the domestic, international, and regional levels as well as to academic debate. Throughout the chapters, the authors express their key findings and concerns in dealing with global governance from a tax, trade, and investment perspective. These key findings will serve to enhance the debate on global governance by international organizations, regional organizations, supranational organizations (EU), developed and less developed countries, and scholars.

The first of these key findings is that there is a need to question past global governance choices including the role played by international organizations such as the OECD vis-à-vis less developed countries. For this purpose, some of the authors in their chapters highlighted the need to create a specific institutional structure that facilitates proactive participation of countries including less developed countries in international tax negotiations (Chapters 2—"A Survey and Critique of International Tax Governance Reform", 18—"Breaking the Cycle of Domination in Global Tax Governance: Africans Defying Asymmetries and Seizing Opportunities", and 19—"Decision-Making in a Proposed African Union Tax Governance Structure"). Further, the role of the EU as a standard-setter vis-à-vis non-EU countries was addressed through a case study of the EU-ACP Post-Cotonou Agreement (Chapter 14—""The Legal Transplant of EU Standards in Taxation: A Case Study of the ACP Post-Cotonou Agreement"").

The second key finding is that there is a need (i) to include in the discussions of global governance concepts such as fairness, transparency in the extractive industry and exchange of information, treaty shopping across tax, trade, and investment initiatives (Chapters 7—"Competition and Complementarity of EU and FATF Beneficial Ownership Transparency Orders", 8—"Dealing with Treaty Shopping Across the Tax, Trade, and Investment Regimes", 9—"Hidden Dynamics and Hierarchies in Tax Policy: A Critical Assessment of Fairness in OECD, EU, and UN", and 10—"Transparency and Transformation: Rethinking Tax Governance in the Mining Sectors of Tanzania and Kenya"), and (ii) to address policy coherence, carve-outs, and competing demands in bilateral and multilateral instruments, for example, treaties, when regulating tax, trade, and investment (Chapters 3—"International Tax and Investment Policy: Navigating Competing Demands", 4—"The Tax Carve-Out Clause in International Investment Law", and 5—"Tax and Trade and Investment Instruments in Sustainable Development Goals Achievement").

The third key finding is that there is a need to address topics such as green energy, digitalization, tax incentives (Chapters 16—"Optimizing Policy Synergies: The Role of Tax Incentives in International Trade and Investment", 17—"Tax, Trade and Investment for Green Transition") with a holistic approach to understand their policy making objectives and how to address these objectives from a tax, trade, and investment perspective. The interactions and overlaps between tax, trade, and investment policies are also addressed in the case studies in this book (Chapters 12—"The Interaction Between IIAs and DTCs: Potential for Overlap and Reform Proposals" and 13—"The Intersection of Treaties on Tax and Trade: A Case Study of Australia and India").

By presenting a comprehensive analysis of these key findings, this book provides readers with a nuanced understanding of the complex relationships of domestic and international tax, trade, and investment law. It offers insights and potential solutions to understand how nation states, businesses, and investors continue to navigate this challenging legal landscape.

Allison Christians

Contents

List of Abbreviations

AEOI	Automatic Exchange of Information
AfDB	African Development Bank
ALS	Arm's Length Standard
APA	Advance Pricing Agreement
ATAF	African Tax Administration Forum
ATAIC	Association of Tax Authorities from Islamic Countries
AMLD	Anti-Money Laundering Directive
AU	African Union
BCA	Border Carbon Adjustment
BEPS	Base Erosion and Profit Shifting
BIAC	Business and Industry Advisory Council (now Business at OECD)
BIT	Bilateral Investment Treaty
BRI	Belt and Road Initiative
CARICOM	Caribbean Community and Common Market
CATA	Commonwealth Association of Tax Administrators
CBAM	Carbon Border Adjustment Mechanism
CbCR	Country by Country Report(ing)
CBDR	Common but Differentiated Responsibility and Respective Capabilities
CDIS	Coordinated Direct Investment Survey
CFA	OECD Committee on Fiscal Affairs
CFC	Controlled Foreign Company
CIT	Corporate Income Tax
CHIPS	Creating Helpful Incentives to produce Semiconductors and Science Act of 2022
CPC	Central Product Classification
CREDAF	Center for Exchange and Studies of Tax Administration Leaders
CRS	Common Reporting Standard
CSO	Civil Society Organization
CSR	Corporate Social Responsibility
DFAT	Department of Foreign Affairs and Trade

DTC	Double Tax Convention
ECOSOC	United Nations Economic and Social Council
ECOWAS	Economic Community of West African States
ECTA	Australia–India Economic Cooperation and Trade Agreement
EITI	Extractive Industries Transparency Initiative
EOI	Exchange of Information
EU	European Union
ESG	Environmental Social and Corporate Governance
ESTMA	Extractive Sector Transparency Measures Act
ETS	Emissions Trading System
FATCA	Foreign Account Tax Compliance Act
FATF	Financial Action Task Force
FDI	Foreign Direct Investment
FET	Fair and equitable treatment
FHTP	Forum for Harmful Tax Practices
FTA	Free Trade Agreement
FTC	Foreign Tax Credit
GATS	WTO's General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
G20	Group of Twenty
G7	Group of Seven
GAAR	General Anti-Avoidance Rule
GIFT	Global Initiative for Tax Transparency
GDP	Gross Domestic Product
GloBE	Global Anti-Base Erosion
GNI	Gross National Income
GST	Goods and Services Tax
GRI	Global Reporting Initiative
HLP	High-Level Panel
IBFD	International Bureau for Fiscal Documentation
ICC	International Chamber of Commerce
ICIJ	International Consortium of Investigative Journalists
ICMM	International Council on Mining and Metals
ICSID	International Center for Settlement of Investment Disputes
ICRICT	Independent Commission for the Reform of International Corporate Taxation
ICTD	International Center for Tax and Development
IFA	International Fiscal Association
IFCMA	Inclusive Forum on Carbon Mitigation Approaches
IFF	Illicit Financial Flows
IGF	Intergovernmental Forum on Mining, Minerals, Metals and Sustainable Development
IIA	International Investment Agreement
IIR	Income Inclusion Rule
IMF	International Monetary Fund

IO	International Organization
IOTA	Intra-European Organization of Tax Administrations
IR	International Relations
IRA	Inflation Reduction Act
IRMA	Initiative for Responsible Mining Assurance
ISDS	Investor–State Dispute Settlement
LDC	Least Developed Countries
LOB	Limitation on Benefits clause
MAP	Mutual Agreement Procedure
MCAA	Multilateral Competent Authority Agreement
MCMAATM	Multilateral Convention on Mutual Administrative Assistance in Tax Matters
MFF	Multiannual Financial Framework
MFN	Most-Favored Nation
MLI	Multilateral Instrument
MNE	Multinational Enterprise
NAFTA	North American Free Trade Agreement
NDC	Nationally Determined Contributions
NGO	Non-Governmental Organization
NT	National treatment
NTM	Non-Tariff Measures
ODA	Official Development Assistance
OECD	Organization for Economic Cooperation and Development
OEEC	Organization for European Economic Cooperation
PE	Permanent Establishment
POEM	Place of Effective Management
PIT	Personal Income Tax
PPT	Principal Purpose Test
PTA	Preferential Trade Agreement
PWYP	Publish What You Pay
QDMT	Qualified Domestic Minimum Top-Up Tax
ROO	Rules of Origin
RTA	Regional Trade Agreement
SBIE	Substance-Based Income Inclusion
SAAR	Specific Anti-Avoidance Rule
SDG	Sustainable Development Goals
SIFA	Sustainable Investment Facilitation Agreement
SPE	Special Purpose Entity
STTR	Subject to Tax Rule
TI	Transparency International
TIN	Taxpayer Identification Number
TP	Transfer Pricing
TPG	Transfer Pricing Guidelines
TRIMS	Agreement on Trade-Related Investment Measures
TSD	Trade and Sustainability Development

UK	United Kingdom
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
UNCTC	United Nations Center on Transnational Corporations
UNDP	United Nations Development Program
UNFCCC	United Nations Framework Convention on Climate Change
US	United States
USD	United States Dollar
USMCA	United States Mexico Canada Agreement
UTPR	Undertaxed Payments Rule
VA	Value Added
VAT	Value Added Tax
VCLT	Vienna Convention on the Law of Treaties
WATAF	West African Tax Administration Forum
WHT	Withholding taxes
WTO	World Trade Organization

Part I
The Tax, Trade, and Investment Governance Landscape

Introduction to Part I

Allison Christians

The Chapters in this Part introduce readers to the multifaceted and interconnected governance aspects of tax, trade, and investment regimes. Navigating these regimes, states find themselves contending with conflicting and sometimes mutually exclusive policy choices, necessitating difficult tradeoffs among internal goals as well as between domestic and international goals. The chapters demonstrate that there is very little policy coherence across the global regulatory areas, and that policymakers do not always seem to acknowledge the inconsistency of their own approaches in each area. In some cases, national policy choices respecting cross-border taxation seem to conflict directly with competing national policy goals in cross-border trade and investment. In other cases, national policy choices in one area seem to be constrained by pre-existing international obligations in another. Sometimes, national policy choices seem wholly constrained by historical international ones. When a need for reform in one area arises, multilaterally embedded policy choices in the other areas may interfere if not prevent reform. Each chapter in this Part examines various aspects of these conflicts, with an eye to understanding the legal, social, economic, and distributive aspects of the contemporary tax, trade, and investment landscape.

In Chap. 2, "A Survey and Critique of International Tax Governance," Karen Brown sets the stage by exploring the ongoing struggle lower income states experience in having their voices heard and their concerns addressed in these global regulatory arenas. In particular, Karen Brown highlights the ongoing governance problems that arise in international tax policymaking owing to the persistent centering of the OECD, an intergovernmental club of highly developed countries, to the practical exclusion of all other nation states and in particular the states of Sub-Saharan Africa. Indeed, the OECD has dominated global tax policymaking for over

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50 years, despite voluminous critique from excluded countries as well as tax law and governance scholars. The basic governance problem emanates from the complicated history of the international tax order, which evolved through historical patterns of geo-political and economic imbalance among states and has always been characterized by a core lack of agreement on any terms that would satisfactorily define multilateral cooperation on tax matters. Because of this lack of agreement, the international tax landscape developed as a networked transnational order filled with contradiction and contestation, most of which ignores the global welfare aspects of each of its institutional and procedural components. Brown's chapter accordingly examines the deleterious policy impacts of the current institutional choices and advocates for a reconstitution of global tax governance to include meaningful input from Africa and other low-income regions in order to achieve a fairer global tax system.

In Chap. 3, "International Tax and Investment Policy: Navigating Competing Demands," Katharina Kuhn introduces readers to the ways in which national policymakers contend with competing policy goals at the intersection of tax and investment. This intersection involves a basic incompatibility as states seek to participate in the evolving international tax regime as it responds to excessive tax competition, but also pursue national economic development and industrial policy strategies aimed at attracting foreign direct investment, including by offering tax incentives of various kinds. She notes that states might attract foreign investment capital by participating in multilateral tax governance, which potentially increases their reputations by presenting them as compliant with international tax best practices, but they do so at the risk of losing the ability to use tax incentives to accomplish their goal of attracting foreign capital. The tradeoff between cooperating with multilateral efforts to reduce tax-motivated cross-border planning and using domestic tax rules to make the jurisdiction more attractive to outside investment creates difficult policy choices. Kuhn's chapter demonstrates the difficulty by mapping the interactions of these competing policy goals under the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS) and the 2021 Two Pillar Solution.

Paloma García Córdoba continues the exploration of the difficult intersection between national investment and tax policy goals in Chap. 4, "The Tax Carve-Out Clause in International Investment Law." The chapter introduces readers to the complicated and evolving relationship between taxation and international investment agreements. In broad strokes, international investment agreements aim to attract foreign capital to a jurisdiction (typically, a less-developed state) by offering assurances that investments will be protected against future costs arising from regulatory action. For example, an international investment agreement might entitle investors to treatment in the country that is "fair and equitable" and non-discriminatory when compared to local investors and investors from other countries, and most such agreements contain anti-expropriation provisions that assure investors their investments will not be at risk of becoming state-controlled in the future. Some contain so-called stabilization clauses, which effectively grant tax incentives that the state can never revise or revoke. Without a tax carve-out clause, investors might view virtually any change in national tax policy as inconsistent with these agreements,

even if the reforms were widely applicable but especially if they primarily impacted cross-border business and investment. Many such agreements have tax carve-out clauses to prevent a too broadly interpreted agreement from effectively preventing national tax reforms. Thus a tax carve-out clause, as the name suggests, seeks to separate national tax policy from national investment policy. Few agreements have total tax carve-outs but many have partial tax carve-outs. Córdoba accordingly examines the language and purpose of tax carve-out clauses and demonstrates their critical importance in the relationship between international investment law and tax law.

Finally, in Chap. 5, "Tax and Trade and Investment Instruments in Sustainable Development Goals Achievement," Sharon Waeytens introduces the reader to a way to reconcile the competing and conflicting aspects of tax, trade, and investment policy instruments. She does so by examining how each of these governance regimes can contribute to the achievement of the Sustainable Development Goals, a set of policy statements which all of the UN member states have agreed in principle to promote (or at least, refrain from impeding). The Sustainable Development Goals constitute an agreed multinational policy with which otherwise incompatible national governance regimes must strive to be coherent. Waeytens explains why and how tax, trade, and investment policy instruments reach different individuals and companies and target different behaviors and interests, and notes that these policy instruments can either cancel or reinforce each other, making it important to understand the interaction among them. The chapter concludes that to achieve the Sustainable Development Goals, governments should use a combination of the policy instruments and make policy coherence a priority.

A Survey and Critique of International Tax Governance Reform

Karen B. Brown

1 Introduction

Commentary published after the Fifteenth Meeting of the Inclusive Framework of the Organisation for Economic Cooperation and Development (OECD) set out a roadmap to institution of one aspect of the most aggressive international tax reform project in nearly 100 years. That project, the Base Erosion Profit Shifting (BEPS) initiative, adopted a template for a global effort to reconfigure major tax policy tenets to target manipulation by multinational enterprises (MNEs) of the opportunities presented by the spaces between separate country tax regimes to minimize worldwide tax liability in ways never anticipated or sanctioned by host countries. Common wisdom is that these tax avoidance schemes can be addressed effectively only through cooperation between sovereign nations. A major objection to the roll out of BEPS reforms, however, is that the blueprint for the plan was constituted and shaped without input from non-OECD member nations. A key component of the excluded group consists of countries in Sub-Saharan Africa, a region of pivotal importance to the rest of the world, if only because it is expected to host no less than a quarter of the population of the globe and to account for ninety percent of the world growth in working-age population by 2050 (World Bank Group 2022, 2023). For this reason, among others, growth and sustainability in Africa are critical to the survival of the remainder of the world.

Post-pandemic, Sub-Saharan Africa has struggled to reset a course to economic health. It faces the challenges presented by climate change, service of debt on loans from high-income nations of the developed world, rising commodity prices for goods imported, decreasing prices for goods exported, and revenue drains resulting

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from very heavy public spending to address the considerable health and other social welfare demands of Covid-19 and other devastating diseases. On top of these obligations, the region struggles to engage with the crushing burden of compliance with BEPS dictates shaped before meaningful consultation with it. The predicament of Sub-Saharan Africa paints a picture of a region of mostly low-income countries fighting to secure a position in the global tax governance hierarchy by serving as a platform for redistribution of economic resources to members of the OECD while it somehow works to marshal resources to bear costs arising from other bad choices made by the developed world. This is particularly troubling when one considers that the enormous financial and administrative resources this region must devote to reconciliation with the BEPS prescriptions may result, in a worst-case scenario, in tax revenue loss or, in the best case, very modest revenue gain.

A call for a new world order in global tax governance is the emphatic response from Africa.[1] At the behest of the Nigerian delegation, the Economic and Social Council (ECOSOC) of the United Nations (UN) sponsored a convention in April 2023 to address the contours of such a reform. The imminent finalization and imposition of the Pillars One and Two BEPS proposals provided the catalyst to confront the impact of this far-reaching reform of the international tax system that unfolded without guidance from the African region. The BEPS program has proceeded not only without true buy-in from this region but also despite demonstrated detrimental effects to Sub-Saharan Africa. While Africa declared early on the ability to attract foreign direct investment through properly tailored tax incentives to be one of its highest priorities in any tax reform effort, the BEPS drafters subordinated this issue, ultimately adopting templates that admittedly serve the choices made by OECD members regarding their separate tax regimes.

Whether or not the BEPS prescriptions are put in place, the prospect of the future progression of international tax reform without initial input from Sub-Saharan Africa and other vulnerable regions is untenable. A governance structure that (even without intent) supports redistribution of economic resources from low-income countries to the developed world is broken and ripe for replacement. The costs of displacing the existing governance structure are far outweighed by the restoration of integrity and legitimacy to global tax reform efforts. Securing for Sub-Saharan Africa a voice in its own development and growth can only serve the remainder of the world in the long term. This article examines the failures of current tax reform by examining the flaws in the construction of the BEPS project and the resultant costs borne by the African region. It concludes by imagining a revised, representative tax governance structure that takes account of the needs of Sub-Saharan Africa.

[1] A parallel movement is addressing this issue in the larger global governance structure at the United Nations ("UN") as well. On behalf of the 1.2 billion people of African ancestry, Prime Minister Mia Amor Mottley of Barbados has detailed at the UN the importance of a challenge to an international governance structure that excludes their voices (Barbados Prime Minister, Sept. 2022).

2 Global Tax Reform Without Representation

Of the many reforms undertaken by the BEPS project, Pillars One (addressing digital economy reforms) and Two (prescribing a fifteen percent global minimum tax) have placed the heaviest burden of compliance on the Sub-Saharan Africa region (OECD, Two-Pillar, 2021). These initiatives were developed in the aftermath of the initial OECD response to the G20's call to target sophisticated tax avoidance techniques structured by large multinational companies resident in high-income countries. After the 15 final BEPS reports were issued in 2015, heavy criticism came from those countries, including Sub-Saharan Africa, that had no or very little input into establishing the core principles guiding the effort. In response, a second phase, BEPS 2.0, was launched. Countries affected by the proposals were invited in 2016, shortly after publication of the final reports, to join the Inclusive Framework, a gesture designed to elicit buy-in for the project. While the OECD expressed that its goal in creating the Inclusive Framework was to place all countries on a "level playing field" as "equal partners" in the delicate process of international tax reform, the critical contours and parameters were set beforehand (OECD, Inclusive Framework, 2017). Ultimately, the very limited input allowed the outsider (non-member) countries before fundamental decisions were made was mostly ignored by the OECD in the final reports.

Sub-Saharan African nations pushed for incorporation of a range of objectives at the very beginning of the OECD tax reform process. Three of these concerned formulary apportionment, simplification of transfer pricing rules, and respect for the region's need to develop sustainable tax incentives to attract foreign investment. All three priorities were viewed as essential to the ability of these nations to meet revenue needs and were identified by Africa at a July 2014 UN Meeting in Addis Ababa (UN, Addis Ababa Action Agenda 2015) and through engagement in an OECD-sponsored Working Group for Developing Countries which published reports in 2014 (OECD, Developing Working Group, Parts 1 and 2, 2014a, b). Unfortunately, the OECD BEPS project commenced in 2013, prior to consultation with developing countries regarding the impact of these reforms on their economies. By 2014, the core initiatives were already developed, presumably leading the OECD to resist redoing the work to reflect priorities of African nations, non-members with little political power to spark re-evaluation of a reform structure closely aligned with the objectives of OECD member countries. Consequently, the BEPS project generally did not engage directly with the needs of Africa, working on the margins to make any subsequent concessions to the region.

After the 2014 Addis Ababa conference, African nations urged the UN to take control of the tax reform process. Under the auspices of the UN, these nations hoped to push for implementation of an alternative method of allocating taxing rights among nations by placing formulary apportionment on the reform agenda, as well as to broaden the focus to address impediments to revenue raising. The UN, however, opted to support primary jurisdiction over these matters in the OECD, because its work was already in progress. When the final reports were issued about a year

later in 2015, the OECD summarily rejected formulary apportionment without explanation (OECD, Explanatory Statement 2015). Because developing countries understood that the burden of complying with the BEPS initiatives would fall on non-members of the OECD, as well as the members, they lobbied for participation in the next phase of work on the BEPS initiatives. The OECD responded by forming the Inclusive Forum in 2016, a forum open to membership for every country hoping to provide input into implementation of BEPS.

Given a BEPS process that did not focus on developing country issues at the outset, it is not surprising that membership in the Inclusive Forum has not advanced the primary objectives of the countries in the Sub-Saharan African region. For those African nations that joined,[2] work in the Inclusive Framework was not designed to help them, and they are not the primary beneficiaries of the reform, because the BEPS project was built to accommodate the interests of the OECD members in search of additional tax revenue (OECD/G20, Outcome Statement July 2023).[3] Subsequent developments arising from the work in the Inclusive Forum on Pillars One and Two have confirmed this insight.

Members of the Inclusive Forum are required to meet the four BEPS minimum standards[4] and to adopt Pillars One and Two by implementing them in their legal systems (OECD 2017). Placing aside for the present the burden of conformity to the minimum standards, the Pillars alone place costly and administratively complex obligations on Sub-Saharan Africa while failing to address identified needs of the region. Pillar One erects a very complicated set of rules designed to identify income generated by large MNEs that operate in the digital economy and to permit taxation by the countries in which these companies do business despite the absence of the physical presence (permanent establishment) typically required by long-standing universal treaty provisions (OECD Model Income Tax Convention, Article 7 2017). In brief, Pillar One has set up a mechanism by which to identify this additional income created by exploiting consumer markets solely online. It does so by describing an Amount A, providing a formulaic approach to identify these residual profits as those in excess of a fixed return on assets. Amount B of Pillar One describes transfer pricing rules to determine allocation of income attributable to a company's baseline marketing and distribution activities in the jurisdiction. Amount C sets up a binding mechanism to arbitrate disputes between affected countries. Pillar One

[2] The Gambia and other Sub-Saharan nations have not joined the IF. Some, like the Gambia, have attended the Inclusive Framework meetings to keep informed of developments in the BEPS process certain to impact the non-joiners.

[3] The Statement recognized that ratification of Multilateral Instrument is not possible unless at least 30 jurisdictions accounting for at least 60 percent of the Ultimate Parent Entities (UPEs) of in-scope MNEs (those in high-income jurisdictions) sign.

[4] They are: eliminate preferential tax regimes (BEPS Action 5), meet country-by-country reporting requirements to monitor transfer pricing between members of a multinational group of enterprises (Action 13), prevent treaty abuse (BEPS Action 6), and update mutual agreement procedures to resolve tax disputes (Action 14).

rules are to apply only to MNEs with group worldwide profits of at least 750 million euros (OECD 2021).

Since their initial promulgation the Pillar One proposals have gone through numerous periods of consultation aimed primarily at reducing complexity and reaching compromise. Their genesis derives from a political brouhaha that ensued after several countries, particularly those in the European Union, argued for modernization of antiquated treaty rules that allow large high-tech multinationals to derive profits generated from accessing consumers online and very profitably mining the very valuable information obtained. These countries acted unilaterally to enact digital services taxes to be imposed on these mostly American behemoth companies. Pillar One is intended as a compromise that promotes agreement on the parameters of a digital tax that forestalls enactment of conflicting rules and retaliation. The most recent iteration of Pillar One requires Inclusive Framework members to agree not to impose a digital tax before 2025 pending further work to achieve a more permanent solution (OECD, Outcome Statement July 2023).

Sub-Saharan members of the Inclusive Framework are obliged to gain the necessary technical expertise to vet and determine the impact of the Pillar One rules on their own economies, a daunting task for countries with limited administrative capacity. The diversion of resources from the administrative issues arising from their own revenue-raising priorities to mastering Pillar One is particularly objectionable when one notes that there is very little revenue to derive from the imposition of the type of digital services tax prescribed by Pillar One (OECD 2024).[5] Indeed, one study showed that the greatest revenue gains from implementation of Pillar One inured to the benefit of the European Union and the United States, while benefits to the African region were too small to estimate (De la Feria 2023). Those countries in the region that had moved to enact a digital services tax independently of the OECD found that it successfully raised revenue (Sarfo 2022; Ogungbenro and Ajayi 2023). They view the OECD mandate as a mechanism to shift revenue from their treasuries to those of high-income members of the OECD, yet they are constrained for reasons discussed below to cooperate with the reform process.

These nations have engaged in the Inclusive Framework deliberative process, while understanding that there is little to address their revenue needs. Their willingness to cooperate has garnered some concessions in the formulation of Pillar One standards, but only on the margins. Notably, through its representative, the African Tax Administrative Forum (ATAF), the region argued for allocation of a greater portion of routine profit under the most important component (Amount A) of this "new taxing right" to market jurisdictions, like those in Sub-Saharan Africa. While ATAF urged allocation of thirty-five percent of profits in excess of the base amount (a ten percent return on assets), the OECD resisted, settling on allocation of only twenty-five percent (ATAF 2022). Thus, under Amount A of Pillar One, African

[5] The study noted "broad gains across all jurisdictional groups, with higher gains for high income jurisdictions relative to lower and upper middle income. Challenges after the 2008 financial crisis motivated high income countries, including many in the European Union (EU), to launch the BEPS initiatives." (Mosquera Valderrama 2020).

jurisdictions stand to gain insufficient revenue to justify membership in the Inclusive Framework. Nigeria and Kenya, for example, had each promulgated their own digital services tax, apart from that which emerged from the OECD deliberations. Both had revenue gains under their separate digital services regimes that met the targets established through their own budget processes (Ama Sarfo 2022).

The Inclusive Framework did accede to ATAF's request to drop the nexus threshold necessary for application of Pillar One's Amount A from five to 1 million euros for Africa and other developing countries, which expanded their ability to tax more multinationals operating in those regions.[6] It failed, however, to grant Africa's urgent request that Pillar One innovations support a shift of taxing rights to the source country, i.e. the country in which the multinational operates (ATAF 2022). This shift has been viewed by the countries of the Sub-Saharan region as essential to their ability to raise sufficient revenue to sustain their populations. With primary taxing jurisdiction in the country of residence of large multinational companies, in particular, inadequate revenue is left within the reach of Africa.

A similar critique arises from the Inclusive Framework's rejection of requests from ATAF to modify the contours of Pillar Two, the proposal for a global minimum tax of fifteen percent. The OECD's insistence on elevating the Income Inclusion Rule (IIR) of Pillar Two above other mechanisms for collecting the tax promised to make the high-income countries in which many multinationals are resident the primary beneficiaries of the reforms. Under rules like the Subpart F provisions of the U.S. Internal Revenue Code (IRC), the country of residence is pressed to impose the minimum tax on the income of its multinationals on profits attributed to operations around the world. If it fails to do so, only then can the source jurisdiction, such as a developing country in which the company operates, impose the so-called top-up tax, collecting tax on those profits derived within its own borders on the difference between the lower residence country rate and fifteen percent (Mason 2022).[7] Consequently, ATAF recommends and has provided guidance to its members regarding implementation of a qualified minimum domestic top-up tax (QMDTT). The primary taxing right is in the hands of the high-income nations that have every incentive to implement the IIR to protect their revenue bases. The little agency allowed Sub-Saharan Africa from the potential opportunity to adopt a QMDTT exists only in the event the high-income countries do not act.

Because many African nations impose corporate income tax at rates between twenty-five and thirty-five percent, the OECD's endorsement of the lower fifteen percent benchmark is problematic. A worldwide minimum tax has the potential to become a worldwide maximum tax. For developing countries, in particular, a fifteen percent rate on corporate profits may not provide the level of revenue needed to sustain the needs of their economies. While in theory nothing in Pillar Two would

[6] The rules requiring binding dispute resolution were relaxed in some cases and the extractive industries were removed from the purview of Pillar One as requested by ATAF.

[7] Ruth Mason refers to the "diabolical machinery" unleashed by the interaction of the Pillar 2 rules that operates to induce cooperation and forecloses unilateral deviation from the global minimum tax.

prevent an African nation from erecting a higher-than-fifteen-percent tax rate on corporate profits, in practice a multinational company with other investment locale options might choose to go elsewhere. If the company were induced to come to or to continue business operations in Africa, inevitable negotiation for other non-tax concessions, such as grants and other subsidies would result in subordination of these countries' economic interests, a result the OECD professes to abhor (Rubinstein et al. 2024).[8] But, for these countries, it can be expected to set into motion the very race to the bottom which the minimum tax rate purportedly is intended to avert. In practice, however, as the final contours of the Pillars take shape, only the type of manipulative tax avoidance targeted is that currently affecting the high-income members of the OECD.

As negotiations proceeded toward the final Pillar Two prescriptions, ATAF proposed the Subject to Tax Rule (STTR) in an effort to achieve a reform of direct benefit to the region. Although the primacy of the IIR foreclosed allocation of first taxing rights to African source countries, the region urged as a second-best option a minimum withholding tax for payments from operations in source countries which have the effect of stripping out earnings to erode the tax base. These include remittances to related parties in transactions structured to couple a deduction from the source country's tax base with a transmission to a related party subject to no- or very low tax. The payments in question included interest, royalties, and services, all susceptible of manipulative tax avoidance strategies by multinationals operating in Sub-Saharan Africa. While the OECD acceded to ATAF's request and adopted the STTR, it initially failed to extend coverage to payments for services, which were of particular concern for the region (ATAF 2022).[9] Bowing to pressure, the OECD extended coverage of the STTR to services (OECD 2023). The withholding rate of nine percent, however, lower than that proposed by Africa, affords insubstantial revenue to the African source country. With uncertainty regarding whether or when the STTR will gain effect, because it must be implemented through the ratification process that attends adoption of the Multilateral Instrument by the requisite number of countries, the promise of this one concession to Africa is limited at present.

The basic framework of the BEPS reform initiatives has failed to address the most pressing need of the Sub-Saharan African region, support for programs to attract foreign investment. Even the OECD has acknowledged that compliance with the global minimum tax in Pillar 2 will cause these countries to abrogate an obligation under existing investment treaties to accord "fair and equitable treatment" and "a stable and predictable legal or regulatory environment" to investors (Rubinstein

[8] As Rubinstein et al. note, referencing Vietnamese Congress, Resolution No. 110/2023/QH15/ (Nov 29 2023), that country, for example, is proposing to set up an investment support fund (financed by Pillar 2 top-up taxes) to continue to attract foreign investment.

[9] The UN Tax Committee's STTR expands coverage to include services, as requested by Sub-Saharan Africa. One commentator notes this concession, but considers whether the OECD version of the STTR would be easier to implement because it must be adopted by other member countries of the Inclusive Framework in the process of ratification of the Multilateral Instrument (Heitmüller 2024).

et al. 2024). Accounting for the needs of the developing world has taken a back seat to accommodation of the requirements of OECD members and resulted in acknowledgement of the struggles of low-income countries only on the margins of reform, mostly as an afterthought, an after-the-fact attempt to tailor a pre-ordained structure to suit Africa's needs. With the considerable burdens of meeting the Inclusive Framework minimum standards and the low return on investment for the region, one wonders why Africa has engaged in the Inclusive Framework process. The next section examines the coercive effect of BEPS standard-making.

3 Why Does Sub-Saharan Africa Engage in the Inclusive Framework?

As noted above, the OECD sought contribution of views and feedback in the development of the BEPS project mostly after the legitimacy of a major international tax reform project, destined to affect (and require the endorsement of) the non-OECD member countries, was called into question (Brown 2022, Tax Incentives). While cooperation by Sub-Saharan Africa in the last stages of an international tax reform process launched without its participation when the primary goals are to enable high-income nations to raise revenue may seem surprising, it derives from this region's need to access any benefit for its residents, although marginal in nature. In the fall 2022, the OECD announced its view of the role of African nations: to provide a platform for the effective operation of the international tax system, acknowledging that the BEPS reforms have little chance of success without the participation of most nations. Even jurisdictions, like those in Sub-Saharan Africa that have little to gain, are expected to accept and implement the new prescriptions. This development places developing countries, in general, in the unenviable position of being good stewards of a global tax system that offers them very little in return. In the OECD's Inclusive Framework on BEPS Progress Report, issued in October 2022, it noted:

> Developing countries have played their part in securing the integrity of the international tax system, taking action to meet the BEPS minimum standards. (OECD Inclusive Framework 2022)

African nations, in particular, have acceded to the pressure to be the so-called good tax citizens for a variety of reasons. The availability of loans through the International Monetary Fund (IMF), largely controlled by the high-income nations, depends upon the perception that the needy nation is worthy of financial support. Ultimately, if these loans cannot be fully repaid, the grant of debt relief, in whole or part, occurs in a fraught process in which the debtor is figuratively brought to its knees, forced to make compromises and concessions viewed as necessary by the lenders, but frequently with deleterious consequences to the nation's constituents (Lustgarten 2022). Cooperation can also lead to other benefits, including eligibility for training of tax administrative officials and provision of other technical

assistance, initially to assist in implementation of BEPS and of benefit to routine tax authority functions that are unrelated to BEPS (OECD, Tax Administrators Without Borders). This type of assistance can expand the technical expertise of Sub-Saharan administrations beyond the capacity of existing infrastructure.

Other examples reflect agreement to participate in BEPS through membership in the Inclusive Framework after actions by OECD members that can only be described as coercive. Namibia and Tunisia joined the IF only after the threat of blacklisting by the European Union for failure to adhere to its Code of Conduct Guidelines. Inclusive Framework members must agree to implement the minimum standards, including Pillar One, designed to raise significant revenue for the EU through a digital services tax fashioned to meet its needs. In trade negotiations with the U.S., Kenya ended its resistance to joining the IF when it became apparent that the U.S. would not conclude trade negotiations without Kenya's agreement to endorse the two BEPS Pillars (Orbitax 2023). Acceptance of the BEPS minimum standards was tied to trade benefits not otherwise available to Kenya from a powerful trading partner, the U.S.

Finally, participation in a BEPS reform project not designed to meet the needs of Africa seems driven, in part, by the desire of the various nations in the Sub-Saharan African region to be treated with respect. None of these countries has membership in the OECD. The only one with some chance of gaining membership in the foreseeable future is South Africa, the most prosperous country in the region. Apart from deriving any specific benefit from cooperation, participation in BEPS by nations in the region appears to be motivated by a desire to be accepted as legitimate and, hence, players in the global economic theater. This type of legitimacy, they hope, may position them for a larger role in the design of future international tax reform efforts.

Given the inadequacy of the BEPS effort to meet Africa's current needs, a reconstitution of the global tax governance structure is in order. If Africa remains on the margins of tax reform, not true players, but rather pawns, the next project and future initiatives that launch will serve only to undermine the goals and aspirations of the region. The next section considers the contours of a global tax governance structure that serves the African region.

4 Global Tax Governance Reform

While it may be very difficult to imagine a dismantling of the OECD's stronghold on global tax governance, just as the thought of undoing, for example, the U.N. Security Council's lock on major aspects of international relations, seems out of reach, the above sections demonstrate that the time has come to envision a truly inclusive framework for international tax reform. Whether or not the new structure continues to include a role for the OECD as a body or direct representation by the member countries, there is a broad range of suitable alternatives that can offer representation for every interested nation. The only viable models are those that will

feature at the outset direct contribution of views by Africa and other low-income regions and a vote in determining the path of reform. Sub-Saharan Africa must become a key player in global tax governance. Given the projection that the region will host a quarter of the world's population in 2050, the constituent nations must be in a position to set tax policy in a manner that will permit them to face the challenges presented by Covid-19, climate change, and the dominance of high-income country multinationals with the power unilaterally to advance their own agendas. If Sub-Saharan Africa does not thrive through a variety of measures, there is little hope of achievement of the UN's SDGs because critical indicia of progress toward achieving those goals will be measured by reference to developments in the region.

Three possible avenues of reform of the global tax governance system are promising: complete overhaul of the system by establishing a truly representative global tax organization, such as a World Tax Organization; construction of a framework for collaboration through existing representative bodies (Christians 2022); or redesign of the OECD consultative practices to include meaningful input from "outsider" countries at the very start of the policy reform project. Adrian Sawyer has thoroughly considered the feasibility of constituting an International Tax Organization (ITO) (so named to avoid confusion with the World Trade Organization) and concludes that implementation is advisable and possible, particularly if it takes form gradually through limited initiatives (Sawyer 2009). Putting aside the logistics involved at the outset in gathering all nations to conclude an agreement about the operations and functions of a new global tax organization and setting a mechanism for covering costs, no small tasks, Sawyer's idea to commit to the new ITO one discrete project could be accommodated. The logical first project would be reform of the BEPS initiatives and the related Pillars to take account of the needs of the Sub-Saharan African region and other low-income countries.

In the near term, the considerable time and effort necessary to reconstitute an international tax governing body may suggest that the second option, establishment of a framework for collaboration through existing representative bodies, including the OECD, is the better first move to achieve transformative input from Africa. Accordingly, the drivers of international tax reform, in addition to OECD and EU membership, would include at a minimum the following organizations: CARICOM, ATAF, the African Union, CREDAF,[10] and the Asian Pacific Forum. To signal that the time for such an approach has come, the UN has responded to the call for broader representation in the important mechanisms of global tax reform. To achieve a "globally fair" international tax system the UN General Assembly acted on November 15, 2023 to approve a UN framework convention on international tax cooperation to make it "fully inclusive and more effective"[11] (UN General Assembly 2023). With a balanced gender and geographical representation of the five delineated regional groups, an ad hoc intergovernmental committee will prepare its draft

[10] Cercle de Réflexion et d'échange des dirigeants des administrations fiscales.

[11] The resolution was approved by a majority of 125, with 48 opposed (including the U.S. and the European Union), and 9 abstaining.

report on implementing a framework convention to the 79th General Assembly in 2024. Approval of the UN resolution portends an important step toward inclusion of all stakeholders in the global tax reform process.

5 Conclusion

The dominance of the OECD, organ of the 38 high-income member countries, in international tax reform, has engendered initiatives that fail to address the needs and concerns of Sub-Saharan Africa, a region whose importance has been perennially discounted. It is a vestige of colonialism ripe for challenge.[12] While the absence of true input from Africa may seem like business as usual, a given not subject to challenge, it promises to undermine progression toward achievement of sustainability goals and the future viability of the region and, importantly, the rest of the world. Consequently, the movement in the UN toward erection of a truly inclusive framework of cooperation and collaboration in global tax reform is essential and welcome.

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[12] Providing an outsider perspective on the occasion of the death of Queen Elizabeth II, a South African observer noted that "[t]he thing that I think Western people need to genuinely try to absorb and realize is that colonialism is history in the West…It is a thing of the past, in the West. But in our countries, colonialism is now" (Ombuor et al. 2022). Abraham Lustgarten shared Prime Minister (Barbados) Mia Amor Mottley's parallel assessment: "The world, she said, 'is segregated regrettably between those who came first and in whose image the global order is now set' and a global order that is itself 'simply the embalming of the old colonial order that existed at the time of the establishment of these institutions'" (Lustgarten 2022).

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International Tax and Investment Policy: Navigating Competing Demands

Katharina Kuhn

1 Introduction

International tax and investment policy are closely intertwined. This does not only concern overlaps of the legal tools governing both regimes, but also the policy rationales that guide policy formulation in both issue areas. Indeed, the first model Double Tax Convention (DTC) published by the League of Nations in 1928 was in part motivated by the fear that double taxation would limit capital mobility and hence slow down post-war reconstruction, for which the members of the League of Nations considered foreign direct investment (FDI) to be essential (Jogarajan 2018, pp. 3–4). With growing capital mobility since the 1980s, the interaction of international tax and investment policy has only increased. Many jurisdictions use tax policy as an integral part of their strategy to attract FDI, which is considered an important driver of economic growth and development particularly for lower-income countries (Okafor et al. 2017, p. 589; Brauner 2013, pp. 25–26; Fuest and Riedel 2009). As a result, many governments engage in tax competition and seek to underbid their competitors with preferential tax treatment (Brauner and Steward 2013, p. 10). At the same time, however, tax is but one of several factors that firms consider in their choice of an investment location, while issues such as the quality of the local infrastructure, the ease of setting up and running a business, or rule of law and good governance equally influence investment decisions (see, for instance, Brewer 1993; Ross 2019). Besides tax incentives, governments therefore use a number of tools to improve their reputation and signal good governance and investor-friendliness.

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With the increasing multilateralization of the international tax regime that has been promoted by the OECD's BEPS initiative (see Chap. "A Survey and Critique of International Tax Governance Reform" in this book), policy makers are experiencing growing pressure to formulate a coherent policy towards international tax cooperation (Cadzow et al. 2023). At the same time, the potential for overlap between the international tax and investment regimes is of increasing concern to policymakers (UNCTAD 2021). The overlap between international tax and investment policy may occur on two levels. Legal overlaps concern moments in which the legal commitments in one regime have ramifications for the policy space of states in the other regime. The most prominent example for such overlaps concerns the risk of investor-state arbitration under traditional Bilateral Investment Treaties (BITs) that do not contain tax-carve-out clauses (see Chap. "The Tax Carve-Out Clause in International Investment Law" of this book). At the same time, overlaps may also occur on the level of policymaking when policy decisions and goals in one issue area interact, and potentially constrain, the policy space in the other issue area.

In the context of the OECD/G20 BEPS Project, many capital-importing countries have raised concerns about the potential impact of membership in the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (Inclusive Framework) and the adoption of the Global Anti-Base Erosion Mode Rules (GloBE) for their ability to attract FDI (Mosquera Valderrama 2021, p. 2024). While on the one hand the commitment to both initiatives may enhance the reputation of an investment destination by signalling adherence to OECD best practices in international tax policy, both have implications for the policy space of capital-importing countries to offer tax incentives. As a result, this chapter argues, policymakers in capital-importing economies need to balance two potentially contradicting policy goals: the ability to safeguard their policy space for investment-oriented tax policy and the reputation of their jurisdiction building on legal and tax certainty and 'good tax governance'.

In the following, Sect. 2 discusses tax-related strategies to attract FDI before turning to the reputational dimension of international tax policy (Sect. 3). Section 4 maps the interaction of different policy goals (the protection of policy space and the signalling of 'good tax governance') in the OECD's recent work on tax and argues that both the participation in and abstention from multilateral tax frameworks have reputational and substantive implications for capital-importing economies. Section 5 concludes.

2 International Tax Policy and FDI

The literature studying the determinants of FDI flows is well developed and has identified a number of factors that contribute to the ability of a host country to attract FDI. Most commonly, political factors such as political risk, 'good governance' and the protection of private property rights, the characteristics of the labour- and consumer market, the quality of the local infrastructure, and economic factors

such as a stable macroeconomic environment and trade-openness have been found to positively affect FDI flows (Dunning 1988; Brewer 1993; Addison and Heshmati 2003; Al-Sadig 2009; Mengistu and Adhikary 2011; Gonzales et al. 2017; Ross 2019).

In addition, tax policy is considered highly relevant for the ability of a jurisdiction to attract FDI. Indeed, the competition for FDI is often identified as key driver of tax competition: based on the assumption that taxpayers respond to changes in tax policy by moving their resources across jurisdictions, rationalist literature conceptualizes international tax policy as prisoners' dilemma in which the attempt to attract FDI through tax policy pushes states to adapt their domestic tax systems to the requirements of the market and therefore lower their effective tax rates (Brauner 2013, pp. 30–31; Pak 2004, p. 191; Avi-Yonah 2004, pp. 375–381; Ring 2009, pp. 561–562). Section 2.1 discusses the various tax policy tools that governments adopt to engage in tax competition, while Sect. 2.2 critically assesses the impact of these tools on FDI flows.

2.1 Tax Policy for Attracting FDI

Tax incentives may serve a variety of purposes such as promoting economic growth in a specific sector or region or managing inequalities between different groups of society (Mosquera Valderrama 2021, p. 2016). Based on the assumption that geographically mobile capital responds to tax incentives, many jurisdictions use features of their tax system to attract foreign capital, thereby engaging in tax competition (Avi-Yonah 2000). Tax incentives, however, constitute only a sub-set of investment incentives that provide economic advantages to investors (World Bank 2017, p. 164; Tavares-Lehmann 2016, p. 25). In the most general sense, tax incentives can be defined as schemes that 'depart from a general and neutral tax system […] resulting in a favourable tax treatment or a reduced combined overall burden for the investor' (Ogazón Juárez and Calderón Manrique 2018). What is or is not a tax incentive is hence relative to the tax system of the jurisdiction.

Tax incentives may be profit- or cost-based. Profit-based incentives reduce the tax rate applicable to the taxable income of a particular company, e.g. through tax holidays, reduced rates, or exemptions for particular income sources. Cost-based incentives are allowances linked to investment expenses such as accelerated depreciation schemes or tax deductions and credits, and tend to be more effective in attracting investments that would otherwise not take place (Andersen et al. 2017, pp. 77–78; International Monetary Fund et al. 2015, p. 20). Tax incentives may concern direct and indirect taxes as well as characteristics of the tax system (Clausing 2016, pp. 28–31).

Different groups of countries tend to offer different types of tax incentives depending on their economic development needs (Oguttu 2020, p. 67). Low-income economies tend to offer tax holidays and reduced tax rates, as they often lack the ability to provide other types of (nonfiscal) investment incentives such as grants or

subsidized loans (Muyaa 2018). High-income countries, on the other hand, tend to offer tax credits and incentives for research and development, while middle-income countries often choose preferential tax zones (Oguttu 2020, p. 67).

In addition to adjustments of the domestic tax system, many jurisdictions adopt measures to prevent double taxation to further incentivize FDI. This can be unilateral measures (tax exemptions or tax credits) or bilateral DTCs (Avi-Yonah 2007; Hearson 2021).

2.2 Tax Incentives and FDI: A Critical Appraisal

The empirical reality of the impact of tax competition on FDI is complex and differs between different types of investments (Morisset and Pirnia 2001, p. 81). Feld and Heckemeyer (2011) find in their meta study that the corporate tax rate has a statistically significant effect on FDI inflows and that this effect remains stable for different target regions and different investment motivations of firms (Feld and Heckemeyer 2011). Focusing exclusively on developing countries, Stausholm (2017) finds a small effect of lowering the effective tax rate on FDI, while Klemm and van Parys (2012) find that lower effective tax rates positively affect FDI flows to Latin American and Caribbean countries, but not to African economies.

The effect of tax competition in the case of a specific investment decision is often mediated by other factors (Dharmapala and Hines 2009). According to the *Global Investment Competitiveness Survey* that was commissioned by the World Bank in 2017, 'political stability and a business-friendly regulatory environment are most important in investors' decision-making' (Gonzales et al. 2017, p. 6). Tax incentives play a subordinate role, especially for investors that seek access to domestic markets or natural resources; while the effect of tax incentives is greatest for efficiency-seeking FDI that chooses between similar locations, incentives alone are not sufficient to attract investment (Kusek and Silva 2017, pp. 28–29). Wells and Allen (2001) further find that FDI did not decline when Indonesia withdrew tax incentives, and investors did not shift elsewhere, even despite other countries continuing to offer tax incentives. Morisset and Pirnia (2001) argue that government officials' views on incentives diverge from those of foreign investors, with the former overemphasizing the role of tax incentives for FDI. Some scholars therefore define tax competition as a discursive structure rather than a material constraint and argue that it is less the observable impact of tax competition, but rather the narrative of its effects that pushes states to offer tax incentives and reduced tax rates (Brauner and Steward 2013; Dagan 2003; Brauner 2013; Hearson 2021; Latulippe 2016; Bauerle Danzman and Slaski 2021). This narrative is particularly strong in many lower-income countries that are worried that other aspects of their investment climate that might be less easy to change may not work in their favour.

The effect of DTCs on FDI is not immediate. New tax treaties have been found to have a zero or negative effect on FDI, while this effect disappears with the

growing age of the DTC (Murthy and Bhasin 2015). Zagler (2023) links this effect to the uncertainty that surrounds the interpretation and application of DTCs in both jurisdictions.

The relative influence of different factors on FDI flows is context-bound and often differs depending on the income-level of the economy in question (see, for instance, Al Nasser 2007; Asiedu 2001; Lopes Dos Santos 2022). Middle-income countries have been found to benefit more from DTCs compared to other income groups (Shah and Qayyum 2015; Neumayer 2007). The positive effect of DTCs on FDI can further be reinforced by certain design choices such as the inclusion of tax sparing clauses[1] in DTCs between a developed and a developing country (Brooks 2009; Leibrecht and Rixen 2010; Azémar and Dharmapala 2019; Brown 2002). At the same time, however, DTCs that contain exchange of information clauses or anti-abuse rules may reduce FDI that has the purpose of tax evasion (Leibrecht and Rixen 2010, p. 69; Blonigen and Davies 2004, p. 602). Based on this observation, Lee and Kim (2022) find that the zero or negative effect of DTCs on FDI found in earlier studies (see, for instance, Blonigen and Davies 2004) disappears when controlling for countries with tax haven status. The same applies to Exchange of Information Agreements, which tend to decrease the attractiveness of a country for FDI (Aigner and Tumpel 2010, p. 50).

3 The Role of Reputation

While the starting point for arguments about tax competition is the assumption that taxpayers respond to changes in the tax regime of their (potential) host jurisdiction, a low tax rate, however, is not the only aspect of a potential host jurisdiction's tax regime that prospective investors are interested in. Instead, Latulippe and Proulx (2021, p. 161) identify four principles that firms consider in tax policy independently of their size or sector: tax certainty (including the protection of taxpayer rights), low compliance costs, confidentiality, and competitiveness (colloquially referred to as a low tax burden). Tax certainty refers to the 'creation and maintenance of stable regulatory and policy frameworks for tax administration, taxpayers and tax compliance' (Diaz de Sarralde et al. 2018, p. 2), and thereby describes a state of predictability for both taxpayers and tax administrations (Diaz de Sarralde et al. 2018, p. 2).

In contrast to a low tax burden, tax certainty is more difficult to measure in quantitative terms and requires in-depth knowledge of not only existing legislation, but also of the potential future behaviour of the government in question. As foreign investors hold imperfect knowledge about a potential host country, they may doubt the credibility of domestic commitments and legislation (Hong and Uzonyi 2018:

[1] Tax sparing clauses allow foreign investors to benefit from special tax treatment in the host country while calculating the tax liabilities towards their home countries as if this special treatment were not provided to them; see, for instance, Christians (2005, pp. 692–693).

1044). To bridge this gap, host governments and foreign investors alike refer to third parties to signal or evaluate the credibility of commitments such as investment climate rankings or bi- or multilateral legal tools (Besley 2015; Holden and Pekmezovic 2020; Schueth 2011; Poulsen 2015). The most prominent examples are Bilateral Investment Treaties (BITs) that protect the investment of residents of one state in the other. By concluding a BIT, host countries signal the protection of investors' private property as BITs provide credible commitment to investors that they will respect the initial terms of the investment and therefore reduce the risks for investors, who therefore may consider costlier investments or such with a longer time horizon (Bonnitcha and Aisbett 2013). Codifying their commitments in a legal tool that imposes penalties in the case of non-compliance may be particularly important for lower-income countries who 'need to convince foreign investors that they have "mended their ways"' (Haftel 2010, p. 351) and hence even more strongly rely on 'external' legal tools to reinforce and monitor their commitments (Haftel 2010, pp. 351–352). The same effect holds for membership in international organizations (IOs), as IOs constrain state behaviour and protect policy commitments and thereby increase the credibility of governments in the eyes of investors (Dreher and Voigt 2011; Dreher et al. 2015; Hong and Uzonyi 2018).

DTCs have been found to have a similar effect. In substantive terms, DTCs reduce the risk of double taxation and provide guidelines for the resolution of tax disputes (Avi-Yonah 2007). The adoption of rules that are consistent with international norms further increases legal certainty (Christians 2005, p. 708). By concluding a DTC, a jurisdiction may therefore signal their 'dedication to protecting and fostering foreign investment' (Christians 2005, p. 706). This is particularly valued by firms that are more likely to experience tax disputes about the appropriate estimation of transfer prices, e.g. by firms that trade in heterogenous inputs (Blonigen et al. 2014). Concluding bilateral DTCs may hence be in the interest of governments that want to signal attractiveness for FDI, even if a DTC is not always necessary to reduce the tax burden on foreign investors (Christians 2005).

The same is the case for multilateral tax policy: Similar to DTCs, the commitment to multilateral tax cooperation can have effects in two dimensions. On a substantive level, multilateral tax cooperation requires the adoption of legal commitments with varying degrees of bindingness and oversight that may reduce the scope for using domestic tax policy for attracting FDI. At the same time, the adoption of international standards and best practices may have reputational benefits by increasing the coherence and therefore certainty of international tax rules (Latulippe and Proulx 2021, p. 161). In contrast to DTCs, where the substantive commitments codified in the bilateral agreement do usually not curtail the ability of capital-importing economies to offer tax incentives to investors and where the substantive and the reputational implications of DTCs hence coincide, the pursuit of both policy goals at the same time is not always possible in multilateral tax cooperation frameworks. While the protection of policy space may require the rejection of international agreements that curtail the domestic policy space for tax incentives, this decision may have detrimental reputational consequences, and vice versa. In order to formulate their approach towards multilateral tax frameworks,

policymakers hence need to carefully balance the substantive implications of multilateral agreements for their policy space with the reputational effects that different levels of commitment to multilateral frameworks may have.

4 The OECD's BEPS Initiative and FDI

Building on the previous sections, the commitment to international tax cooperation touches on two partly contradictory policy goals: the protection of policy space to offer tax incentives and the improvement of a jurisdiction's reputation for 'good tax governance'. The subsequent section briefly discusses recent political developments in international tax cooperation around the OECD (Sect. 4.1), while Sects. 4.2 and 4.3 map the potential signalling and policy implications of various ways of engaging with the BEPS Project for FDI.

4.1 Current Developments in International Tax Cooperation

International tax cooperation is a comparatively recent phenomenon. After a number of attempts by the OECD to create a multilateral framework for the prevention of tax competition (1998 Report on Harmful Tax Practices) and to promote the exchange of information (Global Forum), the G20 mandated the OECD to develop a set of tools to comprehensively combat base erosion and profit shifting (BEPS) issues in 2012. BEPS refers to tax evasion and avoidance through which profits of multinational enterprises (MNEs) are artificially shifted to low or no tax jurisdiction, with the consequence that the tax base of the state where the MNE shifts profits away from shrinks (OECD 2013). The work of the OECD on BEPS was conducted under the so-called OECD/G20 Project on Base Erosion and Profit Shifting (BEPS Project), which was guided by the OECD's Committee on Fiscal Affairs (CFA) (Fung 2017, p. 78). The first phase of the BEPS Project ended with the adoption of a package of measures for 15 Actions that were summarized under the BEPS Action Plan in 2015 (Panayi 2018, p. 49; OECD 2013).

The BEPS Project followed the institutional trajectory of many other international economic negotiations: participation in the first phase of the BEPS Project (2013–2015) was restricted to OECD and G20 jurisdictions, with 'the Rest' featuring in a small number of 'outreach events' and workshops only. As a consequence, the BEPS Project structurally prioritized the interests of predominantly capital-exporting OECD and G20 states, while side-lining the interests of predominantly capital-importing economies from the Global South (Magalhaes 2018; Cobham et al. 2019). In 2016, non-OECD and non-G20 states were admitted to the BEPS Project under the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (Inclusive Framework). The Inclusive Framework is tasked with the implementation and further refinement of the BEPS outcomes (OECD 2016, p. 9).

Participation, however, comes with the obligation to implement four minimum standards that had been developed during the first (closed) phase of the BEPS Project.

In 2021, the members of the Inclusive Framework agreed on a Two-Pillar Solution to address both the taxation of the digital economy and tax competition. Pillar One allows market jurisdictions to tax the profits of the largest and most profitable digital MNEs (Amount A), and further streamlines the determination of transfer prices in this context (Amount B). The Global Anti-Base Erosion (GloBE) rules ('Pillar Two') introduce a global minimum tax of 15% that is collected as a top-up tax either by the host or the parent jurisdiction (OECD 2021).

4.2 The OECD/G20 Inclusive Framework on BEPS

Membership in the Inclusive Framework requires a commitment to the outcomes of the 15 BEPS Actions, including four minimum standards that are subject to peer review.

The purpose of the BEPS Action Plan is to re-align taxation with value creation. Subsequently, the BEPS Actions target the tax avoiding exploitation of differences between tax regimes, including the abuse of low tax rates by highly mobile capital, and offer a number of tools for both capital-exporting and capital-importing economies to reduce abusive behaviour.

Among the 15 BEPS Actions, only Action 5 directly concerns the policy space of jurisdictions to offer tax incentives for FDI. As a minimum standard, Action 5 must be adopted by all members of the Inclusive Framework and is subject to peer review. Action 5 requires members of the Inclusive Framework to abandon 'harmful preferential tax regimes', which the OECD defines as regimes that benefit highly mobile capital and therefore are at high risk of BEPS (Baggerman-Noudari and Offermanns 2018, p. 102). Tax incentives such as tax holidays or reduced rates are not considered harmful by default but are instead evaluated against a set of criteria that seek to identify the risk of BEPS arising from a preferential tax regime. A preferential tax regime is considered 'potentially harmful' if it does not require substantive business activities in the host country, is granted only for certain areas or types of investors, offers a zero or low effective tax rate, and lacks transparency, among other factors (Mosquera Valderrama 2020, pp. 449–451).[2] Preferential tax regimes that are classified as 'potentially harmful' are further evaluated by their economic effects and are considered 'actually harmful' (and therefore require changes by the relevant jurisdiction) if they create 'harmful economic effects' (Gerzova and Olejnicka 2018, p. 137). It is important to note in this context that tax incentives are evaluated against the tax system of the respective jurisdiction and not against the tax regimes offered by other jurisdictions, i.e. the evaluation of a tax regime as preferential happens on a case-by-case basis (Mosquera Valderrama 2021, p. 2023).

[2] For a detailed discussion of the requirements under Action 5, see Mosquera Valderrama (2020).

In order to prevent BEPS arising from preferential tax regimes, Action 5 requires members of the Inclusive Framework to link preferential tax regimes to substantive business activities and to increase the transparency around preferential tax regimes (Oguttu 2020, p. 65; Panayi 2018, pp. 77–79; OECD 2023). However, neither 'substance' nor 'harmful economic effects' are defined in detail by the OECD. The ambiguity about the application of the criteria for peer review creates legal uncertainty and may prompt policymakers to refrain from offering preferential tax regimes altogether (Mosquera Valderrama 2020, p. 456; Oguttu 2020, p. 65; Gerzova and Olejnicka 2018, p. 138).

While non-membership in the Inclusive Framework therefore protects the policy space of capital-importing economies to offer tax incentives, revisions of domestic frameworks may even be necessary for non-members to ensure that preferential tax regimes are not considered harmful by residence jurisdictions. This is especially important to consider in light of the increasing adoption of Controlled Foreign Company (CFC) rules by capital-exporting jurisdictions, which is also recommended under BEPS Action 3. CFC rules may, depending on their design, render some tax incentives ineffective and de facto yield tax revenues to the headquarter jurisdiction rather than benefitting the investor in the host state (Muyaa 2018). Policymakers in capital-importing countries may hence need to reconsider the design of their tax incentives in order to withstand heightened scrutiny and to remain effective, and further consider domestic measures to curtail the abuse of preferential tax regimes (Ogazón Juárez and Calderón Manrique 2018, pp. 8–9).

From a reputational perspective, membership in the Inclusive Framework may signal legal and tax certainty. First, the minimum standard of Action 14 seeks to strengthen dispute resolution procedures for tax treaty-related disputes, thereby strengthening the rights of taxpayers by requiring host states to establish and improve access to mutual agreement procedures (MAP) (OECD 2013, p. 23). By doing so, Action 14 may produce the same effects of legal and tax certainty that earlier studies identified in DTCs (see, for instance, Zagler 2023) and may therefore positively affect FDI flows. Second, as the OECD enjoys a central role in the diffusion of knowledge about international taxation, implementation of the BEPS Outcomes may also have consequences for the domestic tax bureaucracy of a member state and may therefore signal adherence to bureaucratic best practices and transparency in the domestic tax administration. The adoption of Actions 8–10 that revise transfer pricing guidelines, for instance, may reduce the risk of transfer pricing disputes and hence have a positive effect on the perceptions of tax certainty by foreign investors. Third, non-participation may lead to reputational damage in case of blacklisting, as has happened to several lower-income countries under the EU's black- and grey listing scheme (Council of the European Union 2017, 2019, 2020a, 2020b).

Under the Inclusive Framework, two policy goals collide. While Action 5, on the one hand, negatively affects the policy space of capital-importing economies to design tax incentives, membership in the Inclusive Framework may enhance the

reputation of a jurisdiction as investment destination by signalling certainty and commitment to international norms of 'good tax governance'. Non-membership, on the other hand, while protecting the scope for tax incentives, may have adverse reputational consequences.

4.3 GloBE

GloBE has significant implications for the investment policy of capital-importing economies. GloBE introduces a floor of 15% to the effective tax rate (ETR) of corporations with a consolidated annual turnover above EUR750 million, and therefore renders tax incentives that reduce the ETR below 15% ineffective for in-scope firms (Bammens and Bettens 2023, p. 155; Titus 2022, p. 418). The only exception to this rule concerns the Substance-Based Income Exclusion (SBIE) rule. The idea behind SBIE is to allow some degree of tax incentives for income derived from substantive economic activity, while more heavily targeting mobile capital ('excess profits') that is at risk of BEPS (Schoueri 2021, p. 545). In practice, this means that a share of the profits equivalent to 5% of the value of assets and payroll is excluded from the top-up tax (Englisch 2022, p. 862). In theory, SBIE renders tax incentives that reduce the taxation of routine profits below 15% viable (Englisch 2022, p. 864). In practice, however, the substance-based carve-out disadvantages more sophisticated activities that tend to yield a higher profit margin but require less assets and staff (Bammens and Bettens 2023, p. 163; Schoueri 2021, pp. 545–546). Further, the adjustment of existing tax incentives requires a high level of capacity and sophistication, and countries with less capacity may perceive repealing incentives altogether as the safest option (Mosquera Valderrama 2020, p. 452). Countries that adopt GloBE are further limited in their ability to apply incentives that target substantive economic activities or cash-based incentives insofar as adopting jurisdictions are expected not to adopt tax policies that counteract the intention of GloBE. Countries that do so do not qualify for collecting outstanding revenues themselves (Bammens and Bettens 2023, p. 158). As a consequence, mainly cash-based incentives such as tax credits or the deferral of taxation remain viable tools for attracting FDI, as such measures are not considered under GloBE (Bammens and Bettens 2023, pp.166–167). Such measures, however, are costly and often not viable for lower-income countries who lack the possibility to provide capital up front (Muyaa 2018, p. 37; Englisch 2022, p. 870).

Besides practical concerns about the policy space to offer an ETR below 15%, the implementation of GloBE or domestic equivalents 'might be contrary to international investment agreements […] that guarantee investors to benefit from certain tax incentives or tax regimes that must neither be removed *nor effectively undermined* for a determinate period of time' (Englisch 2022, p. 868). Especially BITs with stabilization clauses and those lacking a tax carve-out may therefore invite investor-state arbitration with potentially costly outcomes for capital-importing jurisdictions (Oguttu 2020, pp. 72–73; Lee 2020).

For capital-importing economies that host in-scope MNEs, not adopting a Qualified Domestic Top-Up Tax (QDMT) or raising the ETR of in-scope firms through changes in the tax regime could imply foregone revenues. In this case, policymakers face the choice between adopting GloBE and designing a domestic response to international developments such as an Alternative Minimum Tax (AMT) or reforming tax incentives (Eze et al. 2023). From the perspective of reputational signalling, an AMT may create legal uncertainty if the AMT is not considered a 'covered tax' under GloBE. To prevent legal uncertainty, 'the domestic minimum tax will need to generally align with the parameters for a qualified domestic minimum tax' (Christians et al. 2023, p. 17). Counterintuitively, policies that increase tax certainty hence coincide with the ability to offer tax incentives under GloBE: By adopting a QDMT, countries may ensure that the ETR is only increased for in-scope firms, while out-of-scope firms may continue to benefit from tax incentives that result in a lower ETR; achieving this effect in domestic responses instead may lead to a highly complex system of targeted incentives for different types of in- and out-of-scope firms (Englisch 2022, p. 2). At the same time, a QDMT may provide a higher degree of legal certainty than country-specific alternative responses (Christians et al. 2023, pp. 14–15).

Due to the design of the GloBE rules, the scope for balancing reputational goals with the ability to offer tax incentives is minimal. Instead, the key trade-off faced by policymakers in capital-importing economies concerns the costs and potential revue gains they could achieve when implementing a QDMT compared to domestic responses (Tandon 2022). Nevertheless, different responses to GloBE may have different reputational consequences due to the level of legal certainty around them.

5 Conclusion

The recent deepening of multilateral tax cooperation has implications for the policy space of countries to design tax incentives to attract FDI. Both membership in the Inclusive Framework on BEPS and commitment to GloBE require policy changes that constrain states in designing tax incentives and potentially risk investor-state arbitration in cases where existing tax incentives are withdrawn in line with the BEPS requirements. While the substantive implications of membership in the Inclusive Framework and of GloBE for tax incentives have been discussed widely in academic literature (see, for instance, Perry 2023; Bammens and Bettens 2023; Heitmüller and Mosquera Valderrama 2021; Mosquera Valderrama 2020; Titus 2022), the reputational implications of participating in or abstaining from multilateral tax cooperation frameworks have received less attention.

This chapter identified two partly contradictory policy objectives that governments of capital-importing economies may pursue in their international tax policy. While one concerns the protection of policy space for investment-facilitating tax policy, the other emphasizes reputational elements such as legal and tax certainty and 'good tax governance'. Membership in the Inclusive Framework may have

reputational benefits by signalling commitment to good tax governance best practices, legal certainty, and membership in the international community. This is especially the case insofar as non-participation may be sanctioned, as has been the case for some countries who joined after being blacklisted by the EU. Under GloBE, the scope for balancing both policy objectives is minimal and primarily concerns the degree of legal certainty associated with different responses to GloBE. Both examples illustrate the need for formulating international tax policy in close coordination between different parts of the government that are responsible for tax and investment policy (UNCTAD 2021).

While this chapter primarily focused on the balancing of investment-related policy goals in multilateral tax cooperation, policymakers may further consider other questions in their policy formulation, including the effectiveness of tax incentives for their specific economic circumstances and the trade-off between foregone tax revenues and economic benefits. Further, while some elements of the OECD's work on tax reduce the scope for tax incentives, others may support capital-importing economies in reducing tax avoidance by MNEs, thereby positively affecting government revenues.

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The Tax Carve-Out Clause in International Investment Law

Paloma García Córdoba

1 Introduction

International tax law and international investment law are closely related, falling under public international law (Schill 2011, 101) and being fundamental components of international economic law (Chaisse and Mosquera 2022, 192). Even with their shared foundational basis, some differences exist between these two legal frameworks, requiring a comprehensive understanding of their reciprocal interactions.

International investment agreements (IIAs) may include general exceptions and carve-outs to limit the scope of application of the treaty for specific topics. The wording of the general exceptions is more open-ended,[1] aiming to preserve a broadly defined policy space, while the exclusions (such as tax carve-outs)[2] are more detailed and precise (Henckels 2020, 559). The tax carve-out clause is a provision that states may include in IIAs and defines the range of tax issues the agreement covers. Given

[1] E.g.: Article 5 of the BIT between Guinea and Turkey (2013): "General exceptions: I. Nothing in this Agreement shall be construed to prevent a Contracting Party from adopting, maintaining, or enforcing any non-discriminatory legal measures: (a) designed and applied for the protection of human, animal or plant life or health, or the environment; (b) related to the conservation of living or non-living exhaustible natural resources (…)"

[2] E.g.: Article 20 of the BIT between Japan and Kenya (2016): "Taxation. 1. Nothing in this Agreement shall affect the rights and obligations of either Contracting Party under a convention on avoidance of double taxation. In the event of any inconsistency between this Agreement and any such convention, that convention shall prevail to the extent of the inconsistency. 2. Articles 3, 4, and 7 shall not apply to taxation measures".

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the importance and inherent complexities associated with tax carve-out clauses, it becomes imperative to conduct a detailed examination of them.

This chapter overviews tax carve-out clauses in IIAs and outlines some of their key features. The chapter is organized as follows: Section 1 introduces the topic, Sect. 2 provides the key features of tax carve-out clauses, Sect. 3 outlines the different types of tax carve-out provisions, and Sect. 4 discusses tax carve-out clauses in Investor-State disputes. The concluding Sect. 5 offers closing remarks to summarize the insights presented throughout the chapter.

2 Tax Carve-out Clauses in IIAs

2.1 Key Features of Carve-Outs in IIAs

Tax carve-out clauses can be total or partial. They may provide that the agreement will not apply to tax matters or measures (*total tax carve-out*).[3] Instead, the IIA can apply for tax matters or measures only in limited situations or regarding specific provisions (*partial tax carve-out*).[4]

Without a tax carve-out, all IIA provisions, including the dispute resolution clause, may apply to tax matters (Uribe and Montes 2019, 2). This suggests that a tax measure might be considered inconsistent with the protections provided by IIAs, making it a potential subject for deliberation within the context of investment arbitration (Pistone 2017, 17).

However, there are two significant drawbacks concerning the tax carve-out clause. First, its drafting is not uniform (Uribe and Montes 2019, 1). Second, the language employed is vague and ambiguous as clauses frequently refer to "taxation measures" or "matters of taxation",[5] without providing explicit definitions or specifications for these expressions. Consequently, arbitral panels must carefully interpret tax carve-out provisions.

[3] E.g., Article 11 of the BIT between Iran and Slovakia (2016): "(…) 3. The provisions of this Agreement shall not apply to public health insurance, taxation measures or pension schemes".

[4] E.g., Article 19 of the BIT between Japan and Jordan (2018): "Taxation Measures. 1. Nothing in this Agreement shall affect the rights and obligations of either Contracting Party under any tax convention. In the event of any inconsistency between this Agreement and any such convention, that convention shall prevail to the extent of the inconsistency. 2. Articles 3 and 4 shall not apply to taxation measures".

[5] Both terms are implemented in IIAs. For instance, the 2019 BIT between the Republic of Korea and Uzbekistan says: "Article 18. Taxation. 1. Except as provided in this Article, nothing in this Agreement shall impose obligations with respect to taxation measures (…)". In contrast, the 2019 BIT between the Indonesia and Singapore states: "Article 2. Applicability of agreement (…) 3. This Agreement shall not apply to: (…) (d) matters of taxation (11) in the territory of a Party, which shall, except as set out in Article 43 (Taxation), be governed by the domestic laws of the Party and by any tax treaty between the Parties".

At first glance, tax carve-out clauses in IIAs may seem quite similar. Minor distinctions, however, are critical in determining whether tax matters are covered by IIAs and discussed in investment arbitration (Simonis 2014, 239).

2.2 The Purpose of the Tax Carve-out Clause

There are several reasons to include a tax carve-out provision in an IIA. One significant reason is that taxation is a sensitive issue, and states are reluctant to undertake international commitments because double taxation conventions (DTCs) already cover them (de Nanteuil 2020, 361). States prefer to address international taxation issues through specific treaties (mainly DTCs) to maintain fiscal sovereignty (UNCTAD 2000, 36). States assume that DTCs already cover tax matters and, therefore, tax matters are excluded from IIAs (Wälde and Kolo 2007, 430). In that sense, the tribunal in the ConocoPhillips v. Venezuela case held that the existence of tax carve-out clauses is justified because there is already an extensive network of international agreements dealing with tax matters and that such agreements are excessively technical.[6]

Another reason is that states aim to address tax matters through domestic tax laws and procedures to protect their fiscal sovereignty. Tax carve-out clauses are negotiated primarily to protect the States' taxing powers and to prevent possible abuse of the investor-state arbitration process to file unmeritorious tax-related claims against the State parties.

As noted by the arbitration panel in Eiser v. Spain, tax carve-out clauses reflect the determination of States that tax issues should not become the subject of investment arbitration except in carefully limited circumstances.[7]

In addition, tax carve-out clauses prevent the so-called regulatory chill effect due to the threat of investor-state arbitration (Bantekas 2017, 514). In this sense, States want to prevent IIAs from limiting their right to regulate tax policies (UNCTAD 2007, 81). Some authors consider that these policies should not be solely driven or influenced by the concerns of foreign investors (de Melo Vieira 2014, 80).

2.3 The Genesis of the Tax Carve-out Clause

The first Bilateral investment treaty (BIT) on record, concluded between Germany and Pakistan in 1959, notably did not incorporate any tax carve-out clause, nor did it reference "matters of taxation". Additionally, the OECD's 1967 draft Convention

[6] ConocoPhillips Petrozuata B.V., ConocoPhillips Hamaca B.V., and ConocoPhillips Gulf of Paria B.V. v. Bolivarian Republic of Venezuela (ICSID Case No. ARB/07/30), Decision on Jurisdiction and Merits of 3 September 2013, para. 313.

[7] Eiser Infrastructure Limited and Energía Solar Luxembourg S.à r.l. v. Kingdom of Spain (ICSID Case No. ARB/13/36). Award of 4 May 2017, párr. 270.

on the Protection of Foreign Property did not incorporate provisions related to taxation.[8] However, Article 6 of the draft Convention subtly alluded to "derogatory measures".[9] In the commentary on this article,[10] it is clarified that invoking this clause (allowing the adoption of exceptional measures) is unnecessary if a state enacts taxes of a general and non-confiscatory nature. Consequently, the signatory states of the draft Convention affirmed their authority to impose taxes, presuming the legality of such taxes as part of the normal operations of a state.

Most tax carve-out clauses were introduced when foreign investors were predominantly preoccupied with concerns related to nationalization measures. However, nationalizations are no longer frequent, and foreign investors' concern is "indirect expropriation" (Wälde and Kolo 2008, 307). An indirect expropriation "results from a measure or a series of measures of a Party that has an effect equivalent to direct expropriation without formal transfer of title or outright seizure".[11]

The origin of tax carve-out clauses can be traced back to the United States Model BIT. The inclusion of the tax carve-out clause in the U.S. Model BIT dates to 1984. Specifically, Article XI of the 1984 U.S. Model BIT included a provision addressing the obligation to provide fair and equitable treatment (FET) to foreign investments concerning tax policies.[12] Also, the model 1984 model BIT allowed the application of the expropriation clause to tax-related matters and the possibility of initiating an arbitration in such cases.

A decade later, the U.S. Model BIT was updated. The 1994 version provided that the treaty shall impose any tax obligations, but the expropriation clause applied to

[8] OECD, Draft Convention on the Protection of Foreign Property (12 October 1967), https://www.oecd.org/investment/internationalinvestmentagreements/39286571.pdf

[9] "Article 6. Derogations. A Party may take measures in derogation of this Convention only if: (i) involved in war, hostilities or other grave public emergency of a nation-wide character due to force majeure or provoked by unforeseen circumstances or threatening its essential security interests; or (ii) taken pursuant to decisions of the Security Council of the United Nations or to recommendations of the Security Council or General Assembly of the United Nations relating to the maintenance or restoration of international peace and security. Any such measures shall be provisional in character and shall be limited in extent and duration to those strictly required by the exigencies of the situation".

[10] "The Legal Nature of the Derogations. (a) Article 6 provides for two groups of cases in which a Party may be justified in derogating from the Convention. These derogation clauses are declaratory of existing rules of international law. The Article, however, deals only with 'derogations' in the strict sense of the word, that is to say measures which in its absence would not other-wise be justifiable. No attempt is made here to provide for those cases of State action which, without being of a discriminatory character, accepted as a part of the normal governmental process. The imposition of taxation of a general and non-confiscatory character; (…)—these are all examples of measures which Parties are entitled to take and the legality of which, in relation to the Convention, is not dependent upon the invocation of a derogation clause. (…)".

[11] According to the Annex B.10 of the BIT between Canada and Guinea (2015).

[12] "Article XI 1. With respect to its tax policies, each Party should strive to accord fairness and equity in the treatment of investment of nationals and companies of the other Party. 2. Nevertheless, the provisions of this Treaty, and in particular Articles VI and VII, shall apply to matters of taxation only with respect to the following: (a) expropriation, pursuant to Article III (…)".

tax matters. Nonetheless, a new requirement was added: a prior procedure between each signatory state's competent tax authorities to determine whether the tax measure can be considered equivalent to expropriation (the so-called joint tax veto provision[13]). Subsequently, the U.S. model BIT had another reform in 2004 in which Article 21 was incorporated, and its wording has been maintained in the latest model BIT published in 2012.[14]

In summary, the advancement of the tax carve-out clause in the U.S. Model BIT reflects a tendency to increasingly strengthen the scope of tax protection under IIAs.

3 Different Types of Tax Carve-Out Provisions

There are two types of tax carve-out clauses (Pistone 2017, 20). They may provide that no tax matters will be covered by the agreement (*total tax carve-out*) or allow the application of some of the standards to tax matters (*partial tax carve-out*).

Chaisse distinguishes between tax matters that are excluded in a general manner, or only limited to the national treatment (NT) and most favoured nation treatment (MFN) clauses, or only to the fair and equitable treatment (FET) clause, or a combination of all of them (Chaisse 2016a, b, 158).

Incorporating a complete or total tax carve-out clause means that no tax law or regulation can be challenged under investment arbitration, regardless of its degree of inconsistency with any of a given IIA's obligations. However, partial carve-out clauses are present in most IIAs, with total carve-out clauses being exceptional. IIAs do not exclude the application of expropriation provisions but largely exclude the application of MFN and NT provisions in tax matters (Bantekas 2017, 514).

Excluding the MFN and NT provisions is essential to prevent foreign investors from selectively opting for the most advantageous treatment from available tax treaties. Without this exclusion, IIAs could potentially be manipulated to seek more

[13] The joint tax veto provision entails a collaborative process involving the tax authorities of the parties to the BIT to collectively determine whether a tax measure is equivalent to an expropriation. As a result, the authorities hold the power to exercise a "veto", thereby preventing the inclusion of such a measure in investment arbitration discussions.

[14] "Article 21: Taxation. 1. Except as provided in this Article, nothing in Section A shall impose obligations with respect to taxation measures. 2. Article 6 [Expropriation] shall apply to all taxation measures, except that a claimant that asserts that a taxation measure involves an expropriation may submit a claim to arbitration under Section B only if: (a) the claimant has first referred to the competent tax authorities21 of both Parties in writing the issue of whether that taxation measure involves an expropriation; and (b) within 180 days after the date of such referral, the competent tax authorities of both Parties fail to agree that the taxation measure is not an expropriation. 3. Subject to paragraph 4, Article 8 [Performance Requirements] (2) through (4) shall apply to all taxation measures. 4. Nothing in this Treaty shall affect the rights and obligations of either Party under any tax convention. In the event of any inconsistency between this Treaty and any such convention, that convention shall prevail to the extent of the inconsistency. In the case of a tax convention between the Parties, the competent authorities under that convention shall have sole responsibility for determining whether any inconsistency exists between this Treaty and that convention".

favourable tax treatment, potentially weakening the efficacy of tax avoidance and evasion regulations (UNCTAD 2021, 23).

Also, excluding tax matters from the scope of MFN and NT provisions within IIAs is a reasoned approach since states retain the prerogative to enact tax measures where a government may intentionally differentiate between domestic and foreign investors (Wälde and Kolo 2007, 434).

Opting to exclude tax matters from MFN and NT provisions in IIAs is a well-justified approach. This is because it acknowledges that states have the authority to implement tax measures deliberately distinguishing between domestic and foreign investors,

Expropriation provisions generally apply to tax matters, allowing for the initiation of arbitration proceedings based on an alleged tax measure that is considered equivalent to indirect expropriation. However, in such cases, arbitration panels often exhibit reluctance to hold states liable for expropriation related to tax measures (de Nanteuil 2020, 361). However, discussing a tax measure that is considered equivalent to an expropriation clause in an investment arbitration may be subject to fulfilling the joint tax veto mechanism.

3.1 Joint Tax Veto and Joint Tax Consultations Provisions

The so-called *joint tax consultations* allow specialized tax authorities of the respective signatory parties of IIAs to intervene when there is a dispute over a tax measure. It is an exception to the usual procedure that allows foreign investors to bring actions directly before an impartial arbitral tribunal, given that the matter is previously reviewed by the two signatory states of the agreement through their tax authorities (Davie 2015, 212). In other words, most IIAs do not exclude the application of expropriation provisions concerning tax-related claims. However, the tax authorities can jointly veto this treatment in a particular instance (Bantekas 2017, 514).

Under the joint veto mechanism, when a foreign investor alleges that a tax measure imposed by the host country amounts to expropriation, the investor is required to initially bring the matter to the attention of both the tax authorities in the host country and those in their home country. These tax authorities are given a specific timeframe during which they must jointly assess whether the measure qualifies as expropriation. If both tax authorities agree that the measure does not meet the criteria for expropriation, the foreign investor is barred from initiating arbitration proceedings. As a result, they possess the authority to determine whether the tax measure amounts to expropriation before the arbitration process begins, preventing the arbitral tribunal from addressing that specific issue.

However, there is generally no obligation to express an opinion and usually, a time limit is set for such an opinion;if no agreement is reached within this time limit, arbitration proceedings can be initiated. Hence, it is called a *joint tax veto* system when such a mechanism is a procedural prerequisite for initiating the arbitration and a "veto" by the authorities may occur (Vasudev 2021, 2039).

This system was initially created to minimize the potential abuse in investor-state arbitrations (Chaisse 2016a, b, 442). Also, it preserves the taxing power of the signatory States (Kolo 2009, 475) since States thus retain a certain level of control over investment arbitration in tax matters (Godolphin 2017, 97). The fact that this system is only established for tax-related concerns and not for other subjects is surprising and suggests that such issues are viewed from a political rather than a legal perspective (Bantekas 2017, 525). It also responds to an increased concern regarding fiscal sovereignty raised by these issues (Gordon and Pohl 2015, 31).

While some scholars have traced its initial appearance back to 1994, it was not until the mid-2000s that this mechanism began to gain importance, notably in agreements concluded by countries such as Canada, the United States, Peru, and Colombia (Gordon and Pohl 2015, 29).

Nevertheless, it is not a provision commonly implemented in IIAs.[15] As a result, in cases where IIAs explicitly allow the application of the expropriation clause for tax measures, it is generally without any veto or joint determination system.

On the other hand, certain IIAs introduce a comparable procedure for determining the presence of a tax measure within a dispute. Consequently, there are two distinct variants of this system: one involves a collaborative determination regarding the tax character (or lack thereof) of the contested measure, while the other entails a joint tax veto mechanism in which tax authorities acting jointly have the power to determine if the tax measure amounts to an expropriation (Wälde and Kolo 2007, 441).

While some authors, such as Uribe and Montes (2019, 6), view this as a practical mechanism to prevent tax disputes within the international investment regime, the system has faced numerous criticisms. Mainly, concerns are raised regarding potential political considerations by the intervening authorities, a perceived lack of impartiality, and the absence of participation from the affected investor. If the host state authority is the one deciding whether the contested measure is abusive, there is a likelihood that it may lean towards a ruling approving its non-abusiveness, as it is not an unbiased entity (Godolphin 2017, 101).

On the other hand, in some cases, tax authorities are allowed to decide not to intervene in the matter, i.e. they are not obliged to decide. In this sense, the joint tax veto is recognized as a prerequisite to the procedure and not a real prohibition to initiate tax-related claims (Uribe and Montes, 2019, 6).

Certain arbitral panels have acknowledged that a tax veto mechanism may not be required when referring the matter to tax authorities would have been futile.[16] However, a challenging concern is precisely delineating the circumstances deemed extreme enough to justify avoiding the veto procedure.

[15] A prior investigation revealed that, regarding the joint veto system, and based on an analysis of a sample of 2060 BITs concluded prior to 2013, only a minimal 3.6% of these treaties incorporated the joint veto mechanism specifically pertaining to tax-related measures (Gordon and Pohl 2015, 29).

[16] Yukos Universal Limited (Isle of Man) v. Russian Federation (PCA Case No. 2005-04/AA227). Award of 18 July 2014, párr. 1428.

4 Tax Carve-Out Clauses in the Context of Investor-State Disputes

Tax carve-out clauses directly impact the possibility of bringing an international investment arbitration based on a tax measure. The jurisdiction of an arbitral tribunal to address tax-related disputes depends on the existence, phrasing, and extent of such provisions. The tribunals have emphasized that applying tax carve-out clauses depends on its specific regulation in IIAs.[17]

The arbitral panel that ruled in the well-known "Yukos" case considered that it is not enough that a tax measure is implemented; it must also be carried out in good faith to apply the tax carve-out provision.[18] This means the tax carve-outs mere existence does not ensure its automatic application, and it must also be a measure that has been implemented by the host State in good faith in addition to its tax-related nature.

As a result, the so-called Yukos doctrine implies that if a tax measure is implemented in bad faith, it cannot be shielded by the tax-carve-out provision and may become subject to scrutiny by an arbitral tribunal. Consequently, numerous arbitral tribunals have faced the task of interpreting carve-out clauses following the Yukos case.[19]

Nevertheless, it is imperative to underscore that the Yukos case was exceptional.[20] The bad faith of the measure requires proof that the host States have engaged in

[17] ConocoPhillips Petrozuata B.V., ConocoPhillips Hamaca B.V., and ConocoPhillips Gulf of Paria B.V. v. Bolivarian Republic of Venezuela (ICSID Case No. ARB/07/30), Decision on Jurisdiction and Merits of 3 September 2013, para. 313.

[18] "Secondly, the Tribunal finds that, in any event, the carve-out of Article 21.1 can apply only to bona fide taxation actions, i.e., actions that are motivated by the purpose of raising general revenue for the State. By contrast, actions that are taken only under the guise of taxation, but in reality aim to achieve an entirely unrelated purpose (such as the destruction of a company or the elimination of a political opponent) cannot qualify for exemption from the protection standards of the ECT under the taxation carve-out in Article 21(1). As a consequence, the Tribunal finds that it does indeed have 'direct' jurisdiction over claims under Article 13 (as well as Article 10) in the extraordinary circumstances of this case". Yukos Universal Limited (Isle of Man) v. Russian Federation (PCA Case No. 2005-04/AA227). Award of 18 July 2014, para.1407.

[19] For example, in the case Watkins Holdings S.à r.l. and others v. Kingdom of Spain (ICSID Case No. ARB/15/44) and other recent cases against Spain in which the implementation of a new tax was discussed.

[20] "The Parties refer to the conclusions of other tribunals that have addressed the question whether a measure constitutes a bona fide tax. In Yukos, the tribunal found that the respondent State had launched a "full assault" on the investor and its beneficial owners in order to bankrupt the investor and to appropriate its assets while, at the same time, removing its chief executive officer "from the political arena". No extraordinary conduct of this sort is alleged by Claimant, nor is it established by the record before the Tribunal". SolEs Badajoz GmbH v. Kingdom of Spain (ICSID Case No. ARB/15/38). Award of 31 July 2019, para. 276.

grossly abusive conduct, resulting in a loss of the benefit of access to the tax carve-out clauses.[21]

The case mentioned above demonstrates the importance of how arbitral tribunals interpret tax carve-out clauses that IIAs do not expressly incorporate assessments about the good faith or underlying intentions of the State underlying the application of the tax carve-out clause. Instead, integrating these concepts has evolved through the interpretations rendered by investment arbitration panels.

On the other hand, it is noteworthy to observe that if an IIA only includes MFN and NT exclusions concerning tax matters without any additional explicit references to taxation, a tax measure could be deemed a violation of other provisions within the IIA. Consequently, it may be subject to an investment arbitration.

In the Alghanim v. Jordan case, the presence of a partial tax carve-out clause that only excluded MFN and NT did not prevent the arbitral panel from emphasizing they had jurisdiction over tax matters.[22] Such matters could still be deliberated under investment arbitration since the partial tax carve-out only addresses specific aspects.[23] This underscores the importance for states to be particularly aware of this aspect.

5 Concluding Remarks

In conclusion, this chapter has conducted an overview of tax carve-out clauses in IIAs. It emphasized the critical importance of these clauses in the growing relationship between international investment law and international tax law.

However, it is essential to acknowledge the challenges posed by inconsistencies in the drafting of tax carve-out clauses and the use of imprecise terminology. The consequence of ambiguous and inconsistent tax carve-out provisions is a lack of legal certainty, thereby presenting challenges for arbitral panels in interpreting and applying the vague terms implemented in tax carve-out clauses. This chapter underscores the significance of addressing these drafting issues to ensure the effective implementation of tax carve-out clauses within IIAs.

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[21] "Nonetheless, the Tribunal does not consider that the circumstances of the introduction of the Levy could be said to reach the high bar set by the cases in which a tribunal has concluded that the conduct of a State is such as to merit the loss of the benefit of the Article 21(1) "carve out". Masdar Solar & Wind Cooperatief U.A. v. Kingdom of Spain, ICSID Case No. ARB/14/1. Award of 16 May 2018, para. 291.

[22] Alghanim v. Jordan, Award of 14 December 2017, para. 124.

[23] "Article 4(3)(b) appears in a provision of the BIT that guarantees national and most-favoured nation treatment as well as fair and equitable treatment. In this context, it is understandable that the treaty drafters would have included an express clause providing that preferential tax treatments not afforded to investors could not give rise to an investment treaty claim. This provision in no way restricts the ability of an investor to claim that he has been subjected to an arbitrary measure contrary to the ordinary application of the law otherwise applicable to all". Alghanim v. Jordan, Award of 14 December 2017, para. 124.

Notwithstanding the presence of tax carve-out provisions, it is evident that investment arbitration remains susceptible to adjudicating tax-related matters. Tax carve-out clauses substantially impact the treatment of tax-related matters within investor-state disputes. The jurisdiction of an arbitral tribunal to adjudicate tax-related disputes depends on the presence, phrasing, and extent of these clauses. In summary, this chapter has underscored the crucial role of tax carve-out clauses in IIAs.

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Tax and Trade and Investment Instruments in Sustainable Development Goals Achievement

Sharon Waeytens

1 Introduction

In 2015, the UN Member States adopted the 17 SDGs, with the aim to achieve them by 2030 (UN 2024). The SDGs include the promotion of economic, environmental, and social development that aspires to meet the needs of the present without compromising the ability of future generations to meet their own needs. The achievement of the SDGs is in serious jeopardy because of multiple, mutually reinforcing and intersecting crises such as the COVID-19 pandemic, climate change, and conflicts. Hence, countries urgently need to take action if they want to achieve the SDGs by 2030 (UN 2022).

Governments have different tools to achieve development goals. Development assistance and humanitarian aid are traditionally seen as means to achieve development goals, but governments can also contribute to achieving development goals through other policies. *This contribution demonstrates that tax, trade, and investment policy instruments can contribute to the achievement of the SDGs in four ways*: (i) by (in)directly financing the SDGs, (ii) by influencing taxpayer's behaviour, (iii) by collecting information, and (iv) by redistributing wealth, income, and assets. This chapter also illustrates that *governments should use a combination of tax, trade, and investment policy instruments to achieve the SDGs*. Finally, the chapter highlights the *need for policy coherence*.

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2 Tax, Trade, and Investment Policy Instruments Can Contribute to SDGs Achievement in Four Ways

2.1 Financing the SDGs

Tax policy instruments can contribute to the achievement of SDGs by financing them. Revenue from taxes can ultimately flow to the SDGs through the state treasury department, or they can be allocated directly to fund the SDGs. *The state treasury department can use the tax revenue for the provision of public goods such as healthcare, education, and public transportation* (Avi-Yonah 2006). This indirectly finances the SDGs as they are linked to the provision of public goods. For example, SDG 3 aims for healthy living, which can be ensured by providing healthcare facilities, SDG 4 strives for inclusive and equitable education, and SDG 6 aims at building resilient infrastructure (UN 2022).

Tax revenue can also finance the SDGs directly. The solidarity levy on airline tickets is an example of this. France introduced this minimal levy[1] to finance UNITAID, which aims to ensure that the world's poorest and most vulnerable have access to medicines and diganostic kits of excellent quality at reduced prices to prevent and threat HIV/AIDS, tuberculosis, and malaria. The tax revenue is thus earmarked to fund SDG 3.3, which aims to end epidemics of AIDS, tuberculosis, and malaria (Unitaid 2023; Ministère de la Transition écologique et solidaire 2024; Article 99 Code Géneral des impôts annexe III; European Commission 2006).

Investment policies can raise private funding and at the same time encourage investments in sustainable economic activities through finance products. Sustainable finance takes into account ESG considerations when making investment decisions (European Commission 2024b). They use among others ESG portfolio screenings, with the final aim of having a long-term positive sustainability impact (Popescu et al. 2021). These products include sustainability funds and bonds including green, social, and mixed sustainability bonds that focus on one or more ESG-or SDG-related themes or sectors, with the overall aim of contributing to poverty reduction and equality (UNCTAD 2022; Zhan and Santos-Paulino 2021). Based on an OECD report (OECD 2023b) private finance mobilised for developing countries mostly contributes to the SDGs aimed at developing economic infrastructure (SDG 8 and 9), reducing inequalities (SDG 10), and advancing climate action (SDG 13). The share of mobilised private finance contributing to SDG 7 (affordable and clean energy) and SDG 1 (no poverty) were 18% and 17%, respectively. However, despite a recent surge in investment products with sustainability themes,[2] they still only represent about 4% of the global fund market (UNCTAD 2022). Moreover, almost

[1] « Taxe de solidarité sur les billets d'avion » is a minimal levy of 1 euro for economy-class tickets and 40 euros for business class tickets, which applies to all passengers on all flights out of France.

[2] United Nations Conference on Trade And Development estimates that the value of sustainability-themed investment products in global finance markets amounted to USD 5.2 trillion in 2021, up 63% from 2020 (UNCTAD 2022).

90% of funds and bonds are concentrated in and for developed countries (UNCTAD 2022).[3] Finally, it is debatable that funds through green bonds[4] are used in real terms for climate-friendly projects or become a source of greenwashing for the issuer (Bhutta et al. 2022; UNCTAD 2022; Zhan and Santos-Paulino 2021). Most of the existing bonds are self-labelling and lack consistent standards and high-quality data to assess their sustainability credentials, raising concerns about greenwashing (UNCTAD, 2022).

Also trade finance can contribute to SDG achievement. Trade finance is crucial as 80 to 90% of world trade relies on trade finance (such as trade credits, insurance, and guarantees), and no access to trade finance can limit a country's trading potential and result in missed oppurtunities to use trade as an engine for development and an important means to achieve the SDGs (UN 2015; UNCTAD, Trade & the SDGs 2024; WTO 2024). Based on the findings of an WTO-IFC joint study on trade finance deficits, Economic Community Of West African States' four largest economies—Ivory Coast, Ghana, Nigeria, and Senegal—could gain an additional 8% annually in trade flows if they could raise the share of trade supported by trade finance to the average African level of 40%. In ten years, this would total USD 140 billion in additional trade (WTO 2023).

2.2 *Influencing Behaviour in Line with the SDGs*

Tax rules can steer the behaviour of individuals and companies in the direction desired by governments. The most recent examples of tax rules with a regulatory purpose are tax rules to combat climate change (SDG 13) or simply environmental taxation/green taxation (Anton Anton 2023). These taxes aim to introduce price signals that internalise the externalities associated with greenhouse gas emissions so that taxpayers direct their behaviour towards those alternatives that are more sustainable.

The Revision of the Energy Tax Directive[5] is an example thereof. This Directive aims to support the European Commission's commitment to achieve the greenhouse gas emissions reductions objectives and air pollution reduction. The Commission intends to achieve these objectives by removing disadvantages for clean technologies and introducing higher levels of taxation for inefficient and polluting fuels so that the taxation of motor and heating fuels reflect better the impact they have on the environment and health. The most polluting fuels will be taxed the highest. *In concreto*, the Directive will among others eliminate incentives for fossil fuel use,

[3] Developing economies, especially Least Developed Countries, face tremendous barriers to developing their own sustainable fund markets or benefiting from the international market, because of their limited market size and the higher risks perceived in their capital markets (UNCTAD 2022).

[4] Green bonds promote investment in climate action (SDG 13), affordable and clean energy (SDG 7), and sustainable cities and communities (SDG 11).

[5] Which is part of the European Green Deal and the EU's Fit for 55 package.

introduce a ranking of rates according to environmental performance and switch from volume to energy content-based taxation (European Commission 2023; European Commission 2021a, b; European Council for an Energy Efficient Economy 2023). This Directive steers behaviour in line with SDG 13 through the imposition of (higher) taxes including the removal of tax exemptions on polluting activities. In the fight against climate change, also new taxes have been introduced such as the Spanish plastic tax, i.e. an indirect tax of EUR 0.45/kg on the manufacturing of, importation, or intra-EU acquisition of non-recycled plastic (Ley 7/2022). In addition, behaviour is steered towards products with less harmful effects on the environment through tax incentives such as the US solar investment tax credit,[6] the Malaysian Green Income Tax Exemption, and Indian tax deductions for profit and gains from business of collecting and processing bio-degradable waste (Indian Income Tax Department 2024).

However, a number of considerations should be taken into account when using taxes to influence taxpayer behaviour. First, indirect taxes mostly do not consider the ability-to-pay principle and therefore create a negative redistributive effect. This can be remedied by introducing a subsidy scheme. Without a subsidy scheme, the social disadvantaged will not be able to absorb this higher cost and fall below the subsistence levels, and making that social adjustment in indirect taxation itself makes that tax very complex (Vanistendael 2021). Second, the taxpayer may perform a cost–benefit analysis and decide that paying the tax is cheaper than changing behaviour, or may relocate the undesired activity (Deeks and Hayashi 2022).[7]

Tax incentives to influence the economy could go against the principle of equity and fairness and even act as a form of discrimination against those who do not take advantage of them. Others consider tax reliefs as a fair adjustment. An overly broad range of tax incentives can make the tax system complex and limits the principles of economic freedom and competition (Vanistendael 2021). To avoid potential market distortions, tax incentives for investment should be transparent and granted on the basis of automatic criteria (e.g. the amount invested) (UNCTAD 2022). Lastly, when using tax incentives it is important to monitor whether the behaviour of taxpayers changes. If not, the tax rule only creates negative consequences in terms of less tax revenue for the country (Mataba 2023).

Also, investment policy instruments are used to influence behaviour in line with the SDGs. Countries of outward investors have already various measures in place to stimulate sustainable investments such as providing information services and support services, financial incentives, and political risk insurances or investment insurances (Sauvant and Gabor 2023; Stephenson et al. 2021; Zhan and Santos-Paulino 2021). Mostly, the support measures are provided only on condition that the investments in developing countries have a positive impact on sustainable development

[6] The US solar investment tax credit which is a tax credit that reduces the federal income tax liability for a percentage of the cost of a solar system that is installed during the tax year (US Department Energy 2024).

[7] Taxes will change taxpayer behaviour in line with a regulatory objective only if the cost of compliance is lower than the tax the taxpayer will pay if he/she does not change his/her behaviour, and the after-tax benefits of non-compliance are lower than the after-tax benefits of changing their behaviour (Deeks and Hayashi 2022).

and outward investors undertake environmental and social impact assessments (Sauvant and Gabor 2023).

An increasing number of international investment agreements contain specific references to foreign direct investments that are conducive to the SDGs. However, only 30% of new IIAs concluded since the adoption of the SDGs contain provisions that directly relate to the SDGs. China, the EU, and the USA have already included internationally accepted standards and guidelines in their IIAs such as the UN Guiding principles on Business and Human Rights (Stephenson et al. 2021). On 17 November 2023, the EU and Angola signed the Sustainable Investment Facilitation Agreement, the first EU agreement of this kind (The European Parliament 2024).[8] The European Commission states that: "*The EU is pursuing such agreements to promote sustainable investments in its engagement with African partners. The EU-Angola SIFA will make it easier to attract and expand investments while integrating environment and labour rights commitments in the EU-Angola relationship*". In such agreements, the sustainable development policies and levels of protections must be consistent with each party's commitments to internationally recognised standards and agreements to which it has committed. However, the Agreement does not establish a minimum level of protection in terms of environmental and labour standards (The European Commission 2022; SIFA).

Governments have also used national investment regulation to discourage companies to invest in certain countries, in order to persuade these countries to change their policies (e.g. to stop violations of human rights). For example, the USA discouraged US pension funds from investing in Chinese companies. Members of Congress and the White House criticised a company's Board's proposal to increase its exposure to Chinese companies to diversify its investments and improve its rates of return. In a letter, the Members of Congress and the White House expressed "grave concerns with the planned investment in Chinese companies on grounds of both investment risk and national security" leading to the cancellation of those investments (Deeks and Hayashi 2022). As a response to the Russian–Ukraine conflict, there was a dramatic increase in the adoption of investment policy measures in the first quarter of 2022. The UNCTAD report mentions that "*They included outright prohibitions or limitations on FDI, but also measures that affect a broad range of foreign transactions and, indirectly, investment activities. Among them are sanctions targeting financial institutions, trade and transport restrictions; and travel bans and asset freezes affecting hundreds of individuals and entities*" (UNCTAD 2022).

Trade policy can encourage sustainable imports and exports and discourage unsustainable imports and exports, directly contributing to SDG 12 aiming at sustainable consumption and production patterns. States could do this by limiting the production and consumption of products that have unnecessarily negative social and environmental costs and could provide preferential trade terms for sustainable products (Baumgartner and Bürgi Bonanomi 2021). Governments could also subsidy SDG-friendly sectors and prohibit subsidies to sectors that are contradictory to SDG

[8] The EU and Angola still need to approve it according to their own procedures (The European Parliament 2024).

achievement (UN 2015).[9] States could also promote sustainable products and services through differentiation in import duties (by increasing the import duties on unsustainable imports and reducing or exempting import duties on sustainable imports) (Deeks and Hayashi 2022; Gyamfi et al. 2022; Van Os and Knottnerus 2016). When imposing (higher) import duties, it should be monitored that importers do not pass on their increased costs to the customers or they cut costs by reducing jobs and wages, eventually not achieving the intended goals. In addition, it is important to verify that such import duties do not violate General Agreement on Tariffs and Trade obligations (Article XXI of GATT; Deeks and Hayashi 2022). Moreover, certain existing Free Trade Agreements and IIAs limit the ability of countries to take such measures, and therefore FTAs and IIAs should be amended accordingly.

FTAs and Regional Trade Agreement (RTAs)[10] can also include labour and environmental commitments and sustainability impact assessments (Chong and Srebot 2023).[11] Consequently, countries could retain the option to revise or terminate their FTAs and RTAs at any time if assessments show that they have negative impacts on the SDGs (Van Os and Knottnerus 2016). Since 2011, the EU includes labour and environmental commitments into their FTAs through a Trade and Sustainability Development (TSD) chapter. However, each World Trade Organization (WTO) member may set its own environmental standards at the level it considers appropriate, as long as they are in line with the organisation's standards. This means different protection standards between countries. Although compliance with these provisions is legally required, there is no enforcement mechanism which ensures compliance by the trade partners (Van Os and Knottnerus 2016). In both American and Canadian FTAs, non-compliance with the labour provisions will be subject to a fine or otherwise sanctioned. In order for the TSD chapter to be effective, scholars recommend to include the TSD chapter in the dispute settlement procedure and to establish an effective enforcement mechanism, either economic consequences or sanctions as in the US trade policy (van't Wout 2022; Mortensen 2017; Van Os and Knottnerus 2016).[12]

[9] States could, for example, prohibit subsidies that contribute to overfishing.

[10] Developing countries would have more potential gains from South-South trade because of the similarity of their stages of development and competitiveness levels, so that the countries involved do not have to fear being swamped by imports after trade liberalisation. South-South trade can be facilitated by RTAs. However, research shows that also RTAs can have negative welfare and environmental effects. Alberto Chong and Carla Srebot empirically evidenced that there is a negative link between entering into RTAs and completion of primary education by boys (not by girls) in developing countries. According to them this is due to the increased opportunity cost in households whose adult members tend to be unskilled and relatively poor, as they have higher incentives of having their children work either outside or inside the households (Chong and Srebot 2023).

[11] Also, Urs Baumgartner and Elisabeth Bürgi Bonanomi argue that future FTA should focus more on potential impacts on the SDGs, rather than on decreasing tariffs only (Baumgartner and Bürgi Bonanomi 2021). Laura Barros and Inmaculada Martinez-Zarzoso also advocate for including environmental provisions in FTAs (Barros and Martinez-Zarzoso 2022).

[12] Another possibility is to conclude 'deep agreements', which are agreements that go beyond typical tariff reductions, but cover very diverse policy areas that may affect trade and investment including labour standards and environmental issues (World Bank 2023; Chong and Srebot 2023; Barros and Martinez-Zarzoso 2022; Van Os and Knottnerus 2016).

Countries have also used trade sanctions to coerce other countries to change their behaviour in line with the SDGs. Trade sanctions include import restrictions, export controls, the freeze of assets, travel bans, denial of licences to operate in a foreign country, suspension or prohibition of transactions with companies from a foreign country. In extreme cases, these restrictions can take the form of total embargoes that bar trade and financial relations between the state and the targeted country. The scope of economic actions is generally broad and therefore they can harm innocent participants in the target economy and the interests of the country imposing them. However, it is also possible to implement "smart sanctions" that are narrowly tailored to the objectionable behaviour. A number of considerations must be taken into account when imposing such trade sanctions. If not, these sanctions may not achieve their intended purpose or may have unintended negative consequences. This is the case when governments do not withdraw these sanctions when the target changes its behaviour, when the purposes of these sanctions are unclear, or when those sanctions are imposed without understanding the dynamics of foreign economies. Furthermore, it is claimed that these trade sanctions are complex and expensive for companies because they have to set up systems to avoid business with actors on the sanction list and it can also discourage companies from pursuing lucrative business oppurtunities. The export control system has been criticised for being too restrictive, cumbersome, outdated, and inefficient behaviour (Deeks and Hayashi 2022).

2.3 Collecting Information

Information is key to guiding behaviour, which is why there has been a recent surge in SDG reporting requirements. These initiatives generally collect information on the impact companies have on their external stakeholders (people and the environment). *CSR reporting* is an example of this. Through the European CSR Directive, the EU requires all large and listed companies to disclose information on the risks and opportunities arising from social and environmental issues and the impact of their activities on people and the environment (European Commission 2024a; UNCTAD 2022; Stephenson et al. 2021; Zhan and Santos-Paulino 2021).[13]

Correct information about products can also increase sustainable consumption, if citizens want to make sustainable choices or governments wish to provide favourable trade measures to sustainable products. Private actors have used ecolables, certification mechanisms, and consumer guides to differentiatie sustainable and unsustainable products. However, a study on the measures to distinguish between unsustainable and sustainable fish in Switzerland shows that these measures are still inadequate because they are vague and non-transparent, leading to arbitrary

[13] Governments of non-EU countries could include provisions relating to CSR reporting in binding IIAs or require ESG compliance and reporting from companies investing in their territory.

interpretations of sustainability. They can also be discriminatory and violate existing WTO obligations. They concluded that differential treatment should be based on a holistic, inclusive, and transparent definition of a sustainable product. This definition should be based on a common set of criteria, which is openly shared among stakeholders. Furthermore, a regulation could be designed to exclude specific production practices when they violate certain principles, without penalising similar products or entire production systems, and to impose binding requirements on all producers wishing to market their products as sustainable (Baumgartner and Bürgi Bonanomi 2021).

Information is also important to generate tax revenue (which can fund the SDGs). Developing countries generally have a lack of information on (non)tax residents. Developed countries can help developing countries collect information through tax rules that force their tax residents to disclose information about thier activities in developing countries. In the USA, for instance, certain foreign investors are exempt from 30% tax on interest received from US debtors only if they declare under penalty of perjury that they are a foreign person and provide identifying information (Deeks and Hayashi 2022).

2.4 Redistribution of Wealth, Income, and Assets

The redistribution of wealth, income, and assets is related to SDG 1 aiming at ending poverty, SDG 2 to end hunger, achieve food security and improved nutrition, SDG 8 that promotes sustained, inclusive, and sustainable economic growth, full and productive employment and decent work for all, and naturally to SDG 10 aiming at reducing inequalities within and among countries.

Taxation has a redistribution function, aimed at reducing inequalities that results from the normal operation of a market-based economy (Avi-Yonah 2006). Tax policy could ensure that poor individuals pay little or no tax or help raise revenues required for inequality-reducing spending measures. The main way tax policy can reduce income inequality is through progressive income taxation, i.e. designing a tax system so that the average tax rises with income (IMF 2018).

A recent example of a tax with a redistributive function is the windfall tax, which was reintroduced as a result of the energy crisis. The main objectives to introduce such a (temporary) measure were to generate additional tax revenue to cover exceptionally high public financial needs and to capture profits generated by companies due to or during unexpected circumstances including market-spanning distortions, broad legislative failures, or other structully unfair circumstances such as war and pandemics. The recently introduced windfall tax captured extraordinary profits generated by energy companies due to favourable external conditions while generation costs remained low for those companies. The additional revenue generated was used to help the most vulnerable households and businesses and therefore this tax was considered as an effective instrument for redistribution and an appropriate means to

achieve horizontal and vertical equity (Anton Anton 2023; Magelhaes and De Lillo 2023).[14]

Prices of goods and services can have a different impact on low-income compared to high-income households. For example, high energy prices have a regressive impact, meaning that they tend to disproportionally affect less financially advantaged households compared to those that are wealthier. This is because lower-income households typically spend a greater proportion of their income on energy-related expenses such as heating and electricity. As a result, the burden of increased energy prices is felt more heavily by those EU countries with lower incomes. The distributional impact is thus influenced by the varying consumption patterns of energy products among different groups (Anton Anton 2023). *Therefore, investment and trade policies can have an impact on the (re)distribution of wealth, income, and assets.* In response to energy price increases, low-income households are compensated for increased taxation of fossil fuels used for heathing by being given access to financing for low-carbon and energy-efficient goods and appliances (European Commission 2021b). In addition, the EU has put forward initiatives such as the Social Climate Fund, which has been created to provide funding to the EU Member States so that households in energy or transport poverty are directly supported through a.o. investments in energy efficiency and renovation of buildings, clean heating and cooling and integration of renewable energy, as well as in zero- and low-emission mobility solutions (European Commission 2024c). Trade policy instruments can include price (stabilisation) measures for vulnerable groups or duty-free and quota-free market access for sustainable products originating from least developed countries.

3 The Need for a Combined Approach

The above overview shows that tax, trade, and investment policy instruments can contribute to achieving the SDGs. Trade measures affect importers and exporters of goods and services. Investment instruments capture foreigners investing in the country, and these may be others than those importing or exporting goods and services. Tax law reaches all income earned by tax residents and all income arising in the country. *Indeed, each policy instrument reaches different individuals and firms.*

[14] To coordinate unilateral measures of the EU Member States, Regulation 2022/1854 was adopted by the council. It introduced a temporary revenue cap on 'inframarginal' electricity producers and a temporary solidarity contribution on excessive profits generated by activities in the oil, gas, coal, and refinery sector. The Regulation also seeks to guide the use of the revenue generated from these taxes so that it is directed towards supporting vulnerable households and energy-intensive companies while ensuring that the support measures are aligned with the objectives of greenhouse gas neutrality, energy efficiency, and achieving greater energy independence. Considering that the revenue of windfall taxes (as per the EU regulation) is, at least partially, used to finance environmental programmes and projects, windfall taxes have also a positive impact on the protection and preservation of the environment (SDG 13) (Anton Anton 2023).

In addition, these policy instruments target different behaviour and interests. The interaction between FTA rules of origin and intra-group prices makes this clear. The rules of origin of an FTA that are based on the value-added criterion can limit the manipulation of transfer prices. The rules of origin of an FTA foresees that exports to other member countries are tariff-free if they prove that the exported products originated within the FTA. Therefore, the value-added criterion could be satisfied by increasing the amount of local value added or reducing the price of imported materials to ensure that the good qualifies as originated in the country of assembly. A high transfer price, on the other hand, reduces the VA ratio of the final product inside the FTA country and therefore the presence of the rules of origin restricts the manipulation of the transfer price. The multinational can thus opt: (i) to fully manipulate transfer prices to avoid tax payments at the expense of the preferential tariff of the FTA, (ii) purchasing goods inside an FTA country to comply with the ROO and eliminate tariffs, (ii) adjust its transfer prices to comply with the ROO to eliminate tariffs and pursue partial tax avoidance (Mukunoki and Okoshi 2021). This shows that multinational enterprises have to choose between different interests (tax avoidance or benefiting from the preferential tariff of an FTA), as these tax and trade policy instrumens act on different interests.

This means that a greater number of individuals, companies, and transactions are targeted by using a variety of different instruments (Deeks and Hayashi 2022), and that these policies complement each other and do not replace each other. Indeed, both the public and the private sector are crucial for achieving the SDGs (Zhan and Santos-Paulino 2021; UN 2015). Tax is the tool of choice to generate public funding, and investment and trade policy instruments can be used to raise private funding. The fact that these policy instruments complement each other and not replace each other can also be demontrated by the example of a tax on highly polluting cars. When a government introduces a tax on polluting cars, the intention is to change the taxpayer's behaviour so that they will no longer drive polluting cars but climate-friendly cars. A taxpayer's behaviour will generally change in the event he/she will bear the burden of the tax on the undesired activity. This will be the case if the taxpayer continues to pursue that activity and cannot shift the tax burden onto someone else through higher prices. By reducing the after-tax benefits from the activity, the tax encourages the taxpayer to spend the resources and efforts to alternative activities. Of course, taxpayers will only be able to switch to alternatives to the extent that the market offers them and they are not more expensive than the price an individual has to pay for the polluting car and the additional tax burden (Deeks and Hayashi 2022). Investment and trade policy instruments could encourage the market to make those sustainable alternatives available (e.g. inventing, producing, importing a sustainable alternative product or service) (Mann et al. 2005). Without suitable alternatives, tax rules alone cannot effectively change the behaviour towards climate-friendly cars. *Consequently, to achieve the SDGs, governments should use a combination of tax, trade, and investment policy instruments.*

4 The Need for Policy Coherence

Since tax, trade, and investment policy instruments respond to different interests and behaviour, they can either cancel or reinforce each other. In light of the effectiveness of these instruments, it is therefore important to understand the interaction between different policy instruments. If not, combining different policy instruments could become an obstacle to achieving the SDGs.

This can be demonstrated by the recently introduced *global minimum tax of 15%,*[15] *which will have an impact on tax incentives that many developing countries use to attract foreign investment* (OECD 2021 2023a, b; Mataba 2023; UNCTAD 2022). Profit-based incentives such as reduced Corporate Income Tax rates and tax holidays will significantly reduce the effective tax rate of MNEs and thus most likely lead to the payment of taxes under the global minimum tax, preventing developing countries to use tax incentives to attract foreign investors. Developing countries could shift to tax incentives that promote investment with better sustainable development performance (Mataba 2023; UNCTAD 2022). *However, IIA/ Bilateral Investment Treaty commitments can have constraints on the removal of tax incentives.* This is evidenced by the *Occidental v. Ecuador* case.

In this case, investors succesfully applied the investor-state dispute mechanism with regard to the review of Value Added Tax exemptions. A company was exempt from VAT on all purchases related to a specific output activity. After some years, the Ecuadorian government revoked the VAT exemption and decided that all refunds on VAT were reclaimed because the VAT would have already been accounted for in the profit-sharing formula. The arbitration panel concluded that the fair and equitable treatment provision of the BIT was violated because the requirement of stability was violated as there was no indication that VAT had been accounted for in the profit-sharing formula and no clarity was provided on the sudden change (Bammens 2016). The artibration panel considered stability of the legal and economic context as an essential part of a fair and equitable treatment.[16] This case shows that investors can argue that (tax) policy changes can violate their right to a stable regulatory environment or their legitimate expectations in relation to their investment. The abovementioned case *Occidental v. Ecuador* amounted to USD 1.7 billion plus interest, roughly the equivalent of Ecuador's annual health budget for seven million people. *IIAs thus limit governments' policy space and autonomy to respect, protect, and fulfil the SDGs, as it could weaken or abandon public interest regulations out of fear*

[15] Known as the Pillar Two project which aims to ensure that large multinational enterprises pay a minimum level of tax on the income arising in each of the jurisdictions where they operate. That way, they want to counter Base Erosion and Profit Shifting and generate more tax revenue (globally). More tax revenue will benefit the SDGs by directly and indirectly funding them (OECD 2021).

[16] Note that a fair and equitable treatment was not defined in that specific BIT and that the arbitration panel considered stability in the economic and legal context as an essential element of a fair and equitable treatment considering that both parties confirmed the following in the preamble: "in order to maintain a stable framework for investment and maximum effective utilization of economic resources" (Bammens 2016).

of these claims and associated budgetary effects (Van Os and Knottnerus 2016).[17] *IIAs and BIT provisions could therefore be an obstacle to changing tax law in line with achieving the SDGs.*[18] Moreover, developing countries would lose tax revenue because the tax increase from the global minimum tax would go to developed countries, and at the same time, developing countries would lose the benefit of the investment attraction, given that IIA provisions are an obstacle to remove those tax incentives (UNCTAD 2022).

The above shows that achieving the SDGs requires *coherent policies.* Ideally, policy coherence would be agreed on a multilateral basis, but governments can also take action now, following the EU's example. Indeed, the EU and its Member states are already committed to policy coherence for development (European Commission, PCD).[19] Furthermore, it is recommended that different policy instruments within one country are more aligned and that regular consultations are organised between the various authorities (tax authorities, customs administrations, investment promotion agencies, etc.).[20]

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[17] Of course, this only applies if the BIT does not provide a carve-out for tax matters. In many cases, the carve-out will only apply to some protection mechanisms such as for the national treatment and the most-favored-nation clause so that, for example, the expropriation clause can still be applied in tax matters (Bammens 2016).

[18] Therefore, scholars claim to abolish the investor-state dispute settlement mechanism because currently the result is a race-to-the-bottom that facilitates multinationals making sourcing decisions based on low-regulatory environments and labour laws (Van Os and Knottnerus 2016).

[19] European Commisison, "Policy coherence for development", https://international-partnerships.ec.europa.eu/policies/european-development-policy/policy-coherence-development_en. Accessed 26 September 2023.

[20] Hiroshi Mukunoki and Hirofumi Okoshi state that the interaction between customs and tax authorities is rare. However, the World Customs Organization is working with the OECD and World Bank Group to encourage bilateral communication between both authorities (Mukunoki and Okoshi 2021).

The UNCTAD also endorsed the importance of cooperation between investment and tax policymakers (UNCTAD 2022).

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Part II
Global Tax Governance: Transparency, Fairness, and Regulation

Introduction to Part II

Julien Chaisse

The interconnected nature of the global economy ensures that there are no clear boundaries between the realms of tax, trade, and investment law. Instead, every nation state confronts a bewildering mix of policy choices across these regulatory areas as well as various constraints on the ability to achieve national policy priorities. Every cross-border business or investment decision accordingly involves navigating a web of overlapping regulatory regimes characterized as much by conflict as coordination.

Following geo-political and socio-economic distinctions among states established decades and even centuries ago, today's dominant trends in transnational institution building and standard and rule-setting across tax, trade, and investment reflect deeply inconsistent historical and contemporary aims and capacities of political leaders. The confluence of both interdependence and incompatibility among tax, trade, and investment law institutions and instruments around the world produces constant conflict and renegotiation regarding the terms of cross-border cooperation across states. The way we understand and resolve these conflicts among regulatory areas and across states deeply impacts the livelihoods of individuals around the world as international agreements direct and shape the movement of goods, services, and capital. The rise of digital giants such as Amazon and Google has only underscored the complexities involved as both companies and nation states use and manipulate rules and standards to achieve sometimes congruent and sometimes incongruent goals.

As a result, understanding the complexities of the intersecting fields of tax, trade, and investment law is crucial. Policymakers, legal practitioners, academics, and business leaders must navigate these challenges to strike a balance between

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competing interests, achieve equitable outcomes, and promote sustainable development. The goal of this book is accordingly to introduce and explore these complex interactions and to analyze how the convergence of these three key international legal areas influences global patterns of economic development and shapes the way nations compete and collaborate on the world stage.

A vital part of the production of the book was a weeklong workshop organized in June 2023 at the Lorentz Centre in Leiden, the Netherlands.[1] Several of the book chapters were presented there in their early forms. In light of the discussions that took place during this workshop, we invited scholars at early and later stages of their careers and with different backgrounds in tax, trade, and investment law, to contribute to this book. The result is a comprehensive book with 19 chapters addressing four overarching themes. These themes have been divided into four parts.

Part I, **The Tax, Trade, and Investment Governance Landscape,** introduces readers to the complex governance aspects of tax, trade, and investment regimes. It examines the challenges states face when navigating conflicting policy choices and demonstrates how national policies intersect or conflict with international obligations. The four chapters in this part explore governance issues, including the struggle of lower-income states to have their concerns addressed in international arenas and the interplay between national tax and investment policies.

Chapter "Introduction to Part I" introduces this Part and provides an overview of the themes reflected in its chapters. In Chap. "A Survey and Critique of International Tax Governance Reform," Karen Brown explores the governance problems faced by lower-income states in international tax policymaking, highlighting the dominance of the OECD and advocating for more inclusive global tax governance. In Chap. "International Tax and Investment Policy: Navigating Competing Demands," Katharina Kuhn examines the challenges national policymakers face at the intersection of tax and investment policy, including the trade-offs between attracting foreign direct investment and complying with international tax best practices. In Chap. "The Tax Carve-Out Clause in International Investment Law," Paloma García Córdoba discusses the evolving relationship between taxation and international investment agreements, focusing on the language and purpose of tax carve-out clauses and their impact on the relationship between investment law and tax law. Sharon Waeytens closes out this Part with Chap. "Tax and Trade and Investment Instruments in Sustainable Development Goals Achievement," which explores how tax, trade, and investment policy instruments can contribute to achieving the Sustainable Development Goals and the importance of policy coherence in this

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process. Together, these chapters provide a comprehensive overview of the legal, social, economic, and distributive aspects of the contemporary tax, trade, and investment landscape.

Part II, **Global Tax Governance: Transparency, Fairness, and Regulation,** presents an analysis of the link between global tax governance and the convergence of tax, trade, and investment regimes. It highlights the influence of these regimes on evolving international governance structures and emphasizes the foundational pillars of transparency, fairness, and regulation in promoting equitable economic practices worldwide. Through detailed examinations of beneficial ownership transparency, treaty shopping, and tax policy fairness, this part underscores the importance of creating a coherent and fair international tax system that enhances global economic stability.

Julien Chaisse provides an introduction to in this Part in Chap. "Introduction to Part II". In Chap. "Competition and Complementarity of EU and FATF Beneficial Ownership Transparency Orders," Leyla Ates, Andres Knobel, Florencia Lorenzo, and Markus Meinzer analyze the relationship between the European Union and the Financial Action Task Force regarding beneficial ownership transparency, assessing collaborative or competitive efforts to improve transparency. In Chap. "Dealing with Treaty Shopping Across the Tax, Trade, and Investment Regimes," Frederik Heitmüller examines the practice of treaty shopping within and across tax, trade, and investment realms, focusing on policy synchronization and multilateral approaches to manage this issue effectively. In Chap. "Hidden Dynamics and Hierarchies in Tax Policy: A Critical Assessment of Fairness in OECD, EU, and UN," Ezgi Arik analyzes different conceptions of fairness by intergovernmental organizations and highlights the need for a globally recognized definition of fairness in international tax policy. In Chap. "Transparency and Transformation: Rethinking Tax Governance in the Mining Sectors of Tanzania and Kenya," Anne Wanyagathi Maina focuses on tax transparency in the mining sector, evaluating global initiatives and national reforms to improve governance and combat corruption in the extractive sector.

Part III, **Interactions and Overlaps Between Tax, Trade, and Investment Policies,** focuses on the interlinkages among tax, trade, and investment policies, using case studies and examples of relevant legal texts to illustrate how these interactions play out in practice. It explores how international investment agreements can affect tax policy and the potential for duplicative disputes across double taxation conventions and investor-state dispute settlement provisions. The part also discusses unique cases, including a trade-based side agreement between Australia and India that overrides a double tax convention, which provide rich detail regarding the complexities and potential conflicts in these intersecting legal fields.

Frederik Heitmüller provides an introduction to this Part in Chap. "Introduction to Part III." In Chap. "The Interaction Between IIAs and DTCs: Potential for Overlap and Reform Proposals," Javier Garcia Olmedo discusses investor-state dispute settlement (ISDS) cases related to tax measures, examining the overlap between investment treaties and double tax conventions and proposing potential reforms. In Chap. "The Intersection of Treaties on Tax and Trade: A Case Study of Australia

and India," Sunita Jogarajan and Tania Voon analyze a unique trade discussion between India and Australia, focusing on a side agreement that appears to override an existing double tax convention and examining the implications of this override for international trade and investment policy. In Chap. "The Legal Transplant of EU Standards in Taxation: A Case Study of the ACP Post-Cotonou Agreement," Irma Mosquera and Filip Debelva discuss the Post-Cotonou Agreement, highlighting the potential legal transplant of EU standards and the compatibility of its provisions with existing tax, trade, and investment agreements.

The fourth and final part of the book, **Reforming Global Governance,** addresses ongoing reforms in global governance at the international, regional, and domestic levels. It explores challenges for policy coherence arising from the persistent popularity of tax incentives, including in furtherance of green transition goals, as well as proposed designs and prospects for better decision-making through new regional (particularly African and Latin American) and international governance structures, including the rationale and likely impacts of the elevation of the United Nations in international tax law-making. Through these discussions, it outlines the potential pathways for future reforms in global governance that take a holistic approach to address tax, investment, and trade issues while considering the differences between developed and developing countries.

Irma Mosquera opens this Part with an introduction in Chap. "Introduction to Part IV." In Chap. "Optimizing Policy Energies: The Role of Tax Incentives in International Trade and Investment," Julien Chaisse examines the impact of tax incentives on trade and investment, providing insights into designing tax incentive regimes that balance international legal frameworks with national policy objectives. In Chap. "Tax, Trade and Investment for Green Transition," Suranjali Tandon addresses the need to balance tax incentives and carbon pricing to encourage a green transition, analyzing instruments such as the EU's Carbon Border Adjustment Mechanism and the Inflation Reduction Act. In Chap. "Breaking the Cycle of Domination in Global Tax Governance: Africans Defying Asymmetries and Seizing Opportunities," Lyla Latif discusses the role of African nations in global tax governance, highlighting their proactive participation in international tax discussions and advocating for equitable treatment. And finally, closing out the book, in Chap. "Decision-Making in a Proposed African Union Tax Governance Structure," Afton Titus argues for creating an institutional structure within the African Union to address international tax challenges and coordinate policies to deal with these challenges effectively.

Throughout these 19 chapters, this book demonstrates the difficult trade-offs today's policymakers continue to face in articulating and achieving domestic and international economic goals. It explores how political leaders grapple with a lack of coherence across global regulatory areas that has been forged and facilitated through a history of policy divergence and incoherence as well as deep and persistent inequities among states. A key theme throughout the book is the struggle of lower-income states to have their concerns addressed in global regulatory arenas through decades of institution building around cross-border coordination that has consistently been characterized by policy designers and architects as projects that

sought prosperity for all. Many of the chapters consequently take issue with the continued dominance of highly developed countries that is especially prominent in international tax policymaking, and call for a reconstitution of governance structures to include meaningful input across disparate socio-economic regions.

By providing a comprehensive analysis of these key issues, this book equips readers with a nuanced understanding of the complex relationships among domestic and international tax, trade, and investment law regimes. It offers insights and potential solutions to understand how nation states as well as businesses and investors continue to navigate this challenging legal landscape.

1 Part I: The Tax, Trade, and Investment Governance Landscape

Allison Christians

1.1 Chapter 1: "Introduction to Part I"

The Chapters in this Part introduce readers to the multifaceted and interconnected governance aspects of tax, trade, and investment regimes. Navigating these regimes, states find themselves contending with conflicting and sometimes mutually exclusive policy choices, necessitating difficult trade-offs among internal goals as well as between domestic and international goals. The chapters demonstrate that there is very little policy coherence across the global regulatory areas, and that policymakers do not always seem to acknowledge the inconsistency of their own approaches in each area. In some cases, national policy choices respecting cross-border taxation seem to conflict directly with competing national policy goals in cross-border trade and investment. In other cases, national policy choices in one area seem to be constrained by pre-existing international obligations in another. Sometimes, national policy choices seem wholly constrained by historical international ones. When a need for reform in one area arises, multilaterally embedded policy choices in the other areas may interfere if not prevent reform. Each chapter in this Part examines various aspects of these conflicts, with an eye to understanding the legal, social, economic, and distributive aspects of the contemporary tax, trade, and investment landscape.

In Chap. "A Survey and Critique of International Tax Governance," Karen Brown sets the stage by exploring the ongoing struggle lower-income states experience in having their voices heard and their concerns addressed in these global regulatory arenas. In particular, Karen Brown highlights the ongoing governance problems that arise in international tax policymaking owing to the persistent centering of the

OECD, an intergovernmental club of highly developed countries, to the practical exclusion of all other nation states and in particular the states of Sub-Saharan Africa. Indeed, the OECD has dominated global tax policymaking for over 50 years, despite voluminous critique from excluded countries as well as tax law and governance scholars. The basic governance problem emanates from the complicated history of the international tax order, which evolved through historical patterns of geo-political and economic imbalance among states and has always been characterized by a core lack of agreement on any terms that would satisfactorily define multilateral cooperation on tax matters. Because of this lack of agreement, the international tax landscape developed as a networked transnational order filled with contradiction and contestation, most of which ignores the global welfare aspects of each of its institutional and procedural components. Brown's chapter accordingly examines the deleterious policy impacts of the current institutional choices and advocates for a reconstitution of global tax governance to include meaningful input from Africa and other low-income regions in order to achieve a fairer global tax system.

In Chap. "International Tax and Investment Policy: Navigating Competing Demands," Katharina Kuhn introduces readers to the ways in which national policymakers contend with competing policy goals at the intersection of tax and investment. This intersection involves a basic incompatibility as states seek to participate in the evolving international tax regime as it responds to excessive tax competition, but also pursue national economic development and industrial policy strategies aimed at attracting foreign direct investment, including by offering tax incentives of various kinds. She notes that states might attract foreign investment capital by participating in multilateral tax governance, which potentially increases their reputations by presenting them as compliant with international tax best practices, but they do so at the risk of losing the ability to use tax incentives to accomplish their goal of attracting foreign capital. The tradeoff between cooperating with multilateral efforts to reduce tax-motivated cross-border planning and using domestic tax rules to make the jurisdiction more attractive to outside investment creates difficult policy choices. Kuhn's chapter demonstrates the difficulty by mapping the interactions of these competing policy goals under the OECD/G20 Inclusive Framework on BEPS and the 2021 Two-Pillar Solution.

Paloma García Córdoba continues the exploration of the difficult intersection between national investment and tax policy goals in Chap. "The Tax Carve-Out Clause in International Investment Law." The chapter introduces readers to the complicated and evolving relationship between taxation and international investment agreements. In broad strokes, international investment agreements aim to attract foreign capital to a jurisdiction (typically, a less-developed state) by offering assurances that investments will be protected against future costs arising from regulatory action. For example, an international investment agreement might entitle investors to treatment in the country that is "fair and equitable" and non-discriminatory when compared to local investors and investors from other countries, and most such agreements contain anti-expropriation provisions that assure investors their investments will not be at risk of becoming state-controlled in the future. Some contain the so-called stabilization clauses, which effectively grant tax incentives that the

state can never revise or revoke. Without a tax carve-out clause, investors might view virtually any change in national tax policy as inconsistent with these agreements, even if the reforms were widely applicable but especially if they primarily impacted cross-border business and investment. Many such agreements have tax carve-out clauses to prevent a too broadly interpreted agreement from effectively preventing national tax reforms. Thus, a tax carve-out clause, as the name suggests, seeks to separate national tax policy from national investment policy. Few agreements have total tax carve-outs but many have partial tax carve-outs. Córdoba accordingly examines the language and purpose of tax carve-out clauses and demonstrates their critical importance in the relationship between international investment law and tax law.

Finally, in Chap. "Tax and Trade and Investment Instruments in Sustainable Development Goals Achievement," Sharon Waeytens introduces the reader to a way to reconcile the competing and conflicting aspects of tax, trade, and investment policy instruments. She does so by examining how each of these governance regimes can contribute to the achievement of the Sustainable Development Goals, a set of policy statements which all of the UN member states have agreed in principle to promote (or at least, refrain from impeding). The Sustainable Development Goals constitute an agreed multinational policy with which otherwise incompatible national governance regimes must strive to be coherent. Waeytens explains why and how tax, trade, and investment policy instruments reach different individuals and companies and target different behaviors and interests, and notes that these policy instruments can either cancel or reinforce each other, making it important to understand the interaction among them. The chapter concludes that to achieve the Sustainable Development Goals, governments should use a combination of the policy instruments and make policy coherence a priority.

2 Part II: Global Tax Governance: Transparency, Fairness, and Regulation

Julien Chaisse

2.1 Chapter 6: "Introduction to Part II"

Part II of the book presents an analysis of the link between global tax governance and the convergence of tax, trade, and investment regimes, highlighting the influence of these regimes on evolving international governance structures. It posits global tax governance as a critical area in international law and relations, deeply interwoven with transnational norms that regulate the cross-border flow of goods,

services, and capital. This Part addresses key issues like transparency, fairness, and regulatory measures, essential for promoting equitable economic practices worldwide. The importance of this subject is underscored not only by its economic consequences but also by the legal issues governing international tax operations, shaping the way nations interact and compete on the global stage.

Transparency, fairness, and regulatory measures serve as foundational pillars in the architecture of global tax governance, each playing a distinct yet interconnected role in shaping equitable international economic practices. Transparency refers to the clarity and openness with which tax information is disclosed and shared among countries, enabling the detection and prevention of tax evasion and illicit financial flows. This concept is critical for establishing a trust-based framework where states can cooperate effectively in the enforcement of tax laws and the exchange of taxpayer information. Fairness, on the other hand, embodies the principle that tax obligations should be distributed in a just manner, ensuring that entities and individuals contribute to public finances in proportion to their economic activities and capabilities. It aims to mitigate disparities and prevent the undue burden on any single group, fostering a sense of equity within and across nations. Regulatory measures, comprising both domestic legislation and international agreements, provide the legal backbone for enforcing transparency and fairness. These regulations are designed to close loopholes, standardize tax practices, and facilitate cooperation among tax authorities worldwide. The importance of these legal concepts in global tax governance cannot be overstated; together, they underpin efforts to create a more coherent and fair international tax system that curtails evasion, enhances global economic stability, and promotes sustainable development.

The scholarship on the legal aspects of global tax governance emphasizes the necessity for clear, fair, and enforceable regulations governing international taxation. This framework encompasses tax treaty agreements, strategies to combat tax evasion and avoidance, and mechanisms for resolving disputes both between states and involving states and corporations. Establishing such a legal framework is crucial for leveling the playing field, ensuring that multinational companies and wealthy individuals pay their fair share in the economies they benefit from. Furthermore, the economic and political aspects of global tax governance, including tax competition, base erosion and profit shifting, and the relationships between tax havens and major economies, offer a holistic view of the legal hurdles and possible solutions in this area.

This section introduces four chapters, each examining a specific aspect of global tax governance. Chap. "Competition and Complementarity of EU and FATF Beneficial Ownership Transparency Orders," by Leyla Ates, Andres Knobel, Florencia Lorenzo, and Markus Meinzer analyzes the relationship between the European Union and the Financial Action Task Force (FATF) regarding beneficial ownership transparency. It assesses whether the efforts of these entities to improve transparency around beneficial ownership are collaborative or competitive, providing a detailed review of the manipulation of legal vehicles to hide ownership details for unlawful purposes. The evolving dynamics between the FATF and EU directives

are depicted, moving from a cooperative to a potentially competitive stance in establishing global legal standards for ownership transparency.

Frederik Heitmüller's contribution in Chap. "Dealing with Treaty Shopping Across the Tax, Trade, and Investment Regimes," discusses the practice of treaty shopping within tax, trade, and investment realms, focusing on how entities restructure jurisdictionally to benefit from more favorable bilateral treaties. This chapter extends the discussion to how treaty shopping impacts trade and investment, advocating for policy synchronization and harmonization across these areas. It critically evaluates different responses to treaty shopping, underscoring the significance of international collaboration and multilateral approaches for effective management of this issue.

Ezgi Arik's Chap. "Hidden Dynamics and Hierarchies in Tax Policy: A Critical Assessment of Fairness in OECD, EU, and UN" investigates how different conceptions of "fairness" by organizations like the OECD, EU, and UN shape tax policy debates. Arik points out that the absence of a globally recognized fairness definition allows the predominant ideologies to dominate international tax discussions, possibly overlooking alternative views. This section calls for a reconsideration of the fairness concept in tax policies and its repercussions on global tax regulations.

Finally, Anne Wanyagathi Maina's Chap. "Transparency and Transformation: Rethinking Tax Governance in the Mining Sectors of Tanzania and Kenya" focuses on tax transparency in the mining sector, highlighting transparency's role in combating corruption and mismanagement of resource income. Maina reviews global initiatives and national reforms, evaluating how tax transparency standards can improve governance in the extractive sector. The necessity of aligning transparency efforts with the unique socio-economic and political contexts of different nations to ensure effective enactment and foster sustainable governance practices is emphasized.

Drawing on these findings, a more substantive conclusion can be articulated by integrating the concept of digitalization in global tax governance, an area witnessing significant evolution. The digital economy poses novel challenges for international tax rules, particularly in terms of attributing profits to different jurisdictions and addressing the tax challenges associated with digital giants. The OECD's efforts in proposing a two-pillar solution to address the tax challenges arising from digitalization and the global minimum tax offer a contemporary lens through which to view the themes of transparency, fairness, and regulation. These initiatives aim to ensure that profits are taxed where economic activities and value creation occur, and to establish a global minimum tax rate that curtails the race to the bottom in corporate taxation.

Collectively, these chapters provide a thorough examination of the complex nature of global tax governance, illustrating its effects on international relations, legal challenges, and economic behaviors. Through a combination of legal scrutiny, policy analysis, and case studies, Part II offers significant insights into the ongoing debate on global tax governance and its implications for worldwide equity and collaboration.

3 Part III: Interactions and Overlaps Between Tax, Trade, and Investment Policies

Frederik Heitmüller

3.1 Chapter 11: "Introduction to Part III"

The chapters in this part deal with overlaps of the policy areas of tax, trade, and investment. Complementing the focus on interactions at the governance level adopted in Part I of this book, the chapters in this part focus on individual cases to show how interlinkages between the different areas play out within specific international agreements and in cases heard by investment tribunals.

In Chap. "The Interaction between IIAs and DTCs: Potential for Overlap and Reform Proposals," Javier Garcia Olmedo discusses four recent investor-state dispute settlement (ISDS) cases in which tax measures were disputed. He focusses on whether investment arbitration tribunals found that they had jurisdiction to judge the matter or whether they deferred to a double tax convention (DTC). He shows that investors have increasingly sought to litigate tax issues through ISDS, presumably due to the higher protection for investors that investment treaties offer. The outcomes of these cases are mixed. In some, the investment tribunal found indeed that it did not have jurisdiction or that the matter was subject to a DTC rather than an investment agreement. In others, they upheld the claim of the investor.

From a policy perspective, this type of interaction can lead to a waste of administrative resources if the same subject matter is discussed in different venues at the same time (i.e., DTC dispute settlement provisions as well as ISDS). From the perspective of the government, the impact that investment treaties can have on tax policy may often have been unintended, at least by those departments that are responsible for tax policy.

Compatibility clauses, such as tax-carve out clauses in investment treaties, are a possible solution. These have become prevalent in more recently signed investment agreements. However, as Olmedo discusses, not all of these agreements clarify who should interpret such clauses, which means that in practice the question of jurisdiction is answered by the investment tribunal itself.

In Chap. "The Intersection of Treaties on Tax and Trade: A Case Study of Australia and India," Sunita Jogarajan and Tania Voon analyze a unique trade discussion between India and Australia in which a tax measure is the subject matter. Following demands by Indian businesses, the Indian government convinced its Australian counterpart to sign a side letter to the recently concluded Australia–India Economic Cooperation and Trade Agreement, in which Australia committed to suspend its withholding tax on fees for technical services paid to service providers resident in India. The case is striking because the question of whether a withholding tax

on fees for technical services may be levied is always one of the key negotiated matters in DTCs. Hence, the trade-based side agreement overrides the provision of the DTC between India and Australia, which allows any of the two states to levy a withholding tax on technical services. This peculiar arrangement is likely due to the fact that allowing withholding tax under tax treaties has been a long-standing and consistently defended policy of India. It is likely that the Indian government would not have wanted to create precedent by renegotiating the DTC with Australia. Moreover, the unilateral concession by Australia has more advantages for India than an amendment of the DTC, as the latter would have likely been reciprocal and thus would have prevented India from levying withholding tax on payments to Australian service providers.

The authors further analyze whether the Australia's agreement to remove withholding tax on payments to India is consistent with Australia's WTO obligations, notably the GATS. They find that even though Australia could possibly defend itself on grounds of economic integration, there is a risk that third countries may challenge the preferential treatment that Australia grants to Indian service providers.

In Chap. "The Legal Transplant of EU Standards in Taxation: A Case Study of the ACP Post-Cotonou Agreement," Irma Mosquera Valderrama and Filip Debelva discuss the Post-Cotonou Agreement, a so-called partnership agreement between the EU and African, Caribbean, and Pacific (ACP) countries. This agreement deals with tax, trade, and investment matters, even though these issues may have already been regulated in more specific agreements. The authors focus on one particular provision, namely the "EU Standard of Tax Good Governance." This Standard refers mainly to policy standards developed by the Organization for Economic Co-operation and Development. The authors argue that the inclusion of the Standard in the Post-Cotonou agreement is an attempt by the EU to export norms to third countries and could therefore result in a legal transplant. The significance of such a transplant is critically discussed by the authors who highlight that some of the principles and policy goals included in the agreement are incompatible with each other and that compliance with some of its aspects would require far-reaching policy reforms by the countries concluding the Post-Cotonou agreement. Hence, they may not have any effect in practice, as the more specific provisions of tax, trade, or investment agreements remain in place.

The overlaps described in the chapters in this Part are not uniform. Rather, one can note different degrees of "encroachment" of one policy area upon another: The tax provisions contained in the Post-Cotonou agreement are largely open norms which are unlikely to conflict with the specific provisions of double tax conventions. The cases discussed in Garcia Olmedo's chapter are more challenging. Some of the tax-related investment disputes surveyed deal with matters that are outside the immediate ambit of DTCs. Some of them also involve cases in which no DTC applies, for instance because the immediate entity undertaking the transaction was situated in a low-tax jurisdiction. Finally, the Australia-India trade agreement provision discussed by Voon and Jogarajan is arguably the clearest case of an overlapping claim to govern an issue, as withholding tax on services are specifically dealt with under DTCs.

What is the way forward to address such overlaps and interactions? Countries could contemplate entering into comprehensive agreements covering all three issues in a coherent way rather than negotiating area-specific agreements. Nevertheless, there may be good reasons why, for instance, countries want to enter into a trade agreement but not a DTC with certain countries. Overlaps could also be addressed through administrative approaches. Over the last decade, the idea of "policy coherence" has gained increasing traction and is mentioned in the United Nations Sustainable Development Goals. Some countries have created specific institutions or started processes to review their policy processes for coherence among each other. The hope is that different government departments would be encouraged to enter into dialogues about the respective policies promoted. Such initiatives can be a productive way forward, but increasing the coherence of a country's tax, trade, and investment policies with each other should not be the end point. Indeed, the concept of "policy coherence" can be used in different ways: On the one hand, it can refer to policy coherence within one country to make sure that different arms of the government go in the same direction and do not undermine each other. On the other hand, it can refer to the objective that a country's policies should not undermine the globally shared goal of fostering global development in a cooperative way. For example, a country may adopt tax, trade, and investment policies that are internally coherent with each other. But if these are all based on a zero-sum competition with other countries, they would fail the test of coherence with this overarching ideal.

4 Part IV: Reforming Global Governance

Irma Mosquera

4.1 Chapter 15: "Introduction to Part IV"

This Part addresses the reform of global governance that is currently taking place at international, regional, and domestic level. In this Part, attention is given to tax incentives, green transition, and to the design of new regional (i.e., Africa) and international (United Nations) governance structures.

The topic of tax incentives influences global governance since countries are in the process of revisiting their own rules to align their tax incentives with the global minimum tax (Pillar Two) and their compatibility with countries' investment and trade commitments. These changes present new challenges to policymakers when revisiting or drafting new provisions in their bilateral investment treaties and trade agreements.

The topic of green transition also influences global governance since countries are now in the process of introducing new rules to deal with climate change and to

otherwise facilitate this transition. Policymakers will need to consider the current developments at the level of the European Union Carbon Border Adjustment Mechanism (CBAM) as well as the introduction of tax incentives by countries meant to facilitate the green transition.

The topic of taxation of the digital economy has resulted in countries introducing domestic rules (e.g., Digital Service Taxes) and participating in international initiatives such as the taxation of highly digitalized business (Pillar One). The introduction of Digital Service Taxes has trade implications that will need to be considered by policymakers.

To address all these topics, new governance structures have been proposed, for instance centering the African Union as a united front on the taxation of the digital economy. Another proposal is to elevate the United Nations as the international organization legitimized to serve the needs of developing countries and to provide an inclusive and effective participation in agenda-setting and decision-making process.

By calling to strengthen the role of the United Nations and the African Union as the institutions that can contribute to enhance governance in developing countries, this part addresses a change of paradigm in international tax law-making which, as we saw in prior Parts of the book, has been dominated by the OECD and the G20 when dealing with international tax initiatives to tackle base erosion profit shifting, to facilitate exchanges of information, to tax highly digitalized business, and to introduce a global minimum tax.

This is also the result of regional and international developments that questioned the role of the OECD and advocated for strengthening regional cooperation as well as giving a more important role to the United Nations in international tax law-making. At the regional level, two examples are the creation in 2020 of a Special Technical Committee within the African Union under the theme "Securing Africa's Taxing Rights, Stemming Illicit Financial Flows and developing payment system for AfCFTA" and the introduction in July 2023 of a Regional Tax Cooperation Platform for Latin American and the Caribbean (CEPAL).

At international level, one example is the adoption by the UN in November 2022 of a resolution to develop a globally inclusive new tax framework. This resolution was followed in November 2023 by another UN Resolution to develop an International Tax Framework Convention under the auspices of the UN. This Resolution was initiated by the African Group and supported by a majority of developing countries. As a result, an ad hoc intergovernmental committee has been mandated to develop the terms of reference for the development of such convention with finalization expected by mid-2024.

All these developments show that global governance is being reformed, and that these reforms need to take a holistic approach to deal with tax, trade, and investment, to take into account the differences between developed and developing countries. The chapters in this Part contribute to provide solutions to policymakers at international, regional, and country level to address these new changes.

Chapter "Optimizing Policy Synergies: The Role of Tax Incentives in International Trade and Investment" by Julien Chaisse addresses tax incentives and their impact

on trade and investment. In this chapter, the author provides an analysis of the topic of tax incentives within the current international framework governed by Bilateral Investment Treaties and World Trade Organization Agreements. The aim is to provide insights into designing tax incentives regimes that strike a balance between promoting investments, safeguarding trade interests, and ensuring equitable outcomes. This author concludes with some recommendations when introducing changes to tax incentives in order to take into account the interplay among international legal frameworks, national policy objectives, and strategic choices in economic development paths.

Chapter "Tax, Trade and Investment for Green Transition" by Suranjali Tandon addresses the need to balance the introduction of tax incentives and the implementation of carbon pricing in order to encourage green transition. For this purpose, the author provides an analysis of two instruments, the EU's CBAM and the Inflation Reduction Act (IRA). The chapter starts with analyzing whether the Paris Agreement is binding, and thereafter, the main features of design of the CBAM as adopted in the EU Emission Trading System Directive. In addition, this chapter addresses the introduction of tax incentives to encourage green sectors and its compatibility with Pillar 2. By analyzing the topic of tax incentives, this contribution provides a critical reflection to the policy choices when introducing tax incentives to encourage green transition, including also the introduction in the United States of the Inflation Reduction Act and its consequences for developing and developed countries. This chapter concludes with a warning to countries to be careful in their policy design to ensure that the shift to renewables is not at the costs of economic growth, and to keep in mind when introducing measures that developing countries need to receive their fair share of climate finance due to the changes in the industrial policy.

Chapter "Breaking the Cycle of Domination in Global Tax Governance: Africans Defying Asymmetries and Seizing Opportunities" by Lyla Latif addresses the current changes in international tax law-making by discussing the role of the United Nations and the long-standing historical inequalities and asymmetries (technical, capacity, and resource) faced by African nations. This chapter addresses the new role of African Nations that challenge these inequalities by proactively participating in global tax discussions as it has been seen in the adoption of the UN Resolution to develop a global inclusive new tax framework. This chapter addresses some of the international tax challenges faced by African countries but also applicable to developing countries in general such as the current rules for reallocation of taxing rights, the arm's length principle, the automatic exchange of information, the proposed rules for digital taxation, and the rules introducing a global minimum tax. In addition, this chapter addresses the demanding need of developing countries to increase administrative capacity and resources to implement these rules. Finally, this chapter concludes with an analysis of the three options provided in July 2023 in the "Promotion of inclusive and effective international tax cooperation at the United Nations" Report addressed to the UN Secretary General before adopting the UN Framework Convention option.

Chapter "Decision-Making in a Proposed African Union Tax Governance Structure" by Afton Titus argues for the creation of an African Structure within the

African Union to address the international tax challenges and to coordinate the implementation of policies to deal with these challenges. The focus is on the taxation of the digital economy as an illustrative example on how regional tax organizations such as the African Tax Administration Forum, Regional Economic Agreements such as the East African Community and the Southern African Development Community can contribute to build continental coherence to improve the participation of African countries in the international tax system, and to build a common continental position in Africa. The author also highlights the recent creation of the African Continental Free Trade Area Agreement AfCFTA which can facilitate greater integration in Africa without erasing the good work that regional economic agreements have made across the continent.

Competition and Complementarity of EU and FATF Beneficial Ownership Transparency Orders

Leyla Ates, Andres Knobel, Florencia Lorenzo, and Markus Meinzer

1 Introduction

In the last 10 years, a broad range of transnational organizations and networks have placed beneficial ownership transparency high on their policy agendas. The beneficial owner is the natural person(s) who ultimately own or control a legal person (such as companies, foundations, and partnerships) or a legal arrangement (such as a trust, fideicomiso, fiducie, Treuhand, and Waqf) (Financial Action Task Force [FATF] 2023a). The opacity of beneficial ownership facilitates a broad range of illicit financial flows, including cross-border money laundering, corruption, tax evasion, and abuse of the international trade system. In the past decade, numerous scandals have illustrated the magnitude and systemic and global nature of the issue (International Consortium of Investigative Journalists [ICIJ] 2016, 2017, ICIJ 2021; Organized Crime and Corruption Reporting Project & Suddeutsche Zeitung 2022). Diverse actors at different levels in the global governance of finance have analyzed an extensive body of case studies, demonstrating how legal vehicles (legal persons

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or arrangements) are exploited to conceal beneficial ownership information for illicit purposes. While most of these studies have focused on the use of the financial system and the physical movement of money (FATF 2006a; FATF and Caribbean 2010; van der Does de Willibois et al. 2011; FATF and Egmont Group 2018), some have given considerable attention to the use of the physical movement of goods through the trade system (FATF 2006b; Asian/Pacific Group on Money laundering [APG] 2012; FATF and Egmont Group 2020).

The FATF and the European Union (EU) are salient actors that seek to create order in the absence of a beneficial ownership transparency issue. Within the anti-money laundering and terrorist financing laws and regulations, the FATF produces beneficial ownership transparency norms in its Recommendations (soft law instrument), whereas the EU enacts Anti-Money Laundering Directives (hard law instrument) and directs them toward nation-states to enact and enforce within its borders. By using law to address a problem that transcends nation-state boundaries, the FATF and EU build transnational legal orders (Halliday and Shaffer 2015). The FATF's and EU's beneficial ownership transparency transnational legal orders overlap in geographic and legal scope. With respect to the geographic scope, the FATF seeks to create a global transnational legal order. It is an inter-governmental institution with 36 current member countries, including many EU Member States, and two regional member organizations one of which is the European Commission. In addition, the FATF created associated satellite bodies in its image, each with a regionally confined scope that jointly spans the planet ("FATF-style regional bodies"). Despite some negative consequences stemming from the standards or their inappropriate implementation, such as de-risking, financial exclusion, or violations of the freedom of association and the right to due procedure (Ramachandran et al. 2018; Chakrabarty 2023; Pavlidis 2023), over 200 jurisdictions have committed to implementing the FATF standards, and all 27 EU Member States are among these jurisdictions (FATF 2023b). Thus, the geographic scope of EU legal norms and the resulting transnational legal order fully overlap with the geographic scope of FATF legal norms and transnational order.

Considering this geographic overlap, the question addressed in this chapter is the nature of the relationship between the two. Does the EU's beneficial ownership legal order complement or compete with the FATF's legal order? We argue that the EU not only complements the FATF, but also competes with it in building the transnational legal ordering of beneficial ownership transparency.

While the legal scope of both norms overlaps to a significant extent, they differ in relevant aspects, and the divergence between them has been growing recently. In 2015, the EU required member states to establish central beneficial ownership registries for companies and for some trusts in the 4th Anti-Money Laundering Directive (AMLD 4) (EU 2015). In 2018, the EU obliged member states to enable public access to the beneficial ownership registries of companies in the 5th Anti-Money Laundering Directive (AMLD 5) (EU 2018). Legally, both measures are

more ambitious than the FATF's beneficial ownership transparency standard. Considering the overlap in geographic scope, such divergence signals competition between two transnational legal orders. Borrowing from Halliday and Shaffer, they are in "contention for normative primacy" (Halliday and Shaffer 2015). Moreover, the EU has taken steps to increase the influence of its beneficial ownership legal order beyond the EU borders to gain an advantage in its competition with the FATF. In 2017, the EU launched a global facility to support third countries, mostly least developed and developing economies, in fixing the deficiencies in their anti-money laundering and terrorist financing regimes (EU Global Facility on Anti-Money Laundering and Countering the Financing of Terrorism [EU Global Facility] 2024a). The first area of technical assistance given is transparency of beneficial ownership for legal persons and legal arrangements (EU Global Facility 2024b). Therefore, the EU has mechanisms in place which disseminate and extend the reach of its normative power beyond its member states.

This contestation presents a challenge to the conventional view of the relationship between the FATF Recommendations and EU Anti-Money Laundering Directives. The relationship between the development of the anti-money laundering norms in the FATF and the evolution of such norms in the EU has been seen as a largely uncontested and intertwined process, even a "symbiotic relationship" (Mitsilegas and Gilmore 2007; Mitsilegas 2007; Borlini and Montanaro 2017; Borlini 2017). However, the EU's evolution from a complementary role in global governance to a potentially competing role has also been anticipated by some scholars: "with the increased institutionalization and harmonization of European regulation at the EU level, the EU may […] play an increasingly important entrepreneurial role in global governance" (Shaffer and Pollack 2010).

Notwithstanding, the EU's standard-setter role in beneficial ownership follows a non-linear trajectory. On November 22, 2022, the European Court of Justice suspended the provision of AMLD 5, which enables the general public to access information on beneficial ownership (Court of Justice of the EU 2022), even though nine out of 27 member states have kept the registries publicly accessible as of June 28, 2023 (Lorenzo 2023). Such development underlined that the recursive interaction of institutions and bodies that create the EU's legal order may play an important role in challenging the EU's success in its standard-setting role from within.

The remainder of this chapter proceeds as follows. Section 2 analyzes the emergence of beneficial ownership transparency norms at the transnational level. Section 3 examines how the EU took the lead by introducing beneficial ownership registries in AMLD 4. Section 4 analyzes the introduction of public beneficial ownership registries in AMLD 5 and the dynamic interplay between the EU decision-making institutions and the European Court of Justice for legal ordering. Section 5 concludes.

2 The Rise of Beneficial Ownership Transparency Transnational Norms

The EU recognized the importance of beneficial ownership transparency as early as 1997. In its Recommendation[1] 8 of the Action Plan to Combat Organized Crime, the EU called on Member States to collect information with respect to the physical persons involved in the creation, direction, and funding of legal persons registered in their territory (European Communities 1997). However, with the 2003 version of its Recommendations (FATF 2023c), the FATF became the first international standard-setter for beneficial ownership transparency. Recommendation 33 is devoted to legal persons, whereas recommendation 34 is rated to legal arrangements. According to Recommendation 33, "(c)ountries should ensure that there is adequate, accurate and timely information on the beneficial ownership and control of legal persons that can be obtained or accessed in a timely fashion by competent authorities" (FATF 2003). In a similar vein, Recommendation 34 stated that "countries should ensure that there is adequate, accurate and timely information on express trusts, including information on the settlor, trustee, and beneficiaries, that can be obtained or accessed in a timely fashion by competent authorities."

The EU implemented the standard at the EU member state level through the 3rd Anti-Money Laundering Directive (AMLD 3) (EU 2005). The Preamble of the Directive clearly stated that EU legislation aimed to complement the FATF order:

> The Community action should continue to take particular account of the Recommendations of the Financial Action Task Force (hereinafter referred to as the FATF), which constitutes the foremost international body active in the fight against money laundering and terrorist financing. Since the FATF Recommendations were substantially revised and expanded in 2003, this Directive should be in line with that new international standard.

The FATF substantially revised its Recommendations in February 2012 and reaffirmed the beneficial ownership transparency standard for legal vehicles (FATF 2012). In the revised document, Recommendations 33 and 34 were renumbered as Recommendations 24 and 25, respectively. Moreover, new interpretative notes accompanied both Recommendations 24 and 25 that, according to the FATF, "should be read in conjunction with the Recommendation(s)" (FATF 2012). These Interpretative Notes explicitly stated mechanisms to ensure the access of anti-money laundering competent authorities to beneficial ownership information. The first one was the "registry approach," which requires a central registry to obtain, verify, and retain information on a legal vehicle's beneficial ownership. The second one was the "existing information approach" that leans on intermediaries (e.g., financial institutions or corporate service providers) or other public authorities (e.g., tax authorities) holding information on the beneficial ownership of legal vehicles. The third mechanism was the "company approach" which relies on companies to obtain, verify, and retain their beneficial owners. The equivalent of this measure for legal

[1] EU recommendations are a form of EU acts that do not have legal consequences but offer guidance (EU 2023a).

arrangements, especially for trusts, relies on the trustee to hold beneficial ownership information. When one of these mechanisms was in place, the FATF assumed that the beneficial ownership information would be available to anti-money laundering competent authorities and the standard was thus considered to be complied with.

As a matter of fact, the FATF has required countries to ensure their financial institutions collect beneficial ownership information from their customers since the 1996 version of Recommendations and from corporate service providers since the 2003 version of Recommendations under the due diligence procedure. When a country ensures component authorities' access to beneficial ownership information collected by financial institutions and intermediaries, it correspondingly fulfills the existing information approach. Thus, it was not surprising that countries mostly used the existing information approach to comply with the beneficial ownership standard (Knobel 2020). Nevertheless, international institutions acknowledged the inadequacy of relying on the due diligence procedure alone to avail competent authorities access to beneficial ownership information in the early 2000s (OECD 2001).

Immediately after the 2012 FATF revision, the EU reviewed the implementation of AMLD 3 as a first step to align with the new recommendations (European Commission 2012). Subsequently, it took several rounds of planning and delays until revisions to AMLD 3 were adopted (Van den Broek 2015). At the end of the recursive cycles, the EU reached a settlement that went beyond the FATF regarding several elements, particularly beneficial ownership transparency.

3 The EU Taking the Lead in Beneficial Ownership Registries: AMLD 4

The ordinary legislative procedure of a directive starts with a legislative proposal from the executive arm of the EU, that is, the Commission, and normally continues with the readings of the Parliament and the Council as co-legislators (European Parliament 2023). After the aforementioned 2012 review, the Commission published a proposal together with an impact assessment report in February 2013 (European Commission 2013a, b). The proposal included the beneficial ownership transparency standard for legal entities in Article 29 and trusts in Article 30. In these provisions, the Commission took a clear stance on which mechanism Member States should employ to ensure the component authorities' access to information. Based on the impact assessment, the Commission preferred to require companies or trustees to hold information about their beneficial owners. However, the European Parliament and civil society were not of the same opinion (European Commission 2013b).

The European Parliament discussed the proposal and adopted the first reading on 11 March 2014 with a hundred-and-fifty amendments (European Parliament 2014). One of the amendments was to merge articles 29 and 30 and create a single article

for beneficial ownership transparency requirements both for legal persons and arrangements. The new combined article prescribed the central registry approach for legal entities and trusts especially to be filed with a government authority. Moreover, Parliament envisioned a public registry that is "available online to all persons in an open and secure data format" (European Parliament 2014). In parallel, the Council examined the proposal on several occasions. During subsequent inter-institutional negotiations between the Parliament, Council, and Commission, called the trialogue, an agreement was reached. The parties came to a provisional agreement on 16 December 2014. Following the Council and Parliament's approval of the provisional agreement, some legal and linguistic modifications were made (Council of the EU 2015; European Parliament 2015). Finally, the Directive was published on 5 June 2015.

AMLD 4 struck a compromise. The provisions on the beneficial ownership standard deviated substantially from the commission's proposal. The central registry requirement met the Parliament's demand. However, the Directive required registration for legal persons incorporated in the EU and for trust only when they had tax consequences. Moreover, with the efforts of some Member States led by the Council's powerful member Germany toward some secrecy for beneficial owners, the directive introduced a legitimate interest test that required the public to prove a legitimate interest before accessing the registry information (Borlini 2017).

AMLD 4 initiated the first wave of beneficial ownership registration laws in the world that require beneficial ownership information to be filed by government authorities (Knobel 2020). In 2018, there were 34 countries including the 28[2] EU Member States that had passed these laws. The number increased to 80 countries in 2020 and 97 countries in 2022 (Tax Justice Network 2022) (also see Fig. 1 below). The growth of public beneficial ownership registries beyond the EU in this period of time, despite the FATF not yet having taken onboard this standard, underlines the EU's growing influence and thus its role as a global standard-setter. Eventually, the FATF standard followed suit in March 2022 but only for legal persons. The revised Recommendations 24 requires the establishment of beneficial ownership registries (registry approach) or alternative mechanisms that are equally efficient (FATF 2022).

Shortly after, the EU advanced further in its global standard-setter role in beneficial ownership transparency by introducing an amendment to AMLD 4.

4 Public Beneficial Ownership Information: AMLD 5 and the Resistance of the EU Court of Justice

The EU experienced consecutive terrorist attacks first in Paris on 13 November 2015 and then in Brussels on 22 March 2016. Terrorists did not use legal entities to transfer their terrorist funds during either incident (Open Ownership 2021).

[2] Since the UK formally left the EU on 31 January 2020, the number of EU countries had been 28.

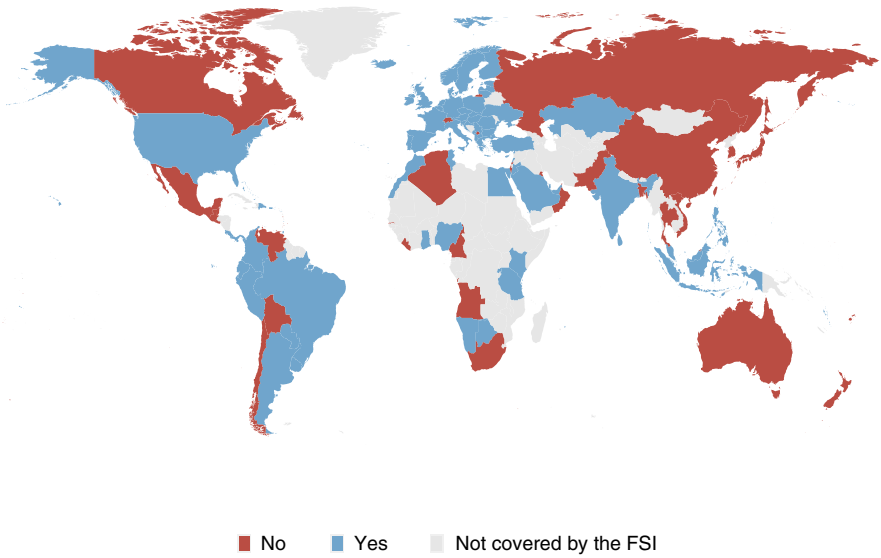

Fig. 1 Map of jurisdictions with beneficial ownership registration laws (Knobel and Lorenzo 2022)

However, considering the possibility of using legal vehicles for the financing of terrorism, the EU highlighted the need to take measures to ensure increased beneficial ownership transparency for legal persons as well as legal arrangements (EU 2018). Moreover, the Panama Papers leak in 2016 and the Paradise Papers leak in 2017 revealed the extent to which people use legal vehicles in offshore jurisdictions to conceal beneficial ownership information for illicit purposes (ICIJ 2016, 2017). These incidents helped galvanize support in the EU's institutions to reform beneficial ownership transparency by requiring central registries with public access.

The Commission proposed a set of amendments to AMLD 4 on July 5, 2016 (European Commission 2016). At a trialogue meeting, EU decision-making institutions reached a provisional agreement on December 13, 2017. The Parliament and Council approved the draft without modifications (European Parliament 2018; Council of the EU 2018). Finally, AMLD 5 was published on June 19, 2018.

AMLD 5 required beneficial ownership information on companies and other legal entities to become publicly accessible. Access to beneficial ownership registries on trusts would still be subject to legitimate testing. Nevertheless, the proposal extended beneficial ownership registration to all trusts administered in an EU country (regardless of tax consequences) and broadened the scope to cover trusts administered outside the EU that acquired real estate or established business relationships (Knobel 2020).

AMLD 5 started a new wave of beneficial ownership transparency (Knobel 2020). As of March 2022, 39 countries consisting of 27 EU Member States introduced public access to information on the beneficial ownership of legal persons held in central registries (Tax Justice Network 2022) (also see Fig. 2 below). However,

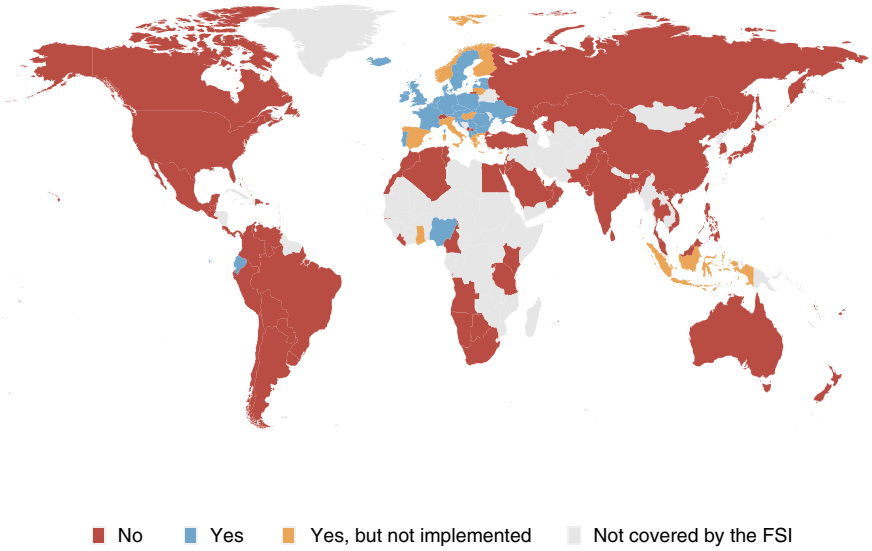

Fig. 2 Map of jurisdictions with public beneficial ownership registration laws (Knobel and Lorenzo 2022)

on November 22, 2022, the European Court invalidated the public accessibility requirement for central beneficial ownership registries. Subsequently, the number of jurisdictions with public beneficial ownership registries started to decrease in the EU.

Cases come before the European Court of Justice in different ways. One of the common types is the preliminary rule. To prevent different interpretations of EU law by national courts, the Court gives rulings to a demanding court that doubts the interpretation or validity of EU law (EU 2023b). The Luxembourg District Court asked the European Court of Justice if the provision requiring public access to beneficial ownership information in AMLD 5 is valid, taking into account fundamental rights. The Court found public access to beneficial ownership registries for AML purposes disproportionate as a result of interfering with the right to respect for private life and to the protection of personal data enshrined in Articles 7 and 8 of the Charter of Fundamental Rights of the European Union.

In fact, the European Court of Justice has dealt with the tension between anti-money laundering and terrorist financing measures and fundamental rights in several cases and has used the proportionality test by balancing money laundering and terrorist financing prevention and the protection of such rights (Borlini 2017; Borlini and Montanaro 2017). Thus, it is not surprising to see that the EU decision-making institutions gave several references to the proportionality through the process of AMLD 5 from the Commission proposal to the recital of the directive for declaring their commitment to the principle (EU Commission 2016; EU 2018). However, they could not escape from the jurisdiction of the European Court of Justice. This decision had an immediate effect on the EU legal framework. The access regime to

beneficial ownership registries in the anti-money laundering system returned to the system before the 2018 amendment (EU 2023c). As a result, the court contested the EU's beneficial ownership transparency standard-setter role. Nonetheless, as of June 28, 2023, Estonia, Slovakia, France, Denmark, Bulgaria, Czechia, Slovenia, Latvia, and Poland have kept registries publicly accessible despite court ruling (Lorenzo 2023).

5 Conclusion

The legal order of responses to the lack of beneficial ownership information went beyond domestic norms to transnational norms. The FATF and the EU are two prominent actors in this regard. Initially, the EU complemented the FATF only when it set its first international beneficial ownership standard in 2003. However, more recently, the EU has begun to differentiate its legal scope. First, the EU introduced the beneficial ownership registry requirement in AMLD 4 in 2015, which obliges Member States to establish central databases of beneficial ownership information held by any government authority. In 2018, the EU continued to require general public access to such registries in AMLD 5. Both measures were ahead of the FATF's beneficial ownership transparency standard in terms of the ambition to go beyond the status quo. Considering the overlap in geographic scope, such divergence means competition between the two transnational legal orders. This conclusion presents a challenge to the conventional view of the interdependent relationship between the FATF Recommendations and EU Anti-Money Laundering Directives. Instead, the EU and FATF's competition for transnational norm-making can spur the development of beneficial ownership transparency norms (see Halliday and Shaffer 2015). However, in 2022, the European Court of Justice resisted the EU's standard-setter role by invalidating the general public access requirement for AML purposes introduced by AMLD 5. From another point of view (Alter 2001), Luxembourg's domestic court inserted itself into the transnational legal ordering process and challenged ALMD 5 through the European Court of Justice. This shows that the EU must be aware of the recursive interaction between transnational and national judicial forums to develop a beneficial ownership transparency order that may interfere with the normative settlement. Otherwise, the EU falters its global standard-setter role.

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Dealing with Treaty Shopping Across the Tax, Trade, and Investment Regimes

Frederik Heitmüller

1 Introduction

Treaty shopping is a strategy whereby companies or individuals restructure a cross-border transaction through a third jurisdiction in order to gain advantage of a more favourable bilateral treaty signed by this third jurisdiction. The phenomenon has received a lot of attention in the tax area, yet there is no agreement on how to address this problem satisfactorily. Hence, it is interesting to investigate how other economic regimes have approached the problem and whether there is potential for transferring policy ideas.

In theory, the issue can arise in any bilateralized international regime. A "bilateralized" regime is an international regime in which countries apply different treatments to different countries, for example because treaties with differing content are negotiated with individual (or groups of) countries or domestic law prescribes differentiated treatment to different geographical areas (Ruggie 1992).

There is increasing attention on treaty shopping in the international investment regime, which, like the international tax regime, is fundamentally built on bilateral treaties. Therefore, this presents an obvious area for comparison. Trade has historically been governed in a more multilateral way due to the most-favoured nation principle embedded in the General Agreement on Tariffs and Trade (GATT), which strives to equalize the treatment that a country applies to different countries. However, bilateralism or preferential treatment among regional groupings has become a prominent feature of the trade regime (Inama 2022). Moreover, as I will show below, there are other features of the trade regime that incentivize treaty shopping practices.

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The similarity of the issues in different policy areas has been noted by different authors. In the investment regime, the term "treaty shopping" appears to have been imported from the tax regime (Baumgartner 2016). In a 2001 article, Avi-Yonah and Slemrod drew a parallel between the anti-treaty shopping rules of tax treaties and the rules of origin of trade agreements (Slemrod and Avi-Yonah 2001, 544). However, a more systematic comparison of policy approaches to treaty shopping has not yet been undertaken.

Governments face several choices when adopting rules to tackle this issue. First, there is always a grey area between genuine situations and illegal behaviour. Governments need to calibrate their anti-treaty shopping rules to achieve an adequate equilibrium. They also face several choices in what kind of rules are used with different implications for effectiveness, compliance burden, and administrability. For instance, rules can be vague, allowing for case-by-case decisions, or mechanical. They can be uniform or differentiated across sectors, types of transactions, or economic actors. They can require routine compliance, or they can enable application in cases of suspected treaty shopping only.

At a global level, there are two relevant issues. First, international harmonization of approaches to treaty shopping is desirable to increase the predictability of rules for genuine economic actors operating across different countries. Second, by fostering multilateralism, international institutions can prevent the problem "at its root", since greater harmonization of fundamental policies means that there are fewer incentives for economic actors to devise treaty shopping strategies in the first place.

In Sect. 2, I describe how the phenomenon of treaty shopping appears in different regimes, what its motivations are, and how prevalent it is. In Sect. 3, I analyse the responses developed in each of the three regimes based on the features described above. In Sect. 4, I discuss which insights can be derived from comparing the three regimes and highlight some interactions of the responses adopted.

2 How Treaty Shopping Works in Each Regime and How Prevalent It Is

In the following sub-sections, I will describe the phenomenon of treaty shopping in each of the three regimes, among them what is "shopped" for, what features of countries' domestic laws or treaties enable treaty shopping, and how prevalent the phenomenon is thought to be. I show that the issue is prevalent in the tax and investment areas, but less so in the trade area. The main difference between the tax and investment areas is how frequent benefits occur as well as the likelihood of being investigated by relevant authorities.

2.1 Tax

In the field of tax, treaty shopping can be defined as a practice whereby a taxpayer routes an international payment through a conduit subsidiary resident in a state C, other than the state B from which the payment originates and the state A of the final recipient of the payment, to benefit from a (more advantageous) tax treaty. "More favourable" in the context of tax usually means that the treaty foresees lower withholding tax rates on different income flows (such as interest, royalty, dividends, technical services) to be levied by the source country or an exclusive allocation of taxing rights on capital gains to the residence state.[1] In addition, the domestic law of conduit jurisdictions is also relevant to this structure. For example, the tax system of the conduit jurisdiction should provide for an exemption from foreign-earned dividends and capital gains and not apply withholding taxes on outbound flows.

One should also mention that the identity of countries "A" and "B" in Fig. 1 could be the same. In that case, one would speak of "round-tripping".

In tax, the evidence of treaty shopping is well established. Even though there is no water-tight methodology to quantify revenue losses, estimates range among several billions (Lejour et al. 2021). This is further confirmed by the important role adopted by jurisdictions with favourable attributes for treaty shopping in global foreign direct investment flows and the number of special-purpose entities registered in these jurisdictions.

However, whether treaty shopping is likely to occur strongly depends on a country's treaty network and its domestic law. For example, if a country only imposes

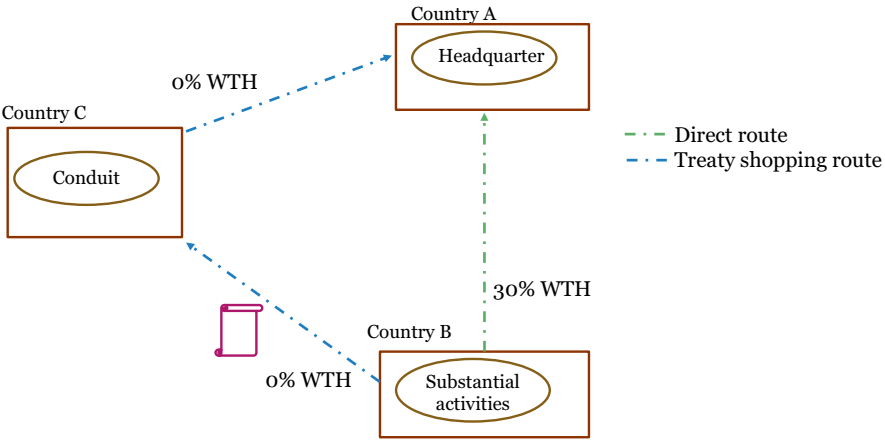

Fig. 1 Treaty shopping scheme in tax. Source: the author

[1] Treaty shopping could be undertaken with the purpose of obtaining favourable treatment in the home state, for example the benefit of an exemption of foreign income, where otherwise only deduction or credit would be granted. But this should not occur often since most main residence countries have similar tax rules applicable to income earned abroad.

low withholding rates on outbound payments or if it has signed similarly worded treaties with all relevant trade partners, treaty shopping is unlikely to be of any advantage for taxpayers. Accordingly, there is considerable variation with respect to individual countries' exposure to the phenomenon (Lejour and van't Riet 2023).

2.2 *Investment*

In the investment regime, the main benefit of treaties is their dispute resolution provision, which typically allows an investor to initiate an investor-state arbitration proceeding (see Fig. 2). Because treaties' substantive provisions mainly restate what is generally accepted as customary international law and thus also applicable in the absence of a treaty, treaty shopping is mainly attractive to investors because of the dispute resolution provisions contained in BITs (Baumgartner 2016, 2; Gray 2019); thus, shopping should mainly occur from countries without any treaty to countries with a treaty. However, there is some variation in the degree of benefit offered by treaties, for example the existence of "umbrella" or tax carve-out provisions, which determine what kind of topics can be submitted to a dispute (see also the chapters by Garcia Cordoba and Garcia Olmedo in this volume). This variation could incentivize treaty shopping by investors from countries that even have a treaty in place (Skinner et al. 2010, 267).

Nevertheless, a difference from the tax regime is that benefits from investment treaty shopping tend to be more "one-off" for an investor (when a dispute occurs), whereas benefits from tax treaties occur repeatedly (at any time that there are taxable transactions affected by a treaty). The number of jurisdictions that can facilitate

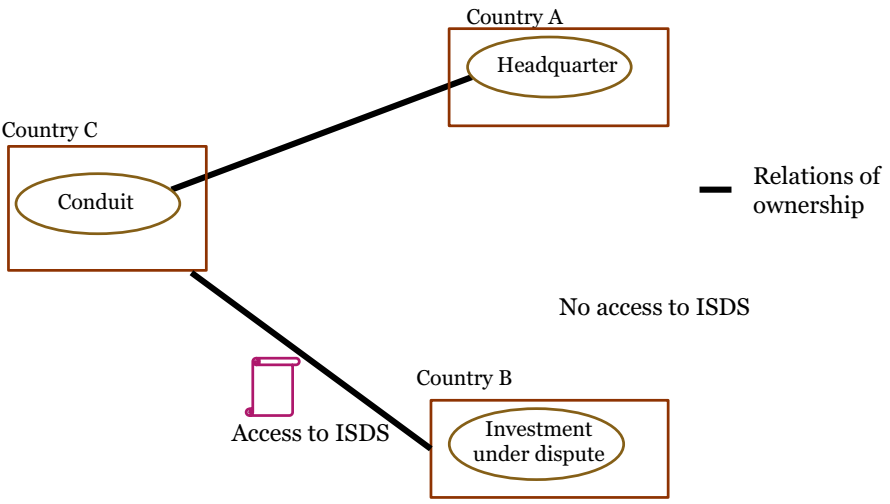

Fig. 2 Treaty shopping in investment. Source: the author

investment treaty shopping is potentially greater than in the tax case, as well, since the domestic law of the jurisdiction used for treaty shopping is not immediately relevant—only the fact that a BIT exists.[2] Nevertheless, some jurisdictions appear to be used more often than others. For instance, the Netherlands is often cited as jurisdiction that can be used by investors for setting up shell companies because it has signed many BITs with comparatively favourable wording (Gray 2019), and possibly because it can simultaneously procure tax treaty shopping benefits (Gray 2019; Thrall 2021).

Although there are no concrete figures, the practice is regarded as prevalent, which is illustrated by the number of arbitration cases in which the Netherlands is involved (despite the comparatively small size of its economy) and the number of arbitration cases in which the matter of nationality is discussed (Chaisse 2015; Böhme 2021).

2.3 Trade

In the trade regime, it is useful to distinguish between trade in goods and trade in services since regulation of both issues fundamentally differs.

Trade in Goods

While in the tax and the investment regimes the true "residence" or "nationality" of an investor or taxpayer is the crucial question, in the regime on trade in goods, the true origin of a product is relevant. A parallel can be drawn between the shell company (or conduit company) in tax and investment law with companies that simply "re-package" or do minimal assembly works on imported goods in the trade regime.

Under the multilateral General Agreement on Tariffs and Trade (GATT), which applies to trade in goods, treaty shopping is prima facie not an issue because of the most-favoured nation (MFN) principle. However, GATT allows countries to conclude preferential agreements. In such cases, treaty shopping concerns could arise because a company could first import into the country with the most beneficial tariffs, and then further to the ultimate destination. Note, however, that in a customs union such as the European Union, this issue does not arise because there is a tariff common to all member countries vis-à-vis third countries (Felbermayr et al. 2018).

Treaty shopping could also arise when a country (or a block of countries) implements different tariffs, such as those implemented by the European Union's Generalized Scheme of Preferences, which provides for lower tariffs for least developed countries, and which is allowed under the GATT.

[2] Even though the tax regime may be relevant a company may prefer to use a country with a low tax rate so that potential arbitral awards are taxed at a low rate, as tribunals most of the time do not accept to "gross-up" an arbitral award by the tax applicable in a home jurisdiction (Leikin and Keller 2020).

In addition, even under the GATT the imposition of anti-dumping and countervailing measures on products from a specific country could incentivize economic actors to alter the origin of their products to obtain a more favourable treatment. While the term "treaty" shopping may not be fully accurate in this case (since no different treaty applies), this type of "duty evasion" shares the same characteristics of the treaty shopping issue, namely a circumvention of a disadvantageous treatment based (among others) on geography (Bjorklund and Marcoux 2022).

Chaisse argues that "treaty shopping is relatively less serious in the field of trade (in goods)" than in investment because defensive measures (the rules of origin) have already been established for a long time (Chaisse 2015, 244). Felbermayr and colleagues show that tariff levels towards third countries are often similar among countries that have preferential agreements among each other, which makes treaty shopping unprofitable in many cases even if no rules of origin applied (Felbermayr et al. 2018). Hence, strategies such as the one shown in Fig. 3 are unlikely to be adopted in many cases by economic actors, especially when considering additional transportation costs stemming from routing goods through an intermediary jurisdiction.

Trade in Services

With respect to trade in services, countries usually do not apply tariffs; therefore, international agreements such as the General Agreement on Trade in Services (GATS) relate to other measures, such as market access regulations, and aim to ensure that foreign service providers are treated like comparable national providers. As in the area of trade in goods, the GATS allows countries to conclude preferential economic integration agreements, and many countries have done so. Therefore, determining the proper origin of a service can also be an issue.

Dinh notes that the issue has received significantly less attention from academics and policymakers, but nevertheless cites a few WTO cases in which the origin of a

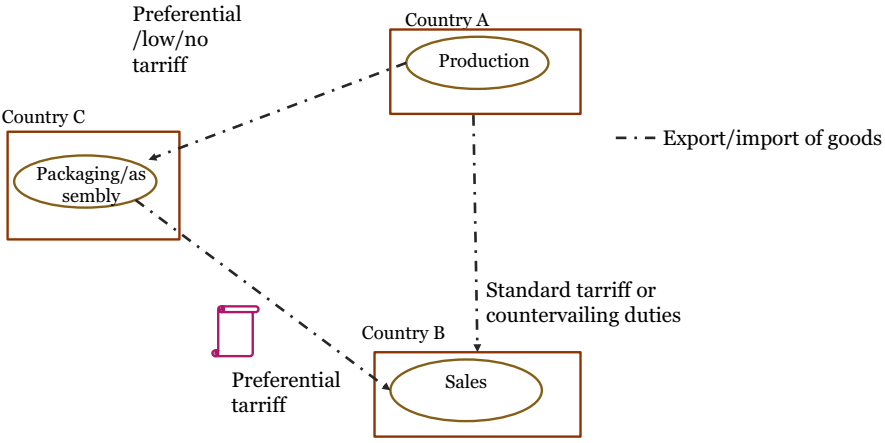

Fig. 3 Duty evasion in trade. Source: the author

service was subject to dispute (Dinh 2020). He further argues that as cross-border services are gaining importance as inputs in the production of goods, determining the origin of services becomes indirectly relevant for determining the origin of goods.

3 Responses Adopted in Each Regime

In all three regimes, governments responded to treaty shopping. Terminology varies across regimes. For example, one can find "principal purpose test provisions" and "limitation of benefits" provisions in tax treaties, "denial of benefit" provisions in investment treaties, and "rules of origin" in domestic trade laws as well as preferential trade agreements. Their purposes are generally similar. However, their approaches can vary. For example, one can distinguish between formulaic approaches (more prevalent in the trade regime) and case-by-case approaches that consider facts and circumstances (more prevalent in the tax and investment regime). One can also distinguish between rules that apply routinely and anti-avoidance approaches that apply only in cases of suspected treaty shopping. At the regime level, there is variation with respect to the extent of harmonization, both within and across countries.

3.1 Tax

The issue of tax treaty shopping has received increased attention from the 1970s onwards, coinciding with the expansion of international investment. The first device, already included in the 1977 OECD Model Convention, was a "beneficial ownership" provision added to the different articles concerning passive income, which can be used to deny benefits if a company does not have the formal right to dispose of the income received. However, these provisions used to be narrowly interpreted and were not judged as effective (OECD 1986).[3] However, in addition to beneficial ownership clauses, countries began relying on domestic anti-avoidance provisions and more stringent provisions included in treaties, or altogether terminated vulnerable treaties such as the United States-Netherlands Antilles, in the 1980s (Avi-Yonah and Panayi 2010). For instance, the OECD released a report in 1987, which described the phenomenon as well as four different responses adopted by countries (OECD 1987). Most relied on formal tests, such as the degree to which a foreign company that claimed treaty benefits was owned by shareholders in third states or the share of income received that was passed on to companies in third states. Until recently, most treaties had not included specific provisions.

[3] This has changed recently with the so-called Danish cases in which the European Court of Justice confirmed a wider interpretation of the concept (Bærentzen 2020).

The Base Erosion and Profit Shifting (BEPS) Project, launched by the OECD and G20 countries in 2013, has spurred harmonization by declaring the introduction of one of the two model anti-avoidance rules in countries' tax treaties as international minimum standards. The most prevalent approach is the one of a General Anti Avoidance Rule, the so-called principal purpose test (PPT), which allows to a state to deny a taxpayer the benefit of the treaty where availing oneself of the benefits of the treaty was one of the principal purposes of the transaction (OECD 2015). The alternative approach endorsed by the BEPS Project is a Limitation-on-benefits (LOB) rule, which is a simplified version of a clause developed by the United States. The LOB rule contains a series of tests based on the type of taxpayer and whether an active business is conducted in the state of the taxpayer's residence. While the LOB test is more formulaic, both PPT and LOB largely require a tax authority to do a case-by-case analysis in case they suspect a taxpayer of treaty shopping.

Through the BEPS Multilateral Instrument, a mechanism to update bilateral treaties, many treaties now contain the same PPT or LOB clause. However, there is no sufficient evidence yet to judge whether this initiative has brought any harmonization in practice (Jiménez 2022). Because applying the PPT rule can be challenging for tax administrations with limited capacity, some countries have undertaken renegotiations of substantial provisions. For example, in 2017, India simultaneously renegotiated the advantages it conferred in treaties with Mauritius, Singapore, and Cyprus, as these treaties had been used by many investors (Bose 2017; Kotha 2017). When they perceive high revenue losses from treaty shopping, other countries have even terminated treaties.[4] However, while these approaches may effectively combat treaty shopping in a low-capacity context, they are politically difficult to enact, since terminating or renegotiating a treaty involves a diplomatic procedure with many potential veto players (Hearson 2021).

3.2 Investment

In the investment regime, treaty shopping has been addressed through anti-abuse doctrines, through definitions of the concept of "investor" or of the concept of the "home state" of the investor, or through specific denial of benefit clauses.

The Model bilateral investment agreement developed by the International Institute for Sustainable Development (IISD), which has significantly influenced recently negotiated BITs (Alschner et al. 2022, 602), contains a clause according to which benefits of the agreement can be denied if the investing enterprise does not meet a "substantial business activities" test in the contracting jurisdictions or if the investing enterprise has activities but is owned by a resident with which the recipient has no diplomatic relations or with respect to which it has specific regulations prohibiting exchanges (Mann et al. 2006, 12). In addition, the definition of the

[4] The termination of the Senegal–Mauritius treaty in 2019 is a notable example.

"home state" in the agreement seeks to exclude shell companies, by stating that an investor's home state is the "principal place of business or a major centre of effective and sustained links with the home state economy and from where effective control over the investment is exercised" (Mann et al. 2006, 5). However, a substantial activity test alone may be less effective in the investment regime than in tax and trade because the treaty shopping benefit is large and concentrated in time; hence, it is profitable for an MNE to start substantial activities in an otherwise empty conduit company when there is a prospect for an investment dispute (Böhme 2021, 516). Therefore, some states include additional purpose-based limitation of benefits clauses in the dispute resolution clause of BITs. The Dutch Model BIT, for example, denies access to investor-state arbitration "if an investor within the meaning of Article 1(b) of this Agreement […] has changed its corporate structure with a main purpose to gain the protection of this Agreement at a point in time where a dispute had arisen or was foreseeable".

As pointed out by several authors, the timing at which planning occurs is often an important factor in arbitral decisions dividing different forms of treaty shopping into acceptable and unacceptable behaviour (Baumgartner 2016, 10; Böhme 2021). In many cases, benefits were denied only if a company structure was changed when an investment dispute was already in prospect, but not if the investment had already been structured through an intermediary company beforehand. In contrast, the moment in time at which a structure is established is usually not part of the consideration in tax matters.

There are debates around the modalities of applying the respective clauses. In some cases, for example, arbitral tribunals judged that a government had to notify an investor beforehand when an investment was made if it intended to apply a denial of benefits clause (Böhme 2021; Azaino 2012).

Termination owing to treaty shopping is rare. Azaino cites the case of the Venezuela–Netherlands treaty, where Venezuela had mentioned treaty shopping as reason for the termination (Azaino 2012, 13). However, this is an exception. In sum, the standard response to treaty shopping in the investment regime appears to be comparatively weaker than that in the tax regime. Nevertheless, Böhme shows how state practice has evolved towards the inclusion of stricter limitation of benefits clauses in newer treaties. However, she concludes that they cannot combat treaty shopping effectively, since it is sufficient that a country has only one treaty without effective clause to be exposed to treaty shopping (Böhme 2021, 529).

3.3 Trade

Rules of origin are the main response to the treaty shopping problem in the trade in goods regime. These rules determine when a good originates from a specific country. Their purpose is not only to prevent treaty shopping but also to compile correct trade statistics (Inama 2022).

When it was concluded in 1947, the General Agreement on Tariffs and Trade (GATT) did not include any rules or guidance on rules of origin. Instead, countries have developed differing approaches in domestic law (Inama 2022). The common basis of most countries' approaches is that a good needs to have undergone "substantial transformation" in the last country of export to be considered as originating from that country. This test has been objectified by different types of formulaic tests such as an "ad valorem percentage criterion", "change in tariff heading" (which would indicate the transformation of a good) or a specified list of manufacturing operations that would qualify for a substantial transformation.[5] For the same type of test, countries can then differ in the strictness. For example, country X requires that 50% of value is added in country Y in order to consider the good as originating from country Y, whereas country Z only requires 30% of value added.

Different countries apply different rules of origin, and often have different rules depending on the type of good. One country may also agree to "preferential" rules in a free trade agreement distinct from "non-preferential" rules applying to other countries. For example, the EU accepts "aluminous cement" as originating from Indonesia based on either the "change in tariff heading" test or a 30% of value-added test. However, imports of the same good from Algeria can qualify for a preferential tariff under the Algeria-EU Free trade agreement, but in that case, only the change in tariff heading is accepted as a criterion.[6]

International harmonization efforts have been started in the 1990s with the drafting of the Agreement on Rules of Origin, which, however, has not been ratified as of 2023, which is why in 2022 Inama still describes them as "no man's land in international trade law" (Inama 2022, xxxv).

In addition to rules of origin, more generally worded anti-abuse rules may apply to protect rules of origin from circumvention (Bjorklund and Marcoux 2022, 228). For example, a company can circumvent a substantial transformation test based on value added by artificially lowering the prices of intermediary goods imported into the country of assembly, which then leads to higher value added in the latter country (Jha 2010). The North American Free Trade Agreement therefore included a generally worded circumvention clause in the chapter on rules of origin.[7]

Anti-circumvention rules for anti-dumping provisions are also more akin to anti-abuse rules in tax and an investigation of the purpose.[8]

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[5] https://www.wto.org/english/tratop_e/roi_e/roi_info_e.htm

[6] For an overview of different rules applied, see: https://findrulesoforigin.org/

[7] "A good shall not be considered to be an originating good merely by reason of […] any production or pricing practice in respect of which it may be demonstrated, on the basis of a preponderance of evidence, that the object was to circumvent this Chapter" North American Free Trade Agreement, art. 412.

[8] For example, the anti-circumvention provision of the EU Regulation on the matter of circumvention is defined as "change in the pattern of trade between third countries and the Union or between individual companies in the country subject to measures and the Union, which stems from a practice, process or work for which there is insufficient due cause or economic justification other than the imposition of the duty" (Council of the European Union 2016, art. 13).

Rules of origin in trade services have been subject to far less attention by academics and policymakers (Dinh 2020). However, rules with similar functions exist, and their application has occasionally become subject to dispute (Dinh 2020). However, rather than to rules of origin in trade of goods they are more similar to those used in the investment and tax areas, as they rely on tests of "substantial business activities" in a member state (Zampetti and Sauvé 2006, 135). In the US–Mexico–Canada Agreement (the successor of the North American Free Trade Agreement), for example, virtually the same denial of benefits clause is used in both investment and cross-border service chapters.[9]

Dinh criticizes that rules of origin for services concern only the "origin" (or better residence) of the supplier of the service, but not the economic origin of the service, which could be different if the service is outsourced to subcontractors residing in third countries (Dinh 2020).

4 Comparison Across Areas

In all three areas, the need for rules capable of combatting treaty shopping arises from the potential of circumvention of preferential rules based on geographical origin, even though this potential may be more or less serious depending on the benefits of bilateral treatment. However, the landscape has evolved differently across the regimes. In the following section, I compare the approaches adopted in different policy areas and review academic discussions around them.

4.1 Routinely Applied Rules or an Anti-Avoidance Approach

In the trade regime, rules are routinely applied, are very detailed, and not even primarily considered as anti-avoidance devices. Zampetti and Sauvé, for example note that, "Rules of Origin are (or should be) merely definitional in character" (Zampetti and Sauvé 2006, 114). In fact, they could be compared to transfer pricing rules in the tax arena, which are very detailed and routinely applied, even in transactions without tax-saving potential for a company. The investment regime represents the opposite end of the spectrum, as the application of anti-treaty shopping rules is clearly associated with an anti-avoidance motive. In the tax regime, different rules have been used in the past but since the BEPS Project, the dominant approach has also been an anti-avoidance approach.

One reason for this divergence may lie in the frequency of their application: Whereas in the investment regime the need to check whether an investor has the right to benefit from a preferential treatment granted by a treatment really only

[9] Articles 14.14 and 15.11 of United States–Mexico–Canada Agreement.

arises in the situation of a possible dispute, the need to apply the correct customs treatment arises in most countries several hundreds or thousands of times every day.[10] However, as referenced above, Felbermayr, Teti, and Yalcin argue that the potential for treaty shopping (or trade deflection, as they call it) is unprofitable for the majority of country-pairs. Therefore, it is questionable whether routine application, which involves a burden of documentation for the relevant economic actor, is justified (Felbermayr et al. 2018). In the investment regime the anti-avoidance regime makes sense since treaty shopping is unlikely to go undetected. When there is a dispute, high stakes are usually involved, and a host government will likely invest resources to explore whether treaty shopping can be used as argument to fend off the dispute.

On this dimension, the tax regime is more similar to the trade regime, since the need to apply a tax treaty arises frequently as well, usually at least once a year for every taxpayer with relevant cross-border transactions. Hence, it is somewhat surprising that the standard approach in tax is now an anti-avoidance approach.

4.2 Mechanical Rules vs. Tests Based on Facts and Circumstances

One can also observe a divergence between mechanically applied rules and those that rely on facts and circumstances. Here again, trade in goods is different from the rest. While in investment much attention is paid to the circumstances in each individual case, trade in goods relies on objective tests, which, however, can be very detailed and differentiated across different situations. Both approaches are used in tax, but the facts and circumstances test is more prevalent.

Usually, the facts and circumstances tests have spurred criticism: Authors have raised concerns that the general anti-avoidance approach in tax could justify non-respect of the treaty in too many circumstances and hence erode the tax treaty's core function of alleviating double taxation (De Broe and Luts 2015). Developing country governments, on the other hand, are concerned that they cannot effectively apply the rule, due to a lack of administrative resources that can be dedicated to carrying out fact-intensive, case-by-case analyses approach (Heitmüller 2024).

However, Dinh argues that the "experiences in the area of trade in goods also reveal that lengthy and detailed origin rules are not always synonymous with complexity. Indeed, the restrictiveness of the rules does not depend solely on the complexity, but indeed the thresholds used in the rules themselves are also one of the factors" (Dinh 2020, 143). Whether detailed rules are burdensome rather depends on whether the information necessary to apply them is readily available or not. Dinh suggests that in the future it could be possible to make trade in services rules of

[10] Of course, most countries only verify a fraction of imports and exports.

origin more similar to rules in trade of goods as more sophisticated statistics on trade in value added become available.

In the case of investment, arguments against attributing nationality based on the ultimate shareholders of an investment are that this is frequently difficult to verify, especially in cases of widely held companies with changing ownership (and with several intermediaries, such as investment funds) (Böhme 2021). However, a similar argument such as the one Dinh makes in the context of services could apply here, as more countries and more countries are introducing ownership registers (see chapter by Ates et al.).

Nevertheless, objective tests can be circumvented, as illustrated by the fact that countries have introduced additional anti-avoidance rules in rule of origins provisions of trade agreements. If, however, the alternative is a complete lack of application of an anti-avoidance rule as the experience in tax suggests, more objective tests appear preferable.

4.3 Should Treaty Shopping Be a Concern at All?

Finally, it is interesting to note that in all three areas, there are debates among academics and policymakers regarding whether treaty shopping should be combatted at all. The arguments that are advanced are similar. With respect to investment, Chaisse, for example, argues that "treaty shopping is not, in principle, prohibited under international investment law, as the precise purpose of IIAs is to encourage investment" (Chaisse 2015, 228). With respect to trade, many authors consider rules of origin simply to be distortionary because of the administrative burden required for compliance and the potential for discriminatory treatment (Mavroidis 2018; Felbermayr et al. 2018; Geraets et al. 2015). For instance, Zampetti and Sauvé argue that consumers are disadvantaged by strict rules of origin for services trade since they may not have access to the most competitive service provider (Zampetti and Sauvé 2006). In the tax area, such arguments even have had legal consequences, for instance in the Azadi Bachao Andolan case, where the preamble of the India–Mauritius tax treaty, which like many treaties refers to broad objectives such as enhancing trade and investment between the countries, was used to justify tolerance of treaty shopping (Union Of India (Uoi) And Anr. vs Azadi Bachao Andolan And Anr. 2003; Baistrocchi 2008).

These arguments all come from a similar perspective that considers treaty shopping within the context of the overall liberalizing (or at least multilateralizing) goal of the respective regime. If one considers bilateralism as a second-best world or just an intermediary step towards the end goal of a fully liberalized regime, one would not consider treaty shopping as undesirable.

These arguments are usually balanced by counterarguments that again are similar across areas. In tax, one argument is that treaties that make a country vulnerable to treaty shopping are often those concluded when negotiation teams had little experience and do not distribute taxing rights in a fair way (Hearson 2021). Since newer

investment treaties are usually less liberal than older ones in terms of the rights granted to investors, a similar argument may apply (Alschner 2022). Geopolitics is also often considered (Finelli 2023). In the EU-Canada Comprehensive Economic and Trade Agreement (CETA), for example, anti-treaty shopping rules for investment and trade apply a stricter test to entities in an intermediary country that are connected to third countries to which the country in question applies sanctions (*EU-Canada Comprehensive Economic and Trade Agreement (CETA)* 2017, art. 8.16).

Inspiration can be taken from the tax regime to prevent interpretations that consider treaty shopping as permissive. Following the introduction of an anti-avoidance rule, the Base Erosion and Profit Shifting Project encouraged countries to change their tax treaties' preambles to clarify that encouraging treaty shopping is not the goal of a bilateral tax treaty (OECD 2015).

4.4 Interactions

Do the treaty shopping phenomenon and the countermeasures adopted by states in the different areas interact with each other? Five types of interactions can be mentioned:

First, one type of treaty shopping opportunity may induce investors to take them in other areas, as well. Thrall shows that, for instance, multinational enterprises first established special-purpose entities to gain tax benefits and later used the same entities for investment treaty shopping (Thrall 2021).

Second, countermeasures taken in one area can have consequences for behaviour in other areas. For instance, when countries adopt stricter rules of origin in trade, or stricter local substance requirements in tax, this may induce companies to invest more in an intermediary country and to increase the amount of local value added and local activities.

Third, recently, investment disputes have arisen with respect to the correct application of anti-treaty shopping measures in tax, such as in the *Lone Star* case (see the chapter by Garcia Olmedo in this volume).

Fourth, policy ideas appear to be influencing the development of policies across areas. For example, the term "treaty shopping", which is now commonly used in the investment policy community, was borrowed from the tax community, where the phenomenon had emerged earlier (Baumgartner 2016, 7). Nevertheless, the different policy discussions still mainly take place in isolation from each other as negotiators of tax, trade, or investment treaties are frequently coming from different ministries (Owens and Zhan 2018, 5).

A symptom of this may be a fifth type of interaction, which until now is of an entirely hypothetical nature, however: The PPT rule tackles tax treaty shopping by querying whether obtaining the benefit of the tax treaty is the principal purpose of a transaction. However, such a design may open the door for an argument by companies or individuals that a specific scheme was designed not principally to take

advantage of the tax agreement, but also to take advantage of a preferential trade treatment or a bilateral investment treaty. From the point of view of the host state, this should not make the arrangement more desirable because it may be equally opposed to treaty shopping for trade benefits or investment protection. However, such an arrangement could escape the letter of the principal purpose test used in tax treaties. Therefore, it could be desirable for countries to adopt measures that protect them from treaty shopping more generally, without focusing on one particular area only.

5 Conclusion

Can anything be learned from one regime for the other? The characteristics of the treaty shopping phenomenon and responses adopted to it are different in each area but also show some similarities. The response to treaty shopping in trade in goods is clearly the odd-one out, which correlates with the differences in the nature of the issue. However, there is already a significant overlap in the issues and approaches to treaty shopping with respect to trade in services, investment, and tax purposes. Hence, there may be scope for harmonization across these issue areas. This could lead to a pooling of administrative resources and increased legal certainty for economic actors. For example, in each country, one agency could be responsible for auditing the geographic origin of a transaction under a common criterion and the outcome of the audit would be valid for the purposes of applying a tax treaty, an investment treaty, and a preferential services trade treaty. Moreover, international organizations working in the areas of tax, trade, and investment could collaborate to define a common standard for tackling treaty shopping.

Further, some innovations from one policy area may lend themselves for application in another. For instance, the idea "customs unions" from the trade regime could be transposed to tax. For example, treaty shopping would be a reduced concern for EU countries if the EU started agreeing tax treaties with third countries on behalf of all their member states and set common tax rules applicable to third countries in the absence of a treaty. In investment, a similar movement has already started as the EU has started negotiating common investment and trade agreements with third states (e.g. CETA).

In the tax regime, international harmonization of rules is most advanced. In the investment regime, there is already a discussion to use a multilateral mechanism to update treaties, similar to the Multilateral Instrument of the BEPS project to include anti-avoidance rules across the board (Böhme 2021, 530). This may also be fruitful for the trade regime.

More generally, the chapter has shown that being aware of academic debates and policy considerations from one policy area can be useful for those engaged in another, be it only for recognizing that different approaches exist and that similar arguments are being exchanged.

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Hidden Dynamics and Hierarchies in Tax Policy: A Critical Assessment of Fairness in OECD, EU, and UN

Ezgi Arik

1 Introduction

The relationship between tax, trade, and investment is inevitable as they interact in various areas, such as the digital economy (Chaisse and Mosquera 2022) or transfer pricing (Bird et al. 2009, 418). In this interaction, they sometimes use the same conceptual language with divergent or convergent meanings. Fairness is one of the common concepts, among others, used in these areas. Accordingly, it is prevalent to see concepts like "fair trade," "fair investment conditions," or "tax fairness." Nevertheless, despite its relevance in tax, trade, and investment, fairness is not a concept with a globally agreed meaning. Aside from a lack of global understanding in the context of tax, trade, and investment, the meaning of fairness diverges even within these individual disciplines. For instance, there is no single common understanding on fairness in international taxation, the concept can be used in an economic, philosophical, juridical, or political sense (Burgers and Mosquera 2017b, 768–769).

Similarly, there is no common position on the meaning of fairness in the context of international trade, and different positions have been adopted, such as liberal ideas of fair play, distributive justice, and anti-globalization (Bird et al. 2009, 411–415). The situation in investment law is not different. While one of the crucial standards in investment law requires fair and equitable treatment, there is no common definition of that standard, and the concept of fairness in this context can be understood as reasonableness and justice in investment (Tudor 2008, 15, 127).

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Therefore, as the concept of fairness does not have a globally agreed meaning, it is context-dependent and can have different meanings depending on who refers to it.

Although various stakeholders contribute to tax, trade, and investment discourse, international organizations (e.g., WTO, OECD, UN) and, as a supranational organization, the EU, influence these matters considerably. Accordingly, these organizations' positions on fairness can directly affect the meaning of fairness. Despite the importance of how these organizations' reference to fairness shapes the overall discourse of tax, trade, and investment, this Chapter will primarily focus on how the OECD, the UN, and the EU conceptions of fairness specifically shape international tax policy discourse. Nevertheless, it should be mentioned that the overall argument of this Chapter can be extended to the trade and investment context, as the concept of fairness does not have a common meaning, and international and supranational organizations play a crucial role in shaping the meaning of fairness in these disciplines.

If there is a lack of an explicit globally accepted definition, the dominant actor's ideological position might potentially affect other actors' discourses (Foucault 1980, 3). Accordingly, other actors might follow the discourse position of the dominant actor, even though they do not reflect their ideology on a certain issue. In this case, the other perspectives remain at risk of being underprivileged, which might potentially be as influential as the dominant perspective. Concerning the concept of fairness in international tax matters, there is no global meaning, and the claim is not that there should be a global understanding of fairness.[1] Nevertheless, there should be awareness that due to a lack of common sense, the meaning of the concept might be shaped, primarily influenced by the dominant actor's ideological position.

The Chapter argues that the current position of the OECD on fairness in international tax-related issues might dominate the tax discourse. Consequently, this dominance might prevent us from seeing the ideological perspectives of fairness in UN and EU discourses. This could cause the acceptance of the dominant actor's position as reflecting global interests without question. Nevertheless, assuming the concept of fairness used by the OECD might reflect global concerns could be misleading as, for instance, developing and developed countries have different perceptions of fairness (Burgers and Mosquera 2017a, 41–45; Bird and Zolt 2003, 21–23). Thus, the perspectives on fairness need deeper analysis as no agreed definition exists. This Chapter examines the discourses of the OECD, the UN, and the EU to understand their perspectives on fairness and how their discourse positions can affect the concept of fairness in international tax governance.

[1] It should be noted that Paul Lamberts in his article advises to have an agreed definition of "fair taxation to achieve the clear goals." *See* in Lamberts (2017, 50).

2 Deconstructive Contextualization of the Concept of Fairness

2.1 Deconstructive Thinking

The concept of fairness in international tax matters has already been analyzed from several perspectives. Accordingly, "fairness" in international taxation is not a new subject. Nevertheless, although the initial topic of this paper is a concept that is somehow familiar to the literature, the novelty lies in the deconstructive contextualization of fairness in the OECD, UN, and EU discourse. A deconstructive perspective can highlight hierarchical orders by revealing overprivileged and underprivileged areas (Derrida 1997; Derrida 1988, 1; Derrida 1981). With this, we can inquire how the dominance of a certain area could affect how we see things. Accordingly, deconstructive thinking could reveal the dominant issues and remind us that less-privileged areas can be as important (or influential) as dominant ones.

From the perspective of this Chapter, the overprivileged status of the OECD is pointed out. The OECD can be considered dominant in international tax discourse when the vast influence of the OECD Model Convention,[2] the dominance of the elements in the Base Erosion and Profit Shifting ("BEPS") Action Plan, the Multilateral Instrument ("MLI"), the minimum standards, and recently the discussions on Pillar One and Pillar Two are considered. Therefore, the discourse position of the OECD in international tax matters inevitably affects the rest of the international tax discourse. Accordingly, its discourse position could also potentially affect the understanding of the concept of fairness. Thus, deconstructive thinking on fairness can reveal how the dominance of the OECD's discourse could affect other discourses. Considering this, it is not possible to analyze the discourses of the UN and the EU without acknowledging the potential influence of the OECD.

2.2 The Concept of Fairness in International Tax Discourse

The concept of fairness does not have an agreed meaning in international tax discourse, and this issue has been raised several times in the literature (Lamberts 2017; Burgers and Mosquera 2017b; Debelva 2018; Lind 2021).[3] The lack of a shared understanding of fairness has led to the identification of the different fairness senses

[2] Even though the UN Model Convention is for the bilateral treaties signed between developing and developed countries, the OECD Model Convention has been increasingly followed by the non-member countries (mostly the developing countries) instead of the UN Model Convention. *See* in Pistone (2012, 2).

[3] Alice Pirlot conducted case studies on the EU Commission's discourse and concluded that the concept of fairness is vague and ambiguous. *See* in Pirlot (2020).

used in international tax discourse.[4] Accordingly, an economic, philosophical, political, and juridical sense of fairness is defined in the literature (Lamberts 2017; Burgers and Mosquera 2017b; Debelva 2018; Fleming et al. 2001). The economic sense of fairness is mainly understood as horizontal (same tax treatment as those under the same conditions) and vertical (different tax treatment than those under different conditions) equity.[5] The reflection of these concepts, specifically in the international tax context, refers to inter-nation equity, which refers to concepts such as paying taxes where value is created or paying the fair share (Lind 2021, 4; Burgers 2021; Debelva 2018, 573; Burgers and Mosquera 2017b, 775). The political sense of fairness is addressed in the literature as a global shared responsibility for the burdens and benefits of taxation (Debelva 2018, 566), with reference to concepts such as justice, global justice, and public goods (Burgers and Mosquera 2017b, 772–773). Furthermore, fairness in a philosophical sense is analyzed by referring to the concepts of justice, distributive justice, and social contracts (Burgers and Mosquera 2017b, 769–770; Debelva 2018, 566). As can be seen, the concept of justice is one of the main reference points in the philosophical sense, as in the political sense. There is no doubt that the concepts of justice and fairness are interrelated.[6] Nevertheless, the relevance of justice in both philosophical and political senses might make the differentiation between these two senses challenging. Finally, the juridical sense of fairness addresses a purely legal point of view, focusing on certain legal principles such as legal certainty, legal equality, and impartiality (Debelva 2018, 566).

Although the different senses of fairness have been analyzed in the tax literature to some extent, one perspective on fairness appears to be dominant: economic fairness (Debelva 2018, 567).[7] While the appearance of an economic sense is somehow understandable as taxation is closely related to financial and economic aspects, it might still be questionable how a concept, philosophical in origin, has become economic-oriented in international tax discourse.

[4] It should be mentioned there is also no consensus on the different approaches to fairness. For instance, Yvette Lind claims that the horizontal and vertical equity can contribute to achieving distributive justice. *See* in Lind (2021, 3). In that case, according to the majority of the literature, vertical and horizontal equity point out fairness in the economic sense. On the other hand, issues related to global justice in fairness would mean fairness in a political sense. However, in this case, it is unclear whether this proposition is related to political or economic fairness or both. Thus, it is unclear how the economic approach differs from the political one. Similarly, the differences between the political and philosophical approaches are also unclear. These different approaches are also somehow intertwined, and it is difficult to set strict boundaries. Nevertheless, these discussions are out of scope of this chapter.

[5] Economic sense of fairness is usually explained in the literature with a reference to Adam Smith and his book on the Wealth of Nations.

[6] Peter Hongler claims that "justice" and "fairness" are intertwined. *See* in Hongler (2019, 4).

[7] It should be noted that, unlike most of the tax literature, Allison Christians focuses on fairness from a human rights perspective. The sense that Christians is referring to can be accepted as an example of fairness in a philosophical sense. *See* in Christians (2009, 211).

3 Case Study: The Meaning of Fairness in Different Discourses

3.1 The Scope of the Analysis

As previously mentioned, different fairness senses have been addressed in the literature. These are the economic, political, philosophical, and juridical aspects of fairness. It should be noted that this Chapter does not search for the definition of fairness in different senses. Instead, it takes already-defined meanings in the literature. Accordingly, this Chapter inquires about which senses of fairness are being used in the OECD, UN, and EU discourses and how their discourse positions can affect the international tax discourse in general. To that end, not all fairness senses are searched separately. Therefore, the philosophical and political senses of fairness will be considered together within the scope of this paper, as they are very close to each other. For instance, with reference to justice, fairness can be accepted as used both in a philosophical and political sense. Differentiation may be possible, but this is beyond the scope of this Chapter. Thus, political and philosophical senses of fairness will be considered together, without attempting to distinguish between them, even if such a distinction may exist.

The case study will be conducted on the chosen documents of the OECD, the UN, and the EU to understand their discourse positions on fairness in international tax matters. Documents were selected based on certain criteria to limit the scope, as these organizations publish hundreds of documents. Accordingly, limitations have been created based on time and subject matter. Since the initiation of the BEPS Project by the OECD, BEPS-related issues have dominated the literature[8] and international tax conferences.[9] For this reason, the subject matter has been limited to tax avoidance and tax evasion, as these subjects were the center of the BEPS Project. Consequently, the time limitation was determined as documents published as of 2013, corresponding to the initiation of the BEPS Project.

After choosing the documents for the analysis, documents that included the concept of fairness (or fair, unfair) were selected for detailed analysis. A detailed study examines how different organizations use the concept of fairness and which senses are used in different discourses. Additionally, it is believed that analyzing only the

[8] It should be noted that the following references are given in an exemplary way. There are a lot more publications on BEPS-related areas. *See*, e.g., (Brauner 2014; Shrivastav 2015; Christians 2017; Rocha and Christians 2017; Brauner 2016; Brauner 2017; Avi-Yonah and Haiyan 2017; Van Apeldoorn 2018; Moreno and Brauner 2019; Dourado 2019; Mosquera 2020; Schoueri and Tomazela 2021; Brauner 2023).

[9] It should be noted that there are more conferences addressing BEPS-related issues. Thus, the following conferences are given as an exemplary way. *See*, e.g., International Taxation: Base Erosion, Profit Shifting (2014), Base Erosion and Profit Shifting (BEPS) (2015), The OECD/G20 (BEPS) (2015), The Impact of BEPS on Business (2016), Assessing BEPS (2017), Anti-BEPS and Protection of Taxpayers Rights (2019), Reflections on BEPS (2020), International Taxation, BEPS, and PPT (2020), Transfer Pricing Implications of BEPS (2023).

concept of fairness is not sufficient to fully understand the discourse position. For instance, even though the concept of fairness might look like it is used in a philosophical sense in the first instance, it might not fully show the discourse position as there might be hidden dynamics in the documents. In this case, the discourse position should be supported with related concepts to determine whether the concept of fairness is used in a certain sense. Accordingly, if the concept of fairness is used in a philosophical or political sense, then there should be a sufficient reference to concepts such as justice, morality, or human rights (including social rights[10]). The initial understanding of the discourse should be supported by related concepts.

Similarly, in the economic sense, the discourse should be supported by concepts such as revenue, financial, or fair share.[11] Thus, to fully understand the discourse positions of these organizations, other supporting concepts[12] rather than fairness will be analyzed in the documents as well. Sometimes, discourse can refer to fairness in a philosophical sense regarding the right to development for all human beings. Nevertheless, if the rest of the discourse highlights the importance of taxation for enabling a fair contribution to revenue, there is an indication that the economic sense is followed more than the philosophical one. Accordingly, the dominant discourse position suggests otherwise, despite reference to fairness in the philosophical sense in the discourse.

3.2 The OECD

The document Action 1 Final Report will be analyzed in detail as it refers to the concept of fairness in most of the selected documents (*see* Appendix Table 5) (OECD 2015). This document is one of the Final Reports within the scope of the BEPS Project, specifically addressing the digital economy's tax challenges. Accordingly, the Action 1 Final Report tackles BEPS challenges in a digital economy. In this document, some of the BEPS risk areas have been addressed as economic activities and value creation, the permanent establishment definition that aligns with the digital economy, controlled foreign company ("CFC") rules, and value added tax ("VAT"). Therefore, the Action 1 Final Report analyzes these issues, emphasizing certain principles to be considered for tax policy design for the digital economy. These principles are identified as neutrality, efficiency, effectiveness and fairness, flexibility, and equity (OECD 2015, 20–21).

[10] Human rights are a general term for other specific economic, cultural, social, or political rights. In case the discourse refers to particular types of rights, such as social rights, it needs to be considered under the scope of human rights.

[11] It should be noted that other supporting concepts can be chosen as these do not represent an exhaustive list of related concepts.

[12] It should be noted that these chosen concepts should be accepted as indications on understanding the discourse position concerning the concept of fairness. Thus, they should not be accepted as the only related concepts with fairness.

Thus, the concept of fairness in the analyzed document is essential as the OECD explicitly states that fairness should be considered while developing tax policy solutions for the challenges arising from the digital economy (OECD 2015, 134–136). The concept of fairness is primarily used in the context of VAT. Action 1 Final Report points out the VAT exemption for low-value imports and how it caused a decrease in VAT revenues (OECD 2015, 120–121). Additionally, the possible unfair results between importers and domestic retailers that are required to charge VAT are emphasized. Accordingly, the OECD uses the concept of fairness as a financially fair result for taxpayers. The document also explains the concept of fairness as follows: *"The potential for tax evasion and avoidance (*e.g.*, undervaluation and misdescription) should be minimized (while keeping counteracting measures proportionate to the risks involved.* Thus, under a specific document, the concept of fairness has been primarily referred to as fairness for taxpayers and for countries by eliminating tax avoidance and tax evasion. The results of the analysis show that the OECD uses fairness in an economic sense without reference to fairness in a philosophical and political sense.

After this determination, the other supporting concepts are examined in the document to understand whether they also support the identified position of the OECD concerning the concept of fairness. Thus, the concepts of justice, morality, human or (social) rights, development, revenue, fair share, financial, and profit were searched in the document to see their occurrence. Accordingly, more references to justice, morality, human rights, and development would contribute to the philosophical and political perspective on fairness, while other concepts would support the economic position of the OECD. In Table 1, the number of references to each concept is presented.

Concepts Supporting the Philosophical and Political Sense of Fairness: Justice, Moral, Human Rights, Social Rights, and Development

The analyzed document does not refer to the supporting concepts of fairness in a philosophical and political sense. This result aligns with the initial determination that the OECD uses fairness in an economic sense.

Table 1 Word counts in addressing the tax challenges of the digital economy, Action 1, 2015 Final Report

Addressing the tax challenges of the digital economy, Action 1, 2015 final report	
Justice	0
Moral	0
Human rights Social rights	0
Development	0
Revenue	142
Fair share	3
Financial	43
Profit	195

Concepts Supporting the Economic Sense of Fairness: Revenue, Fair Share, Financial, and Profit

The Action 1 Final Report emphasizes the importance of raising *revenues* for countries to finance public expenditures (OECD 2015, 20). Additionally, the document refers to inter-nation equity by claiming that every country should have its share of tax *revenues* coming from cross-border transactions (OECD 2015, 21). Specifically, from the perspective of VAT, how the exemption for low-value imports could adversely affect VAT *revenues* has been pointed out (OECD 2015, 120). The OECD raises concerns about these VAT challenges, as it might incentivize local businesses to relocate to offshores and create an unfair situation for domestic companies in addition to *revenue* loss (OECD 2015, 122, 184). Along with the emphasis on *revenue* collection and the prevention of loss of *revenue*, this document also often refers to the concept of *profit*. The concepts of *revenue* and *profit* are closely related to OECD discourse. Accordingly, the primary aim of the document is to develop a system that ensures that *profits* are taxed where economic activities are and value is created (OECD 2015, 3). In turn, taxing the necessary *profits* of taxpayers contributes to *revenue.* The concept of *financial* is broadly referred to in the analyzed document of the OECD. This result is expected because the OECD is a *financial* institution that considers international taxation matters from a *financial* perspective. The concept of *financial* is referenced in a technical manner, focusing on topics such as new business models in the digital economy related to *financial* services (OECD 2015, 51), the use of *financial* payments as a tool for base erosion (OECD 2015, 89), and the role of *financial* intermediaries within the VAT intermediary collection model (OECD 2015, 124, 125). Finally, the reference to *fair share* has been made to claim that taxpayers must pay their fair share and that tax avoidance, harmful practices, and aggressive tax planning should be prevented. Accordingly, as a result of the analysis of the supporting concepts, it can be understood that the OECD almost always uses the concept of fairness in the economic sense with a broad focus on collecting revenues.

3.3 The UN

The document the UN Manual on Transfer Pricing will be analyzed in detail as it refers to the concept of fairness most among the selected documents (*see* Appendix Table 6) (UN 2021). The document presents the recent developments in transfer pricing. The transfer pricing-related issues have been addressed in the UN Manual on Transfer Pricing, considering the special needs of developing countries and their specific experiences with that matter (UN 2021, Foreword iii). Therefore, the document begins by presenting transfer pricing issues such as the arm's length principle, comparability analysis, and transfer pricing methods. The UN Practical Manual on Transfer Pricing gives special attention to a common understanding of the arm's length principle to avoid double taxation.

The UN Manual on Transfer Pricing refers to the concept of fairness from different perspectives. For instance, in its Foreword, it is stated that the document aims to enable the effective operation of the arm's length principle in developing countries so that the investors in the developing countries can have fair and predictable results (UN 2021, Foreword xiii). Accordingly, searching for fairness from the perspective of investments can point out the concept of fairness in an economic sense. Another perspective is given as fairness for taxpayers in administrative practices of developing countries. For instance, in case tax administrations use secret comparable, it might have unfair results for the taxpayers (UN 2021, 120). Additionally, according to the document, the dispute resolution systems used by tax administrations might also trigger unfair consequences for taxpayers with unnecessary disputes (UN 2021, 429, 448, 470, 511, 514, 522). Therefore, the UN Manual on Transfer Pricing approaches the concept of fairness from a rather philosophical sense, as the references are directly related to the taxpayer's rights. Similarly, the document raises concerns about mandatory tax treaty arbitration and how those rules might bring unfair results for less-experienced developing countries against developed ones (UN 2021, 531). Thus, fairness in a philosophical and political sense has been again referred to.

As a result of the general analysis of the document, it seems like the UN refers to fairness both in an economic sense and also in a philosophical and political sense. In the next step of the analysis, the UN's position on fairness might be better understood. The concepts of justice, moral, human (or social) rights, development, revenue, fair share, financial, and profit have been searched in the document to see their occurrence. Accordingly, more references to justice, moral, human rights, and development would contribute to the philosophical and political perspective on fairness, while the other concepts would support the economic position of the UN. The number of references to each concept is given in the table (Table 2).

Table 2 Word counts in the UN Practical Manual on Transfer Pricing for Developing Countries

UN Practical Manual on Transfer Pricing for Developing Countries	
Justice	0
Moral	1
Human rights Social rights	0
Development	17
Revenue	81
Fair share	1
Financial	410
Profit	More than 600[a]

[a]The exact number for the concept of profit is not provided as it is referred more than 600 times, it is sufficient to accept that as it is referred very often

Concepts Supporting the Philosophical and Political Sense of Fairness: Justice, Moral, Human Rights, Social Rights, and Development

In the document, the concepts of *human rights (or social rights)* and *justice* have never been referred to. Additionally, there is only one reference to the concept of *moral*. Nevertheless, that reference does not constitute a *moral* consideration. But, it is referred to as "*moral* hazard issues" to explain the situations under intra-group financial guarantee fees (UN 2021, 388). On the other hand, the concept of *development* has been referred to in the UN Manual on Transfer Pricing. The document claims that not following the arm's length principle might hinder cross-border transactions and *development* (UN 2021, 288, 513). Although the concept of *development,* as used in the document, might seem as a contribution to the philosophical and political sense of *fairness,* the concept has been used as *economic development,* but not as *development* as a part of human rights. Accordingly, it can be said that the overall discourse of the UN Manual on Transfer Pricing does not contribute to *fairness* in a philosophical and political sense.

Concepts Supporting the Economic Sense of Fairness: Revenue, Fair Share, Financial, and Profit

In a document on transfer pricing, it is inevitable to refer to the concept of *financial* and especially *profit* (as *profit is* also broadly used in transfer pricing methods). Accordingly, the choice of the UN on preparing a document on transfer pricing and approach that subject from a *financial* perspective (UN 2021, 36) shows in a way that the UN focuses on the more *financial* side of transfer pricing rather than human rights-based perspectives. For instance, the UN could have analyzed how the transfer pricing manipulation affects the right to development of individuals or how/why these practices are morally unacceptable. However, as the document raises more *financial* concerns, it can indicate that the UN uses fairness more in an economic sense.

The UN Manual on Transfer Pricing also claims that transfer pricing regulations are crucial to enhance cross-border transactions and prevent losing tax *revenues.* The document emphasizes the importance of raising tax *revenue* for developing countries (UN 2021, 353). Thus, the extensive focus on the collection of *revenue* might be accepted as an economic motivation and can contribute to the concept of *fairness* in an economic sense.

Finally, the concept of *fair share* has only been used once in the Country Practice—China of the document. Accordingly, it is stated that the transfer pricing issues are initially to deal with the allocation of taxing rights between jurisdictions and eliminate double taxation. Despite that, the current tax reform project focuses on addressing double taxation and paying the *fair share* (UN 2021, 558). Accordingly, the UN has not focused on the concept of *fair share* in its discourse. Thus, the analysis shows that despite certain references to fairness in the philosophical and political sense of fairness, the throughout discourse of the UN follows fairness in an economic sense.

3.4 The EU

The document Annual Report on Taxation 2022 ("the Annual Report") will be analyzed in detail as it refers to the concept of fairness most among the selected documents (*see* Appendix Table 7) (EU 2022). The Annual Report presents a general analysis of the design and performance of member states' tax systems, as well as certain international tax developments, such as green taxation, digitalization, and business taxation (EU 2022, 14). Although the concept of fairness is not the main focus of the Annual Report, there is a considerable reference to fairness from various perspectives, including in the context of tax avoidance and tax evasion (EU 2022, 37–68).

In the Annual Report, the importance of a fair and effective tax system to secure tax revenue, finance public expenditures, and enable fair, sustainable growth has been mentioned several times (EU 2022, 4, 29, 139). The Annual Report analyzes the concept of fairness in different areas, such as work incentives and labor taxes, income inequality, health taxes, tax avoidance, and tax evasion from international and EU perspectives. Concerning tax avoidance and tax evasion, the EU appraises the efforts of the OECD to tackle tax avoidance at the global level and highlights the Pillar Two Agreement as an essential step for addressing current issues (EU 2022, 56, 142). As per the EU-level actions on tackling tax avoidance and tax evasion, the Annual Report points out the EU list of non-cooperative jurisdictions and how there is a risk of tax abuse and tax competition having unfair results (EU 2022, 58). The Annual Report refers to tax avoidance and tax evasion as being a revenue loss which should be avoided (EU 2022, 59–62). Accordingly, it can be said that the EU, in its analyzed discourse, follows the economic sense of the concept of fairness with references to economic concepts such as growth, revenue loss, or public finance.

On the other hand, the EU also refers to fairness in philosophical and political senses. For instance, in the Foreword, the Annual Report refers to an approach that considers fairness for all levels of society (EU 2022, 4). The Annual Report also refers to fairness in the context of the Green Deal. Although the reference has some elements of economic fairness with attention paid to economic growth and revenue sustainability, it also points out that balancing climate change can enable a fairer society (EU 2022, 96). Therefore, although it is not possible to say that the Annual Report only refers to fairness in an economic sense, that sense appears more frequently compared to the philosophical and political ones. Thus, in the first instance, it seems that the EU follows an economic sense of fairness in its discourse, with a slight consideration of philosophical and political senses. Nevertheless, further analysis will be conducted to understand whether these positions are supported in the discourse.

The concepts of justice, moral, human (or social) rights, development, revenue, fair share, financial, and profit have been searched in the document to see their occurrence. Accordingly, more references to justice, morality, human rights, and development would contribute to the philosophical and political perspective on

Table 3 Word counts in annual report on taxation

Annual report on taxation	
Justice	1
Moral	0
Human rights Social rights	1
Development	4
Revenue	138
Fair share	2
Financial	52
Profit	50

fairness, while other concepts would support the economic position of the EU. In Table 3, the number of references to each concept is given.

Concepts Supporting the Philosophical and Political Sense of Fairness: Justice, Moral, Human Rights, Social Rights, and Development

The reference to these concepts has not been made very often in annual reports. First, it can be seen that reference to the concept of *justice* has only been made once in the context of international tax avoidance, and how it can adversely affect social *justice* (EU 2022, 44). Similarly, the EU also considers rights from a social perspective but not in the context of international taxation. Accordingly, the Annual Report emphasizes that income inequality can hinder the European Pillar of Social Rights (EU 2022, 45). Although there is no direct reference to the concept of human rights, a reference to *social rights* (i.e., the right to education, health, and water) is still a human rights-related reference. In the Annual Report, there are several references to "taxing rights," which could support the concept of fairness in an economic sense as it indicates the revenue collection of states. The Annual Report points out the concept of development in the context of green taxation by showing that EU member states have reached a certain level of human development. However, climate change-related issues remain a challenge (EU 2022, 83, 140). Finally, there was no reference to morality. As can be seen in the analyzed document, the EU has a limited reference to the concepts supporting the philosophical and political sense of fairness.

Concepts Supporting the Economic Sense of Fairness: Revenue, Fair Share, Financial, and Profit

The concept of *revenue* has been referred to in the Annual Report very frequently, as it is not surprising to indicate revenue in a document on taxation. Nevertheless, it is still important how the EU has used the concept. The Annual Report supports the idea that a fair tax system is needed to ensure stable and sustainable tax *revenue* (EU 2022, 22). Additionally, the document emphasizes how *revenue* collection is crucial and that revenue loss through international tax avoidance and tax evasion should be refrained (EU 2022, 14, 29, 60–62). As closely related to the concept of *revenue, profit* has been primarily used in the document in the context of base erosion and *profit-shifting* activities of companies and wealthy individuals (EU 2022, 32, 56, 80,

116, 125). Additionally, it can be seen that the Annual Report has a broad emphasis on the concept of *financial* to refer to how the *financial* crisis has affected the revenues (EU 2022, 4, 14, 21) and other tax-related *financial* concerns such as aggressive tax planning and financial activities in offshores (EU 2022, 56, 62). Although it is expected to refer to the concept of *financial* in a document related to taxation, it can still support the main discourse position, which is on a more *financial* side rather than the human rights perspective. Finally, the concept of *fair share* and how it is used can indicate which sense of fairness is prioritized in a specific discourse. Thus, EU refers to the concept in two different settings with the same motivation. The Annual Report states that everyone should pay their *fair share* to support the economy (EU 2022, 14) and to minimize tax-related administrative costs (EU 2022, 30). As can be seen, both of them support the economic sense of fairness. Therefore, as a result of the analysis of the supporting terms, the concept of fairness has been used in the Annual Report with more economic motivations rather than normative ones.

3.5 Comparative Analysis Between the OECD, the UN, and the EU

In the previous part, the OECD, the UN, and the EU conceptions of fairness have been analyzed. As a result of this analysis, the different senses of fairness used in their discourses have been identified. In this section, the outcome of the discourse analysis is evaluated comparatively.

As seen in Table 4, the OECD uses fairness in an economic sense, which is also visible in its discourse with references to supporting concepts such as revenue and profit. Similarly, the UN refers to the concept of fairness in an economic sense. Fairness in a philosophical and political sense is also visible in the UN discourse. Nevertheless, a detailed analysis showed that the UN does not support the

Table 4 Summary of the discourse analysis outcome

	Sense of fairness	Reference	Limited/no reference
The OECD	Economic sense	Revenue Profit Financial Fair share	Human rights Development Justice Moral
The UN	Economic sense Philosophical & political sense	Revenue Profit Financial	Human rights Development Justice Moral
The EU	Economic sense Philosophical & political sense	Revenue Profit Financial Fair Share	Human rights Development Justice Moral

philosophical and political sense of fairness, as it primarily focuses on the financial side. Therefore, it can be accepted that the UN mainly supports an economic sense of fairness.

Finally, the EU also refers to philosophical, political, and economic senses. Unlike the UN, the EU supports (somewhat limits) the political and philosophical senses of fairness to a certain extent throughout the analyzed document. Nevertheless, despite the visibility of the philosophical and political senses of fairness, it is clear that the economic sense of fairness dominates its discourse.

Accordingly, the economic sense of fairness seems like more dominant in all examined discourses than the philosophical and political senses. This outcome can be understandable from the perspective of the OECD, as it is an organization interested in financial matters. However, it might be challenging to understand why the UN, which aims to promote more normative values such as human rights, would use fairness in an economic sense. This issue might be explained by the effects of OECD's dominant discourse on other discourses. Therefore, we can see traces of the OECD's ideological position on fairness in both the EU and UN's discourses. Accordingly, as the UN and EU are affected by the dominant ideology of the OECD, through knowledge production in international tax discourse, they contribute even more to the ideological position of the OECD.

Apart from the analyzed organizations, the economic sense of fairness is also dominant in the tax literature. This common perspective on fairness cannot be accepted as a coincidence. Although several stakeholders contribute to shaping international tax discourse, international organizations (especially the OECD and the UN), and supranational organizations, the EU has the most influence. If the OECD (as the dominant actor) follows a certain ideology in international taxation, the UN and EU are more likely to be influenced by that ideology. As a result of this influence, the UN and EU would contribute even more to the ideology of the OECD. Inevitably, the dominant ideological position of the OECD on fairness influences the entire international tax discourse, including the tax literature.

4 Conclusion

This Chapter analyzes, from a deconstructive perspective, the discourse positions of the OECD, EU, and UN on fairness and how their positions shape tax policy discourse. It has been argued that, in the case of a lack of global understanding of a concept, the dominant actor's ideological position influences the discourse position of others. Accordingly, the discourses of the OECD, EU, and UN have been analyzed to understand which sense of fairness is being used by these organizations. As a result of the analysis, it was observed that the OECD uses economic fairness. On the other hand, the UN and the EU refer to fairness both economically, philosophically, and politically. Nevertheless, their overall discourses with reference to concepts such as revenue, profit, financial, and fair share more closely follow the economic sense of fairness. Thus, the economic sense of fairness dominates all three discourses.

This Chapter explains the dominance of the economic sense of fairness with the dominance of the OECD and its financial perspectives in international tax discourse. Therefore, we see traces of the OECD's ideological position on fairness in both the EU and UN's discourses. This dominance not only influences the observed organizations' discourses, but also directly and indirectly (through the EU and the UN) influences the general tax policy discourse. Thus, because there is no globally agreed meaning for fairness, the ideological position of the OECD could easily overshadow other perspectives on fairness.

Consequently, the dominance of the OECD's fairness approach could potentially have adverse effects on shaping global tax governance. If the economic sense of fairness is accepted as the most common approach in international taxation, reflecting global concerns, as the UN and the EU have also followed the same approach, the tax policy outcome might not correspond with global interests. For instance, we might think that the UN's conception of fairness reflects the developing countries' positions by overlooking the influence of the OECD's economic focus on the UN's discourse. However, the appearances might be misleading in addressing the interests in global tax governance. Accordingly, even if the conceptions of fairness by the OECD, the UN, and the EU are more on the economic side, it should not be accepted that their similar approaches reflect global interests, including those of developing countries. Therefore, in designing global tax governance policies, the potential influences of the dominant actors should be considered. Otherwise, there is a risk of overlooking the interests of certain groups, including developing countries, in global tax governance.

Appendix

Table 5 Word counts of "fairness" in the selected documents of the OECD

Number	Name of the document	Number of reference to fairness
1	Addressing Base Erosion and Profit Shifting (12 February 2013)	11
2	Action Plan on Base Erosion and Profit Shifting (19 July 2013)	4
3	Addressing the Tax Challenges of the Digital Economy, Action 1: 2014 Deliverable (16 September 2014)	21
4	Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, Action 6: 2014 Deliverable (16 September 2014)	0
5	Guidance on Transfer Pricing Documentation and CbC Reporting, Action 13: 2014 Deliverable (16 September 2014)	0
6	Guidance on Transfer Pricing Aspects of Intangibles, Action 8: 2014 Deliverable (16 September 2014)	2
7	Countering Harmful Tax Practices more Effectively, Action 5: 2014 Deliverable (16 September 2014)	3
8	Neutralising the Effects of Hybrid Mismatch Arrangements, Action 2: 2014 Deliverable (16 September 2014)	1

(continued)

Table 5 (continued)

Number	Name of the document	Number of reference to fairness
9	Developing a Multilateral Instrument to Modify Bilateral Tax Treaties, Action 15: 2014 Deliverable (16 September 2014)	2
10	Mandatory Disclosure Rules, Action 12, 2015 Final Report (5 October 2015)	1
11	Aligning Transfer Pricing Outcomes with Value Creation, Actions 8–10, 2015 Final Report (5 October 2015)	3
12	Making Dispute Resolution Mechanisms More Effective, Action 14, 2015 Final Report (5 October 2015)	1
13	Transfer Pricing Documentation and CbC Reporting, Action 13, 2015 Final Report (5 October 2015)	0
14	Developing a Multilateral Instrument to Modify Bilateral Tax Treaties, Action 15, 2015 Final Report (5 October 2015)	2
15	Designing Effective Controlled Foreign Company Rules, Action 3, 2015 Final Report (5 October 2015)	0
16	Measuring and Monitoring BEPS, Action 11, 2015 Final Report (5 October 2015)	0
17	Limiting Base Erosion Involving Interest Deductions and Other Financial Payments, Action 4, 2015 Final Report (5 October 2015)	9
18	Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, Action 6, 2015 Final Report (5 October 2015)	0
19	Addressing the Tax Challenges of the Digital Economy, Action 1, 2015 Final Report (5 October 2015)	33
20	Neutralising the Effects of Hybrid Mismatch Arrangements, Action 2, 2015 Final Report (5 October 2015)	7
21	Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance, Action 5, 2015 Final Report (5 October 2015)	3
22	Preventing the Artificial Avoidance of Permanent Establishment Status, Action 7, 2015 Final Report (5 October 2015)	1
23	BEPS Project Explanatory Statement, 2015 Final Reports (26 August 2016)	3
24	Neutralising the Effects of Branch Mismatch, Action 2: Inclusive Framework on BEPS (27 July 2017)	1
25	Harmful Tax Practices 2017 Progress Report: Inclusive Framework on BEPS, Action 5 (16 October 2017)	3
26	Tax Challenges Arising from Digitalization, Interim Report (16 March 2018)	4
27	Harmful Tax Practices 2018 Progress Report: Inclusive Framework on BEPS, Action 5 (29 January 2019)	3
28	Tax Challenges Arising from Digitalisation- Economic Impact Assessment: Inclusive Framework on BEPS (12 October 2020)	0
29	Tax Challenges Arising from Digitalisation-Report on Pillar One Blueprint: Inclusive Framework on BEPS (14 October 2020)	12
30	Tax Challenges Arising from Digitalisation-Report on Pillar Two Blueprint: Inclusive Framework on BEPS (14 October 2020)	27

Table 6 Word counts of "fairness" in the selected documents of the UN

Number	Name of the document	Number of reference to fairness
1	UN Handbook on Selected Issues in Protecting the Tax Base of Developing Countries (2015)	16
2	UN Handbook on Selected Issues in Protecting the Tax Base of Developing Countries—Second Edition (2017)	22
3	UN Manual for the Negotiation of Bilateral Tax Treaties between Developed and Developing Countries (2019)	1
4	UN Handbook on Dispute Avoidance and Resolution (2021)	12
5	**UN Practical Manual on Transfer Pricing for Developing Countries (2021)**	**30**

Table 7 Word counts of "fairness" in the selected documents of the EU

Number	Name of the document	Number of reference to fairness
1	Tax Reforms in EU Member States	13
2	Investing in Sustainable Development	7
3	Reflections on the EU Objectives in Addressing Aggressive Tax Planning and Harmful Tax Practices	35
4	Evaluation of Administrative Cooperation in Direct Taxation	46
5	Letter Box Companies: Overview of the Phenomenon and Existing Measures	14
6	**Annual Report on Taxation 2022**	**66**

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Transparency and Transformation: Rethinking Tax Governance in the Mining Sectors of Tanzania and Kenya

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1 Introduction

In recent years, tax transparency reporting has gained traction, with governments and investors in various sectors, including the extractive industry, increasingly embracing it. Opaqueness in tax information has been attributed as the key reason for mismanagement of resource revenue and corruption (Haufler 2010). It is perceived to be a factor that contributes to politicians' rent-seeking behavior, a phenomenon often associated with the resource curse experienced by numerous developing nations abundant in natural resources (Mehlum et al. 2006). Lack of transparency in administration and management of resource revenues can lead to distrust among the public, governments, and corporations, as well as tax evasion by multinational corporations (Craig and Kopits 1998; Gaventa and McGee 2013). Consequently, a global movement advocating for greater openness in the extractive industry has grown.

Global initiatives have advocated and developed guidelines and standards to promote the disclosure of revenues and taxes paid by extractive companies to governments and the allocation and management of this revenue. Advocates of tax transparency view it as a means to not only ensure that governments receive their fair share of resource revenues but also to foster accountability, increase tax compliance, reduce corruption, and promote sustainable development in resource-rich countries (Haufler 2010). Multi-stakeholder initiatives like the Extractive Industries Transparency Initiative (EITI), Publish What You Pay (PWYP), Open Contracting Partnership, and Global Reporting Initiative (GRI) advocate for transparency, accountability, participation, and sustainability in governance (EITI 2019; Open

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Contracting Partnership 2023; PWYP 2024). Investors in the extractive industry have become keen on transparency reporting with industry initiatives such as the International Council on Mining and Metals (ICMM) and Initiative for Responsible Mining Assurance (IRMA) incorporating transparency reporting requirements for their members to keep up with the changing operating environment (ICMM 2003).

Countries have introduced domestic legislation in the extractive industry to align themselves with international policies. The United States of America (US) introduced Dodd–Frank legislation Section 1504 which requires listed extractive companies to disclose payments to governments to provide information to investors and support global efforts to promote transparency in the extractive industry (Security Exchange Commission (SEC) 2010); Canada's 2015 Extractive Sector Transparency Measures Act (ESTMA) requires disclosure of certain payments made by Canadian extractive entities to governments in Canada and abroad (Government of Canada 2015). Many developing countries have implemented major reforms in mining to align with international best practices. For instance, Ghana, Nigeria, and Tanzania have laws for implementing EITI requirements. However, despite the transformations and availability of guidelines on mining governance, countries have experienced mixed outcomes with some notable resource-rich developing countries facing challenges in adoption and implementation of transparency policies, ultimately falling short of realizing improvements in governance (Rosser 2006; Andrews 2013; Sovacool and Andrews 2015; Magno and Gatmaytan 2017; Ejiogu et al. 2021).

Tax transparency is a global norm intended to improve the governance of extractives but its effectiveness in improving governance has been challenged on the basis that as a global norm, it may not address the diverse needs and the different social, political, or economic contexts of various countries (Grindle 2007; Fukuyama 2013). The fact that institutional reforms driven by global organizations are not always driven by the need to solve local problems but rather by the priorities of these organizations leads us to question their efficacy in solving local problems (Andrews 2013). Lack of political commitment and inadequate capacity in poor countries act as another impediment. Scholars have not been able to establish concrete proof that these global norms improve governance and development outcomes (Andrews 2013). Therefore, implementers must critically consider norms in their contextual environment before adopting them.

The growing number of voluntary and mandatory tax disclosures impact trade and investment policies in mining. This has necessitated industry players to act and institute voluntary disclosure requirements to mitigate risk and build investors' confidence. On the other hand, governments need to consider mandatory transparency disclosures and how they interact the broader governance strategies and policies including trade and investment policies. Policymakers may incorporate transparency reporting into trade and investment policies. Harmonized transparency reporting standards may be considered in trade and investment policies to ensure a level playing field and a consistent global business environment. Countries therefore need to be aware of the importance of transparency when formulating trade and investment policies for a conducive business environment that balances economic and public interests. This underscores the importance of exploring the

conceptualization, implementation, and the transformative nature of transparency in governance.

This chapter explores the concept of tax transparency in extractives, specifically in the mining sector, based on international experiences and experiences of Kenya and Tanzania. It sheds light on the various approaches employed by countries to enhance tax transparency in mining governance, highlighting the successes and challenges, using an institutional analysis approach. This chapter provides insights into the evolving landscape of transparency practices in governance.

The section that follows delves into the theoretical framework underpinning the implementation of governance norms, preceding an analysis of the concept of tax transparency and its application in the mining sector. A comparative review of its implementation in Kenya and Tanzania follows. The chapter concludes by deriving insights and providing recommendations.

2 Theoretical Perspective

This section establishes a theoretical foundation in an effort to comprehend the motivations and mechanisms behind the adoption and implementation of transparency measures by different nations to enhance mining governance.

Governance encompasses a state's authority to formulate laws and regulatory frameworks to run a nation's affairs, and the implementation and enforcement of those laws, with the involvement of various actors (Hyden et al. 2004; Dietsche 2014). Weak governance has been associated with suboptimal development results, prompting international organizations to advocate for good governance principles, such as transparency, to strengthen governance (Brautigam 1991; World Bank 1992a; Kaufmann et al. 1999). North explains that the adoption of global governance norms can potentially drive institutional changes that in turn influence the behavior of actors, ultimately enhancing governance outcomes. Institutional analysis theories seek to explain how institutions change and how institutions affect policy outcomes.

Institutional theories define institutions as a set of rules, both formal and informal, that shape human behavior (North 2007). North and Williamson have argued that institutions matter for economic outcomes (Williamson 2000; North 2007). This implies that formal rules, informal rules, norms, and organizational structures play a crucial role in shaping human behavior, decision-making processes, and policy outcomes. From an institutional analysis perspective, governance principles like transparency aim to create institutions that will shape human behavior, that is, the behavior of state and non-state actors toward achieving desired outcomes.

Institutional arrangements influence policy outcome through a complex process (March and Olsen 2008). Hall and Taylor identify three forms of institutionalism developed from different schools of thought, to analyze how institutions influence development and implementation of policy outcomes (Hall and Taylor 1996). The three forms of institutionalism are sociological institutionalism, historical

institutionalism, and rational choice institutionalism. The interaction between these three institutional theories provides an understanding of how institutions operate and evolve in various contexts.

According to sociological institutionalism, developed by sociologists to understand institutional change, the social context, values, norms, culture, and society expectations affect how institutions operate (Schmidt 2006). The social values and norms affect the behavior of actors. Institutions are constructs of the social environment. Sociological institutionalists suggest that organizations embrace a new way of doing things, not because it makes the organization more efficient in achieving its goals, but because it boosts the organization's or its members' social acceptance. This explains the rationale behind nations embracing global norms to attain recognition and acceptance within the international community.

Historical institutionalism, developed by political scientists, explains that institutions develop from past events and once in existence do not easily adapt to change (Hall and Taylor 1996). According to this theory, it is the existing institutional arrangements that have developed over time and political economy that shapes people's behavior and policy outcomes, not the social norms and cultural values. This theory explains how historical events such as colonial history continue to influence current decision-making and behavior. It explains why inefficient institutions may persist and resist reforms. However, critical junctures which are periods of significant change such as financial crisis, change in government leadership, and civil society activism may change institutional trajectories, as witnessed in the countries' adoption of transparency norms in resource governance. Power shifts may occur during critical junctures, leading to the establishment of new institutions that redefine the distribution of political authority. Power structures influence institutional change, and institutional changes, in turn, affect power dynamics. The eventual redistribution of power among various actors shapes the implementation and outcome of policy reforms.

Rational choice institutionalism, developed by economists, posits that individuals act out of self-interest, and incentives can be used to shape their behavior (Hall and Taylor 1996; Williamson 2000). Individuals seek to maximize their utility giving consideration to their preferences and available information. Institutional changes are thereby effected to achieve efficient outcomes. Institutional structures can be used to shape the decision-making environment to achieve desired outcomes. This means that politicians can be incentivized to make reforms.

The critics of institutionalism theories note that the theories take institutions as given. However, the theories remain relevant in that they provide a framework for analyzing how institutions change and influence policy formulation, implementation, and outcome. The three institutional theories offer a holistic perspective of how institutional theories evolve and transform over time. According to the theories, policy formulation, implementation, and resulting outcome are not automatic, but rather a complex process shaped by the interactions with the social, historical, economic, and political context. This chapter applies the institutional theories to shed light on the adoption and implementation of transparency reforms in mining.

3 What Is Transparency

Transparency is regarded as a fundamental principle aimed at enhancing institutions' quality (Craig and Kopits 1998). There is a general consensus that quality institutions are a prerequisite for economic growth and development and resource-led development (Ahrens 2000; Mehlum et al. 2006; Holmberg et al. 2009). This led to the development of the concept of good governance which gained prominence from the 1990s with development aid agencies and international organizations such as the World Bank, IMF, UNDP, WTO, EU, and OECD advocating for better quality of institutions as a way to improve economic performance in developing countries (World Bank 1992a; Rhodes 1996; Kohler-Koch and Rittberger 2006). There is no concrete definition of good governance, despite the fact that it has been heavily referenced in development literature. However, common principles are considered to contribute to better governance outcomes or better institutional quality. The key principles identified in literature are transparency, accountability, participation, effectiveness and efficiency, equity, human rights, and environmental sustainability (Cheema 2005; Mimicopoulos et al. 2007; Addink 2019). Different international organizations and initiatives have established good governance principles depending on their priorities. The governance principles that stand out in international global mining frameworks are *transparency and accountability, inclusion, and environmental sustainability*. The principles of transparency, accountability, public participation, and inclusion are closely linked, in that, transparency reinforces the accountability of the actors responsible for providing information and provides a basis for public participation. This chapter narrows its focus on transparency as deployed in mining governance.

Transparency has become a common phrase in governance discussions across disciplines and is widely acknowledged as a means of providing information accessibility to mitigate corruption and foster desirable values, such as democracy and accountability, to avoid negative governance outcomes. However, the literature has not properly conceptualized transparency in governance despite its wide application across disciplines. The meaning of transparency is presumed known, although it may imply different things to different actors and within different contexts. Transparency for the government may be driven by the need to promote democracy and public participation, while investors may want to disclose particular information for their public image and may even prefer to keep some private information for commercial interests. The perception of transparency by government, investors, and international organizations and initiatives differs depending on their goals and priorities.

Some international organizations and initiatives perceive transparency as making information accessible while others perceive it as a means to an end. The UNDP (1997) defines transparency as the free flow of information, and the African Development Bank (AfDB 1999) defines it as the public access to knowledge of the policies and strategies of government. The two organizations view transparency as a way of making information accessible. Transparency International (TI) regards

transparency as a means to reduce corruption (Pope and Transparency International 2000). TI views transparency as a means to achieve an end. While the World Bank's report on Extractive industry (Salim 2003) does not provide a definition of transparency, it identifies transparency in payments and flow of revenue as one of the building blocks of governance in the extractive industry. The EU Principles of Governance require that decisions be taken and enforced in accordance with the rules and regulations for openness and transparency. These definitions do not go beyond explaining how transparency is implemented to strengthen governance.

Transparency involves making information accessible and having open processes and policies, to achieve defined objective, achieve certain values, and evaluate whether a group of actors are moving toward a set goal (Michener and Bersch 2013; Forssbaeck and Oxelheim 2014). This information should be reliable and relevant for decision-making. According to Michener and Bersch, the information should be visible, accurate, and complete. The information is made available through self-reporting, data collected by other actors, or may be driven by the need to resolve common problem (Michener and Bersch 2013). The processes, rules, and policies should be clear and predictable to the users (Forssbaeck and Oxelheim 2014; Schnell 2020). Literature has not provided guidance on how to design transparent public policies (Ball 2009). This remains open for implementation.

Transparency can be gauged based on the extent to which the intended goal or objective is achieved. This objective is an important aspect that should be defined before implementing transparency policies. The objectives can broadly be classified as functional or value driven (Forssbaeck and Oxelheim 2014). Functional refers to the improvement of governance outcomes such as economic growth, while value driven refers to achieving values such as democracy and public participation. The basic assumption is that transparency improves the quality of institutions, leading to more foreign investment, an increase in government revenue from mining, and better revenue management for resource-led development. Thus, the evaluation criteria depend on the goals of the specific transparency policy being implemented.

Transparency is a complex concept; hence, it is difficult to define it in various governance frameworks. Notwithstanding, it is essential that any implementing country properly define the concept before applying it in any given context. The following aspects of transparency need to be carefully considered: *goal, nature of the information disclosed, structure and scope of the information, providers and users of the information, and whether it is voluntary or mandatory*.

An effective transparency policy should meet the following criteria: clearly defined policy objective; clearly defined scope and nature of information to be disclosed; instituted within the law with clear enforcement measures, allowing for feedback and revision; information is accurate, comprehensive, and verifiable; platform of information to be disclosed is identified, whether a physical document, online form, or website; information disclosers and users are identified; users of information are able to interpret and use the information in decision-making for intended purposes; and use of the information leads to change in behavior of the disclosers and governments toward the intended policy objectives.

4 Tax Transparency in Mining

Transparency has been widely adopted across numerous mining frameworks, and some frameworks such as EITI, Open Contracting Partnership's data standard (OCDS), and IMF Fiscal Transparency Code are dedicated to promoting transparency in the industry. Blank defines tax transparency as the obligation of the government to disclose information on tax rules, rulings, decision-making, and enforcement procedures in tax administration to promote democracy and accountability (Blank 2016). Global Initiative for Tax Transparency (GIFT) defines tax transparency as making information about the tax system available for use by the government and other stakeholders including citizens and minorities to hold the leaders accountable and make informed judgements about the tax system (GIFT 2022). The definitions differ in terms of the actors responsible for providing the information, intended users, and the use of information. This chapter conceptualizes tax transparency as *having open and clear tax processes and policies, and making tax information accessible to all stakeholders, including the public*.

4.1 Forms of Tax Transparency

Tax transparency reporting can be made mandatory through legislation or voluntary. Industry players voluntarily report taxes, Corporate Social Responsibility (CSR), and Environmental, Social and Governance (ESG) activities to build public trust and reputation. Companies like BP have made report on payments made to the government public (BP p.l.c. 2021).

Tax transparency disclosures have been embedded in countries' legislation. Some of the notable tax transparency disclosure reporting standards are the OECD's standards on Exchange of Information on Request and Automatic Exchanges of Information and the implementation by the EU under the 2018 EU Directive on mandatory automatic exchange of tax information which is transposed into law across EU member states (EU 2018; Global Forum 2023). These disclosure requirements aim to counter tax evasion and avoidance by disclosing tax information to and across governments.

The government possesses the capability to access tax information disclosed, but this information may not be accessible to the broader public. The exchange of tax information under bilateral and multilateral conventions provides information only to the government. Some disclosures under legislation also make it mandatory for companies to disclose tax matters to the government, such as disclosure of particular transactions and tax planning arrangements. Transparency disclosures in mining are meant to increase the visibility of tax information so that the public can hold the government accountable and reduce corruption. This requires tax information to be made publicly available. Therefore, it is necessary for the mining sector to have public disclosure of information. Therefore, *this chapter focuses primarily on*

mandatory tax transparency measures to make mining tax information available to the public. The author's idea of tax transparency in mining is having open and clear tax processes and policies, and making tax information accessible to all stakeholders including the public, which is supported by law. This chapter does not cover transparency on revenue management.

4.2 Transparency Measures by International Organizations and Domestic Countries

Transparency is a universally acceptable principle in mining governance by stakeholders including governments, international organizations and initiatives, and the industry. The author explores international and unilateral transparency measures in mining governance.

4.2.1 Transparency Measures by International Organizations

The following paragraphs discuss tax transparency as conceptualized in the mining guidelines of various organizations.

World Bank

The World Banks 1992 Strategy for African Mining sought to accelerate growth of the mining sector by opening up economies to encourage private investment (World Bank 1992b). Among other things, it advocated for transparency as having clear, stable, and predictable economic and regulatory frameworks for the mining sector to stimulate private investment. The mining performed poorly despite many countries in Africa liberalizing their economies to attract foreign investment (Ahrens 2000). The 2002 Evaluation of the World Bank Group's activities in Extractive Industries identified poor governance as a factor contributing to unfavorable mining performance. This led to a shift by the World Bank from supporting reforms to open up economies and encourage private investment to supporting the improvement of governance and development outcomes. The World Bank's 2004 report on the review of its projects in the extractive industry stated that it would fund projects committed to transparency in revenue reporting, to support good governance and sustainable development.

The 2017 Sourcebook for Understanding the Extractive Industries published by the World Bank highlights the importance of good governance principles of transparency and accountability across the entire value chain, from exploration, issuance of licenses, legal and regulatory frameworks, and revenue management. It defines transparency as *the "degree to which information is available to outsiders that*

enables them to have an informed voice in decisions and to assess the decisions made by insiders' (Cameron and Stanley 2017). The information is to be made available throughout the value chain. The Sourcebook makes reference to the information disclosure requirements under the EITI and IMF Guide on Resource Revenue Transparency. It supports transparency requirement for better resource management and as a tool to discourage corrupt practices and reduce information asymmetry between government and mining companies. The Sourcebook notes some of the challenges and concerns associated with public disclosure of information including striking a balance between the interests of the state and investors, pertaining to the exposure of sensitive government strategic activities and companies' commercial interests. However, it underscores the importance of transparency in improving governance of the extractive industry and supports mandatory disclosure requirements for governments and producers to provide information to various stakeholders, multi-stakeholder approach to the transparency process, and participation of countries in international transparency initiatives (Cameron and Stanley 2017).

United Nations

The 2017 United Nations Handbook on Selected Issues for Taxation of the Extractive Industries by Developing Countries provides guidance to governments and policymakers for dealing with specific challenges in tax administration for the mining sector and guides taxpayers in their dealings with tax administrations (UN 2017). It requires clear and comprehensive natural resources laws and refers to EITI and IMF Guide on Resource Revenue Transparency, 2007. It underpins the challenges for developing countries to balance between transparency and confidentiality. The document highlights the importance of transparency in contractual terms, and payments made to the government. It describes transparency as a way to build trust between investors, the government, and local communities (UN 2017).

IMF

Kopits and Craig view transparency as an important element to promote good governance and attain allocative efficiency and macroeconomic stability, though fail to provide concrete evidence for this relationship (Craig and Kopits 1998). Openness involves making information available, in sufficient detail, and having clear process and rules (Craig and Kopits 1998). Fiscal stability ensures openness about government finances, fiscal policies and intentions to the public. They define transparency in the tax area as clearly defined tax laws and rules that do not leave room for discretion.

The IMF highlighted the importance of transparency in the management of natural resources in the IMF Fiscal transparency code, first published in 1998 and complemented by the Manual on Fiscal Transparency (IMF 2002, 2007a). The IMF

Code advocates for comprehensive, reliable, and timely public reporting of public finances, to foster effective fiscal management and accountability for stability of macroeconomic policies and improve confidence in the budget process. The IMF Guide on Resource Revenue Transparency, which was published in 2005, provides detailed guidelines for transparency, specifically for resource revenue. The guide mainly focusses on revenue reporting for non-renewable resources, mainly revenues from oil, gas, and mining activities (IMF 2007b).

The IMF has been providing technical expertise to developing countries on tax issues, including supporting countries in implementing fiscal transparency and conducting voluntary fiscal transparency assessments. Fiscal transparency has also become a condition for countries implementing IMF-supported programs.

EITI

The EITI is a multi-stakeholder initiative constituting of government membership, civil society, and industry players (EITI 2022). The EITI standard is the most influential tool for transparency in extractive industries. Most of the mining frameworks by international organizations and initiatives such as the UN, AMV, IGF, GRI, IMF, and ICMM refer to the EITI transparency standard. EITI has expanded its scope from transparency of government's revenues and payments made by companies to the government in the extractive industry during its inception in 2003, to a more comprehensive EITI Standard lastly updated in 2023 (EITI 2003, 2023a).

The EITI Standard advocates for transparency throughout the extractive industry value chain and provides for public disclosure of the following information by governments and mining companies: contracts and model contracts, beneficial ownership, license data and coordinates, exploration activities, production figures, export data, tax revenues, sales by governments and state-owned enterprises, infrastructure and barter agreements, revenue management, distribution of revenues, subnational transfers, CSR payments, quasi-fiscal expenditures, contribution to the national economy, employment figures on gender, and environmental impact. This information is publicly available. The EITI aims to promote accountability by companies and the government and provides information to inform policymaking and facilitate dialogue among various stakeholders in the extractive industry. In doing so, it seeks to prevent corruption, improve resource management, ensure fair revenue share, and promote sustainable development.

EITI standard is a voluntary initiative which has garnered support from the industry, civil society organizations, and many resource-rich countries, with 57 countries currently implementing the Standard (EITI 2022). The implementation is done through multi-stakeholder committees in each country. National multi-stakeholder committees constitute membership from government departments, civil societies, and extractive companies. The committed countries are required to conduct evaluations and publish transparency reports.

OECD

OECD has been in the forefront to promote international tax transparency under the Global Forum on Transparency and Exchange of Information for Tax Purposes for OECD and non-OECD members, to end bank secrecy and tax evasion.[1] The tax transparency standards cut across all industries including extractive industry. The Global Forum supports the implementation of internationally agreed transparency standards of Exchange of Information on Request and Automatic Exchange of Information. The international tax transparency standards are implemented through the Multilateral Convention on Mutual Administrative Assistance in Tax Matters signed by contracting states, to achieve common goals and objectives.

Members of OECD developed the Common Reporting Standard (CRS) in 2014 to promote automatic exchange of financial information to deal with aggressive tax planning (OECD 2014). The Multilateral Convention on Mutual Administrative Assistance in Tax Matters supports exchange of tax information, including financial information under the CRS, among competent authorities of the countries party to the agreement and has been signed by 147 countries to date, Kenya having signed in November 2020 (OECD 2010). The parties to the convention are required to sign the Convention on Multilateral Competent Authority Agreement on Automatic Exchange of Financial Account Information (CRS MCAA) and Convention on the Exchange of Country-by-Country Reports (CbC MCAA) to agree on the extent of information exchanged and the procedures to be followed (OECD 2014). These disclosure requirements aim to counter tax avoidance and evasion by disclosing tax information to governments and across governments, and are not open to the public.

4.2.2 Unilateral Transparency Measures

Transparency policies in governance of mining revenue have been implemented by various countries around the world both developed and developing nations. Developing countries like Liberia, Ghana, Nigeria, and Tanzania have transparency laws for implementing EITI requirements (Sovacool and Andrews 2015; Ejiogu et al. 2021). A detailed discussion of the cases of Kenya and Tanzania is presented later in this chapter.

Developed nations have yielded to pressure from international initiatives to implement transparency in the extractive industry. The US, EU member countries and Canada introduced mandatory disclosure requirements for payments made by extractive companies to governments around the world. The US introduced Dodd–Frank legislation Section 1502 which requires listed companies to disclose

[1] The Global Forum was restructured in 2009 to implement international transparency standard following G20 declaration to end of banking secrecy in 2009. More information is available at: https://www.oecd.org/tax/transparency/who-we-are/about/. Assessed on 15 January 2024.

and verify the sourcing of conflict minerals;[2] Section 1504 of the legislation introduced the requirement for listed extractive companies to report payments of over US$100,000 to governments on a project basis, so as to provide information to investors and support global efforts to promote transparency in the extractive industry (Security Exchange Commission (SEC) 2010). The payments include taxes, royalties, license fees, dividends, production share, bonuses, and other form of benefits-in-kind. The US Securities Exchange Commission (SEC) issued the implementing rules for Section 1504 on 22 August 2012 which were challenged in court by industry players in 2013, and vacated by court the same year.[3] New rules were issued in 2016 and later disapproved by the US Congress in 2017. The Congress raised concerns mainly on the excessive compliance costs on companies and unfair competition for the US companies compared to foreign companies not subject to similar disclosure requirements (Security Exchange Commission (SEC) 2020). Subsequently, the SEC issued Final implementing rules in 2020 in attempt to address concerns raised and meet its obligations of implementing Section 1504, with first reports expected in 2024 (Grabar et al. 2021). The road to implementation of the section has been marred by obstacles, but is on course more than a decade after its enactment. Other countries have since introduced similar laws. The experience in other countries like Canada and within the EU has been a lot smoother.

Canada's 2014 Extractive Sector Transparency Measures Act (ESTMA) requires disclosure of certain payments of at least US$100,000 made by Canadian extractive entities to governments in Canada and abroad (Government of Canada 2015). The Act focuses on enhancing transparency and imposing reporting obligations on entities engaged in the commercial development of oil, gas, or minerals. The Act outlines different categories of payments to be disclosed, such as taxes, royalties, fees, production entitlements, bonuses, dividends, infrastructure improvement payments, and any other form of payment. The payment is to be broken down on a project basis. The objective is to align with international commitments to fight corruption and enhance transparency in the extractive sector. The information is made available for public access. Canada has so far published data for many extractive companies on government website (Government of Canada 2024).

The EU introduced similar reporting requirements by amending its Accounting (and Transparency) Directive in 2013 (Chap. "Hidden Dynamics and Hierarchies in Tax Policy: A Critical Assessment of Fairness in OECD, EU, and UN"), now adopted by all member states, requiring listed and large extractive and logging companies to report payments above €100,000 made to governments for production

[2] US law on conflict minerals, Section 1502 of the Dodd–Frank Act, passed in 2010 requires public companies to perform due diligence by checking on their supply chains for tin, tantalum, and tungsten from DRC Congo and its neighboring countries to ensure they are not funding conflict. https://www.sec.gov/spotlight/dodd-frank/speccorpdisclosure.shtml. Accessed on 19 June 2023.

[3] US SEC rules to Section 1504 of the Dodd-Frank legislation of 2012 were vacated by court in 2013. New rules of 2016 were disapproved in 2017 by a joint resolution of Congress pursuant to the Congressional Review Act, culminating in the rules of 2020. https://corpgov.law.harvard.edu/2021/01/20/sec-resource-extraction-payments-final-rule/

share, income taxes, production or profits of companies, royalties, dividends, signature, discovery and production bonuses, licence fees, rental fees, entry fees and any payments for licences and/or concessions per project (EU 2013). The intention of the Directive is to make information publicly available and to provide information to civil society to empower them to hold the governments accountable for resource revenues (European Commission 2013). The UK was one of the first movers to implement the EU Directive (UK Government 2014). Many others have followed suit.

The transparency on payments made to government by extractive companies as discussed above, is a form of targeted transparency meant to provide information to empower the public to hold their governments accountable and discourage corruption and mismanagement of funds. However, the extent to which the information disclosure has achieved the intended end goals and outcomes remains unclear. A Post Implementation Review on the reporting of payments in the UK conducted in 2018 did not indicate any significant costs or benefits, citing that it was too a short period time between implementation in 2015 to discern any measurable outcome (Department for Business, Energy and Industrial Strategy and (BEIS) 2018). The reviews conducted measured how the transparency Directive had been interpreted and transposed into law, the number of reports made, and how those reports had been used by civil societies (Chatzivgeri et al. 2020). Just like many other impact assessments, the Post Implementation Review failed to measure how the transparency laws had improved governances and development outcomes in resource-rich nations.

4.2.3 Observations

For each of the transparency guidelines by the different international organizations, there are common elements in terms of the need to make information accessible, and at the same time underlying differences when it comes to the purposes of disclosure, the use of the information, and whether the information disclosed is open or closed to the public.

The OECD and EU support tax transparency disclosures to prevent corporation tax avoidance and evasion. Companies, including extractive companies and business advisors, are obligated to disclose information to governments. This information is not publicly available.

In the 1990s, the World Bank promoted transparency in tax policies and processes by governments to provide certainty and promote foreign private investments in the mining sector. This approach proved ineffective in achieving the intended private sector investments, prompting a transition toward advocating for a commitment to transparent revenue reporting by the government to reduce information asymmetry and corruption in order to support good governance and promote sustainable development. The IMF advocates for public reporting of public finances and open fiscal policies, including government budget processes, to promote good governance and achieve allocative efficiency and macroeconomic stability.

The UN supports transparency in contractual terms and payments made to the government as a way to build trust between investors, the government, and local communities and to manage revenues for sustainable development. The EITI Standard is a multi-stakeholder approach that supports transparency along the mining value chain, including tax transparency, as a way of promoting accountability, providing information to inform policymaking, and facilitating dialogue among various stakeholders in the extractive industry. Companies may voluntarily disclose tax information to build trust and enhance their reputation.

As demonstrated above, it is clear that different international organizations support the notion of tax transparency, although with different interpretations and objectives. While the World Bank initially advocated for transparency to open up economies to foreign investors in mining, the objectives later changed to the promotion of good governance and sustainable development. The latter objectives align with those of the UN and EITI. The IMF objective for tax transparency differs slightly, in that the organization places emphasis on promoting macroeconomic stability. The international organizations support engagement of the public, more so the EITI, whose implementation relies on multi-stakeholder engagements.

The international initiatives are voluntary, but countries can opt to implement them through their legislation, making them mandatory, as has been the case for the US, EU, and Canada, and the implementation of EITI in countries like Tanzania and Nigeria. Countries have different experiences in the implementation. For instance, the US initially experienced hurdles in implementation of Section 1504 on transparency for extractive companies due to a law suit by the industry players on concerns about competitiveness, while Canada experienced a smooth implementation that has made publicly available numerous reports from the extractive companies. The IMF, which provides technical advice and financial support to many developing countries, can exert its influence over the adoption and implementation of transparency policy in developing countries and has effectively done so by making its transparency norms conditions for its support programs.

The practice of concealing critical information through confidentiality clauses in mining contracts is losing relevance, indicating how transparent practices can significantly impact trade and investment dynamics. Transparency has now become a tool to build investors' confidence and promote foreign investment. Transparency has become a fundamental requirement for promoting trust and responsible governance in international trade and investment, making it necessary for trade and investment agreements to conform to international transparency standards.

The discussion reflects the complexity in understanding the nature of transparency in mining frameworks and the specific outcomes that it seeks to achieve. Tax transparency standards in the international context are in a continuous state of change. Implementing countries need to be aware of all this, including the local contextual environment and interaction with trade and investment policies.

5 Implementation of Tax Transparency in Mining in Kenya and Tanzania

Various states across the world have implemented and enacted tax transparency laws to achieve among others accountability, democracy, sustainable development, and curb tax evasion and avoidance. This section explores how tax transparency has been implemented in the mining sectors in Kenya and Tanzania and compares the country experiences. The author investigates the tax transparency, *legal reforms* made to increase public access of tax information, and to have open and clear tax processes and policies, *objectives* of the reforms, and the *implementation*, in both countries.

5.1 Tax Transparency in Tanzania

Mining holds significant economic importance for Tanzania, a developing nation with an estimated population of 61 million in 2022 (United Republic of Tanzania 2022). The country is rich in a variety of mineral resources, including gold, iron ore, nickel, copper, cobalt, silver, diamonds, ruby, garnet, pearl, limestone, soda ash, gypsum, salt, phosphate, coal, uranium, kaolin, titanium, gravel, sand, and stone, and a rare gemstone, tanzanite, found only in Tanzania. The mining sector contributed 7.2 percent of the GDP in 2021 (Tanzania Extractive Industries Transparency Accountability Initiative (TEITI) 2023) and employed about 218,353 people as of 2021 (Tanzania National Bureau of Statistics (NBS) 2021). The number excludes employment in artisanal and small-scale mining which is estimated to be more than 550,000 people (Kinyondo and Huggins 2019).

Tanzania has implemented reforms to improve mining governance. The country developed its first mineral policy in 1997 which was later replaced by the Mineral policy 2009 (Ministry of Energy and Minerals, Tanzania 2009). The aim of the 1997 policy was to attract private investments, streamline artisanal and small-scale mining operations, increase contribution of mining to economic development, and protect the environment. The 2009 Mineral policy builds on this and seeks to attract private investments, integrate mining to the rest of the economy, and establish a fiscal regime that ensures the country gains and at the same time remains internationally competitive, while supporting small-scale mining operations and promoting public participation (Ministry of Energy and Minerals, Tanzania 2009). The Mineral Policy seeks to transform mining sector to contribute to socioeconomic development, by among others creating a transparent and stable macroeconomic environment to promote investment (Ministry of Energy and Minerals, Tanzania 2009), but, offers no additional information regarding the implementation approach.

In order to align with the Mineral Policy, Tanzania joined the EITI to enhance competitiveness within the extractive sector and optimize the gains derived from mining activities (EITI 2023b). Tanzania is an EITI implementing country since

2009 (TEITI 2024). Tanzania enacted the Tanzania Extractive Industries (Transparency and Accountability) Act (TEITA), 2015 to domesticate the EITI (United Republic of Tanzania 2015). TEITA establishes a committee that ensures accountability and transparency in reporting revenue from the extractive industry and publishing mining contracts. TEITI has so far generated 13 reports, each providing comprehensive details on various aspects on mining activities, including production volumes, mining revenues reported by companies, licenses granted, employment figures, export data, and payments made to the government. The Tanzanian government committed to publish mining agreements after joining the EITI and published a roadmap for disclosure in 2021 (TEITI 2021). The government is yet to publish any mining contracts.

The government introduced 2017 Natural Resource Laws to increase control over natural resources (Jacob and Pedersen 2018). One of the Acts is the Natural Wealth and Resources Contracts (Review and Re-Negotiation of Unconscionable Terms) Act 2017 (United Republic of Tanzania 2017) which requires all mining agreements to be tabled before the Parliament, and the Parliament to review all contracts that have unconscionable terms. This establishes a transparent process and allows for contract disclosure and public engagement in mining contractual agreements through parliamentary representatives.

The objective of introducing tax transparency in mining governance in Tanzania is to enhance competitiveness, public participation, increase mining revenue to foster economic development (Ministry of Energy and Minerals, Tanzania 2009; EITI 2023b). Legal reforms have made progress towards achieving these objectives. There is increased public participation through the multi-stakeholder engagements for the implementation of TEITI. Public reporting of data on mining revenues is now available to the public in the TEITI reports. The requirement under the Natural Wealth and Resources Contracts (Review and Re-Negotiation of Unconscionable Terms) Act, 2015, for mining agreements to be tabled before parliament promotes a clear and transparent tax process. The mining contribution to GDP has increased steadily from 4.8 percent in 2017 to 7.2 percent in 2021 (Tanzania Extractive Industries Transparency Accountability Initiative (TEITI) 2023).

However, there are challenges in implementation. The Mineral Policy falls short of providing a clear conceptualization of transparency, its associated objectives, and the specific process for its implementation. An additional hurdle pertains to sluggish progress in enacting pertinent legislation. While the Tanzanian government has expressed its commitment to contract disclosure, full implementation remains incomplete due to the absence of the necessary legislation as stipulated in the 2021 Roadmap (TEITI 2021). It is also unclear whether any mining agreements were tabled before parliament.

Political environment and government commitment influence the implementation and performance of the mining sector. The introduction of the 2017 Natural Resource Laws was done during a political regime that supported resource nationalization (Jacob and Pedersen 2018). The journey toward tax transparency in Tanzania has been marked by notable achievements despite encountering some hurdles along the way.

5.2 Tax Transparency in Kenya

Kenya is endowed with several minerals including soda ash, fluorspar, titanium, gold, manganese, iron ore, gypsum, diatomite, chromite, limestone, and silica sand. Kenya's mining industry currently remains modest in size, but there is potential for more discoveries of rare earth minerals, as highlighted in the Mining and Minerals Policy 2016 (Ministry of Mining 2016). There was discovery of huge coal deposits in the Mui Basin back in 2008 but efforts to develop a power plant have been delayed due to environmental concerns (Coal in Kenya 2019). The country is in early exploration of its mining potential. The Mineral Rights Board reports estimate a mining revenue potential of 12 percent of GDP (Mohammed 2021).

Currently, mining contributes less than one percent of GDP; in 2021 and 2022, mining contributed an average of 0.8 and 0.9 percent of GDP, respectively, and 5 percent of exports in 2021 (Kenya National Bureau of Statistics (KNBS) 2023). Kenya's mineral exports mainly constitute of titanium ore and concentrates, soda ash, salt, diatomite, gold, gemstones, and fluorspar. The national statistics indicated that the mining sector employed about 15,000 people in 2022 (Kenya National Bureau of Statistics (KNBS) 2023); the number does not include people doing informal mining such as artisanal and small-scale mining (ASM). ASM is estimated to employ about 140,000 people country wide (Barreto et al. 2018). The country population is projected to be 52 million people in 2024 (Kenya National Bureau of Statistics (KNBS) 2023). Kenya Vision 2030 aims to harness the potential of mineral resources as a pillar to spur industrial development for sustainable growth and development (Government of Kenya 2008).

Kenya has joined a number of multinational initiatives that promote transparency. It has been a member of the Open Government Partnership (OGP) since 2011, which brings together state and non-state actors in governance. Some of the commitments by Kenya in the 2021–2022 OGP National Action Plan IV are open contracting, increasing access to information by citizens on online platforms, and an open legislative process. Kenya expressed its intention to become a member of the EITI, but is yet to implement it (Gary 2015).

Kenya has a number of laws that promote tax transparency in mining. Article 35 of the Constitution of Kenya 2010, and the Access to Information Act, 2016, grants the general public the right to access information (Government of Kenya 2010, 2016). The country enacted a new Mining Act in 2016 to increase transparency and investors' confidence (Ali 2016). This was followed by several regulations to implement the law and streamline the mining sector regulations. The government, during the same year enacted the seven (7) Mining Regulations to implement the Mining Act: Mining (License and Permit) Regulations, 2017; Mining (Dealings in Minerals) Regulations, 2017; Mining (Work Programmes and Exploration Reports) Guidelines, 2017; Mining (State Participation) Regulations, 20I7; Mining (Use of Local Goods and Services) Regulations, 2017; Mining (Employment and Training) Regulations, 2017; and Mining (Use Of Assets) Regulations, 2017.

The Mining Act 2016 requires that all mineral agreements be made accessible to the public, as per Section 119. The Section 4 of Mining License Regulations, 2017, requires that all applications and granting of licenses to be done through an online mining cadaster, a platform provided by the Ministry of Mining (Government of Kenya 2017a). Non-confidential information on mining rights and dealings on the online platform is to be made open to the public. Kenya maintains a computerized mining cadaster through which mining permits and dealers' licenses are made (Ministry of Petroleum and Mining 2024a). The cadaster contains information on mining licenses granted on the portal but it is not up to date.

Mining (Work Programmes and Exploration Reports) Guidelines, 2017 (Government of Kenya 2017b) requires new applicants and existing mining right holder to submit work programs and exploration to the Director of Geological Surveys. The work program contains descriptions of activities to be carried out under the license including geological mapping, geochemical survey, and a breakdown of the expenditure for the period. The exploration report contains a description of work conducted and a summary of findings, exploration strategy including equipment and assets utilized and staff employed. Regulation 6(3) allows the public to access this information upon payment of a fee. This however is subject to confidentiality requirements in the contracts.

The Mining (Reporting of Mining and Mineral Related Activities) Regulations, 2017 (Government of Kenya 2017c) require mining companies to report on payments made to the government, quantity produced, and sales revenues. The Cabinet Secretary in charge of mining is required to compile report on all payments made to the national and county governments, production volumes, sales revenues of mining rights holders, and licenses granted and mining agreements signed during a reporting year. Regulation 6 requires this information to be published on the Ministry's website. Further, Regulation 7 requires the Cabinet Secretary to publish on its website all mining agreements ratified by the Parliament within 30 days of ratification, including mining agreements signed before the time the Regulations came into force.

Kenya has made significant strides in attaining its objectives of tax transparency. Kenya's OGP National Action Plan IV aims to promote open legislative process, open contracting, and increase access to information by citizens on online platforms (OGP, GoK 2021). The objectives of the overhaul of the mining laws and the new regulations were meant to increase transparency and credibility for the investors (Muigua 2021). The government has always published aggregated mining data in production volumes and revenues in annual Statistical Abstracts and Economic Surveys. The online cadaster allows for application and renewal of new licenses online (Ministry of Petroleum and Mining 2024b).

The country has also experienced some hurdles in legal reforms to improve transparency in mining. Just like the case for Tanzania, Kenya policies fail to provide concise conceptualization of tax transparency as introduced in the various laws. There are also implementation gaps in publishing of mining contracts. Kenya's mining contribution to GDP has remained almost constant between 0.7 and 0.8

during the last 5 years (Kenya National Bureau of Statistics (KNBS) 2023), despite the legal reforms in place to promote tax transparency to increase investors' confidence. The Government has also been accused of cancelling mining licenses thus creating uncertain operation environment (Business Daily 2015; Simiyu 2023). Political environment has influenced the implementation and performance of the mining sector, including the issuance of licenses.

5.3 Discussion of Country Experiences

Kenya and Tanzania have embraced tax transparency as a way to increase accessibility of information to promote public participation, increase investors' confidence thereby enhancing mining gains for socioeconomic development (Ministry of Energy and Minerals, Tanzania 2009; OGP, GoK 2021; Muigua 2021). The efficacy of tax transparency initiatives hinges on the realization of the desired objectives. Both countries have made strides toward achieving the objectives. However, the author notes that tax transparency is not clearly conceptualized in legal instruments. The objectives and process of implementation have not been clearly defined.

In Tanzania, TEITA is the main law that legislates tax transparency. In Kenya, various legal provisions within the Parliament Acts contain transparency provisions. Both countries have continuously improved their laws to comply with international standards. It is evident that Tanzania's mining sector experienced tremendous growth compared to the Kenya mining sector, whose performance has stagnated in the past few years. The author notes that, the improvements in mining performance in Tanzania is not entirely attributable to transparency laws due to the difficulties in isolating the specific impact of transparency from other variables influencing the mining performance. While both Tanzania and Kenya are both members of the Global Forum, Kenya signed the Mutual Administrative Assistance Convention in 2020 but Tanzania is yet to sign. This means that Kenya is able to exchange tax information with the other 147 participating countries to the Convention, though such tax disclosures are not available for public scrutiny, hence may have little impact on resource governance outcomes.

The transparency requirements are mandatory and cover payments made by companies to governments, without providing a minimum threshold. There is no standardized format to report the payments. The governments have the power to verify information disclosed. Companies are not required to report on a project basis, unlike the US and EU transparency laws. The transparency requirements in Kenya and Tanzania go beyond reporting payments to having open processes and procedures and making mining contracts public. However, there is a deficiency in the implementation and enforcement of these laws.

Both countries have experienced implementation gaps. Despite Kenya expressing its intention to become a member of the EITI, it has not yet taken the necessary

steps to formalize its membership. Additionally, neither country disclosed any mining agreements. The users of information, mainly the general public and civil society require to be empowered to interpret and use the information for intended purposes, a capacity that is currently lacking. There have been no monitoring reports to assess the extent to which the reforms achieved their intended objectives, giving the impression that the transparency laws are merely a checkbox exercise.

The implementation gaps could be explained by the culture or resistance of established institutions to change. Sociological institutionalism emphasizes the role of social norms, beliefs, and practices in shaping behavior within institutions (Hall and Taylor 1996). Thus, established norms and practices within a society or organization may lead to sluggish implementation of new laws, especially if they challenge the status quo. If a new law requires greater transparency in government but the prevailing norm is to keep information confidential, there may be resistance from within the institution to adopt the new law's provisions. Policymakers should be aware of social norms, culture, and values to overcome the inertia of sluggish implementation and drive meaningful changes in institutions.

Political will and commitment also play a role in the adoption and implementation of new policies, as seen in the case of Tanzania's political regime leaning toward the nationalization of resources. Therefore, it is paramount for countries to consider their social, economic, and political contexts when adopting and implementing transparency norms. Finally, legal instruments should provide a clear conceptualization of tax transparency, the objectives and motivation driving the adoption of the tax transparency principle, and the implementation process. The objectives provide clear measures against which implemented norms can be evaluated.

6 Conclusion

This chapter has explored the nature of tax transparency, its implementation and implications for mining governance. The chapter has explored the various forms of transparency measures by international institutions and domestic countries and has presented the experiences in Tanzania and Kenya, highlighting both the successes and challenges in the implementation of tax transparency measures.

Tax transparency involves having open and clear tax processes and policies, and making tax information accessible to all stakeholders including the public. An effective tax transparency policy is instituted within the law with clearly defined policy objectives and scope, with room for feedback and improvement. The platform of information disclosure should be identified whether it is a physical document, online form, or website, and information disclosed should be accurate, comprehensive, and verifiable. The users of information should be able to interpret and use the information in decision-making for intended purposes, leading to behavioral change of the disclosers and governments toward the intended policy objectives.

Tanzania's commitment to tax transparency, as reflected in its legislative reforms and the disclosure of mining data, has fostered openness and accountability in the extractive sector. However, challenges, such as delayed legislative enactments and non-disclosure of mining agreements, underscore the need for continued efforts to fully realize the potential benefits of tax transparency. In Kenya, the implementation of legal reforms to incorporate tax transparency requirements and the intention to join the EITI and disclose mining agreements signifies a step toward increased transparency. Nevertheless, slow progress in actualizing the latter highlights the complexities inherent in institutional change and the influence of social and political factors on implementation. In both cases, it is evident that tax transparency is important for enhancing mining governance, but having a concise transparency conceptualization and clear goals that are relevant to the social, economic, and political context is pivotal for successful implementation, which is lacking in both countries. Government commitment is a crucial component in driving tax transparency initiatives in mining governance to achieve the desired outcomes.

Country and international experiences reveal the acceptability of transparency standards as a global norm, and at the same time the challenges in implementing impactful transparency policies. Measuring the extent to which transparency attains improved governance outcomes remains a daunting task, since transparency is just one of the many factors that influence governance outcomes. Transparency also interacts with other contextual factors like the policy environment, social, economic, and political conditions, making policy outcomes unpredictable. The integration of transparency policies with broader governance strategies and contextual environment then becomes instrumental in enhancing accountability, curbing corruption, and improving resource governance. A holistic approach that aligns transparency policies with trade, investment, and overarching governance objectives is crucial for fostering positive governance outcomes.

The journey toward tax transparency is ongoing, marked by achievements and challenges. The lessons learned from these experiences provide valuable insights for policymakers, stakeholders, and scholars engaged in the ongoing pursuit of transparent and accountable governance in and beyond the extractive sector.

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Part III
Interactions and Overlaps Between Tax, Trade, and Investment Policies

Introduction to Part III

Frederik Heitmüller

The chapters in this part deal with overlaps of the policy areas of tax, trade, and investment. Complementing the focus on interactions at the governance level adopted in Part I of this book, the chapters in this part focus on individual cases to show how interlinkages between the different areas play out within specific international agreements and in cases heard by investment tribunals.

In Chap. 12 "The Interaction Between IIAs and DTCs: Potential for Overlap and Reform Proposals," Javier Garcia Olmedo discusses four recent investor-state dispute settlement (ISDS) cases in which tax measures were disputed. He focusses on whether investment arbitration tribunals found that they had jurisdiction to judge the matter or whether they deferred to a double tax convention (DTC). He shows that investors have increasingly sought to litigate tax issues through ISDS, presumably due to the higher protection for investors that investment treaties offer. The outcomes of these cases are mixed. In some, the investment tribunal found indeed that it did not have jurisdiction or that the matter was subject to a DTC rather than an investment agreement. In others, they upheld the claim of the investor.

From a policy perspective, this type of interaction can lead to a waste of administrative resources if the same subject matter is discussed in different venues at the same time (i.e., DTC dispute settlement provisions as well as ISDS). From the perspective of the government, the impact that investment treaties can have on tax policy may often have been unintended, at least by those departments that are responsible for tax policy.

Compatibility clauses, such as tax-carve out clauses in investment treaties, are a possible solution. These have become prevalent in more recently signed investment agreements. However, as Olmedo discusses, not all of these agreements clarify who

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should interpret such clauses, which means that in practice the question of jurisdiction is answered by the investment tribunal itself.

In Chap. 13 "The Intersection of Treaties on Tax and Trade: A Case Study of Australia and India," Sunita Jogarajan and Tania Voon analyze a unique trade discussion between India and Australia in which a tax measure is the subject matter. Following demands by Indian businesses, the Indian government convinced its Australian counterpart to sign a side letter to the recently concluded Australia–India Economic Cooperation and Trade Agreement, in which Australia committed to suspend its withholding tax on fees for technical services paid to service providers resident in India. The case is striking because the question of whether a withholding tax on fees for technical services may be levied is always one of the key negotiated matters in DTCs. Hence, the trade-based side agreement overrides the provision of the DTC between India and Australia, which allows any of the two states to levy a withholding tax on technical services. This peculiar arrangement is likely due to the fact that allowing a withholding tax under tax treaties has been a long-standing and consistently defended policy of India. It is likely that the Indian government would not have wanted to create a precedent by renegotiating the DTC with Australia. Moreover, the unilateral concession by Australia has more advantages for India than an amendment of the DTC, as the latter would have likely been reciprocal and thus would have prevented India from levying withholding tax on payments to Australian service providers.

The authors further analyze whether the Australia's agreement to remove withholding tax on payments to India is consistent with Australia's World Trade Organization (WTO) obligations, notably the General Agreement on Trade in Services (GATS). They find that even though Australia could possibly defend itself on grounds of economic integration, there is a risk that third countries may challenge the preferential treatment that Australia grants to Indian service providers.

In Chap. 14 "The Legal Transplant of EU Standards in Taxation: A Case Study of the ACP Post-Cotonou Agreement," Irma Mosquera Valderrama and Filip Debelva discuss the Post-Cotonou Agreement, a partnership agreement between the EU and African, Caribbean, and Pacific (ACP) countries. This agreement deals with tax, trade, and investment matters, even though these issues may have already been regulated in more specific agreements. The authors focus on one particular provision, namely the "EU Standard of Tax Good Governance." This Standard refers mainly to policy standards developed by the Organization for Economic Co-operation and Development. The authors argue that the inclusion of the Standard in the Post-Cotonou agreement is an attempt by the EU to export norms to third countries and could therefore result in a legal transplant. The significance of such a transplant is critically discussed by the authors who highlight that some of the principles and policy goals included in the agreement are incompatible with each other and that compliance with some of its aspects would require far-reaching policy reforms by the countries concluding the Post-Cotonou agreement. Hence, they may not have any effect in practice, as the more specific provisions of tax, trade, or investment agreements remain in place.

The overlaps described in the chapters in this Part are not uniform. Rather, one can note different degrees of "encroachment" of one policy area upon another: The tax provisions contained in the Post-Cotonou agreement are largely open norms which are unlikely to conflict with the specific provisions of double tax conventions. The cases discussed in Garcia Olmedo's chapter are more challenging. Some of the tax-related investment disputes surveyed deal with matters that are outside the immediate ambit of DTCs. Some of them also involve cases in which no DTC applies, for instance because the immediate entity undertaking the transaction was situated in a low-tax jurisdiction. However, some may clearly overlap. Finally, the Australia-India trade agreement provision discussed by Voon and Jogarajan is arguably the clearest case of an overlapping claim to govern an issue, as withholding tax on services are specifically dealt with under DTCs.

What is the way forward to address such overlaps and interactions? Countries could contemplate entering into comprehensive agreements covering all three issues in a coherent way rather than negotiating area-specific agreements. Nevertheless, there may be good reasons why, for instance, countries want to enter into a trade agreement but not a DTC with certain countries. Overlaps could also be addressed through administrative approaches. Over the last decade, the idea of "policy coherence" has gained increasing traction and is mentioned in the United Nations Sustainable Development Goals. Some countries have created specific institutions or started processes to review their policy processes for coherence among each other. The hope is that different government departments would be encouraged to enter into dialogues about the respective policies promoted. Such initiatives can be a productive way forward, but increasing the coherence of a country's tax, trade, and investment policies with each other should not be the end point. Indeed, the concept of "policy coherence" can be used in different ways: On the one hand, it can refer to policy coherence within one country to make sure that different arms of the government go in the same direction and do not undermine each other. On the other hand, it can refer to the objective that a country's policies should not undermine the globally shared goal of fostering global development in a cooperative way. For example, a country may adopt tax, trade, and investment policies that are internally coherent with each other. But if these are all based on a zero-sum competition with other countries, they would fail the test of coherence with this overarching ideal. Creating policies that are internally coherent and compatible with overarching global objectives is arguably the next policy frontier.

The Interaction Between IIAs and DTCs: Potential for Overlap and Reform Proposals

Javier García Olmedo

1 Introduction

International tax law and international investment law are two of the fastest growing areas of international economic law. The international tax law regime is governed by more than 3600 double taxation conventions (DTCs or tax treaties), most of which are based on the Organisation for Economic Cooperation and Development (OECD) Model Tax Convention (Kobetsky 2011 and Model Tax Convention 2019). These treaties 'serve several goals, including anti-double taxation of cross-border investment, prevention of excessive taxation, avoidance of tax evasion, cooperation in tax administration, and the exchange of information' (Chaisse ICTSD 2016a). DTCs do not provide taxpayers with direct access to dispute resolution. Instead, tax treaty disputes are predominantly resolved through the (purely intergovernmental) Mutual Agreement Procedure (MAP). The MAP is administered by the competent tax authorities of the Contracting Parties to the applicable DTC with the aim of avoiding or mitigating double taxation for taxpayers. Despite being of vital importance for taxpayers since it guarantees the proper application and interpretation of DTCs, the MAP has suffered from well-known criticism over the last few years. It has been criticised for not always ensuring a satisfactory and timely resolution of the dispute and for failing to grant taxpayers participation rights (Chaisse 2016b; Dourado 2019; Perrou 2019).

For its part, the international investment law regime is governed by over 3000 international investment agreements (IIAs or investment treaties), including bilateral investment treaties (BITs), free trade agreements (FTAs), and multilateral investment agreements, which aim to promote foreign direct investment (Salacuse

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2021). These treaties provide investors with an unprecedented level of substantive and procedural protections but offer no reciprocal rights for states wishing to preserve regulatory space (Dumberry 2016). Unlike DTCs, IIAs contain investor-state dispute settlement (ISDS) clauses, which allow investors to directly challenge policy measures that may affect their investments before arbitral tribunals and claim for high compensation amounts. This regime is also facing a legitimacy crisis that has spread across the globe, prompting several states to denounce investment treaties or to exclude ISDS provisions from these agreements (Dietz et al. 2019; Waibel et al. 2010). Critics argue that the regime unduly restricts host states' regulatory policy space, cannot guarantee arbitrators' independence and impartiality, fails to ensure consistency between decisions, lacks transparency and leads to overly long and expensive proceedings (Giorgetti et al. 2020; Arato et al. 2020; Henckels 2016).

Concerns have also been raised with respect to the interplay between DTCs and IIAs. Investment treaties do not generally exclude taxation from their scope of application, meaning that they can cover tax measures aimed to raise revenue, eliminate double taxation or limit opportunities to engage in tax avoidance or evasion. Investors have brought tax-based ISDS claims in an increasing number of cases given the limits and shortcomings of the MAP. These claims can overlap with the subject matter covered by DTCs, creating uncertainties for tax and investment policymakers. This chapter examines selected cases in which tribunals have examined the relation between IIAs and DTCs. These cases include *Cairn v India*, *ConocoPhillips v Vietnam*, *Schooner v Poland*, and *Lone Star v Korea.* It will then make suggestions in the form of treaty drafting approaches that states can adopt in their IIAs to regulate possible conflicts between the two regimes.

2 Case Law

As O'Brien and Brooks explain, '[t]ax treaties and IIAs have much in common' (O'Brien and Brooks 2012 at 303). These instruments 'share the same purpose of facilitating FDI, […] provide similar legal protections, such as prohibition of discriminatory treatment of non-nationals [and] are intended to create security and predictability' for investors (O'Brien and Brooks 2012 at 304). IIAs offer, however, a larger scope of protection for investment than DTCs (Ortino 2015). As mentioned in the Introduction, tax treaties do not provide investors/taxpayers with direct access to dispute resolution and only deal with the allocation of taxing rights between Contracting Parties over certain types of income and capital gains. Investment treaties offer expansive substantive protections in respect of investments that generate that income and enable investors/taxpayers to bring direct claims against host states.

Moreover, most IIAs do not exclude taxation from their scope of application and are silent on their relationship with DTCs (UNCTAD 2021). This means that investors can be protected from tax-related measures adopted by host states that violate the IIA's substantive protections, including measures that 'may simultaneously fall within the scope of a DTC as well as an IIA between the relevant countries'

(UNCTAD 2021 at 16). More recent investment treaties contain tax carve-out provisions, which exclude tax measures from all or certain investment protection standards and attempt to prevent inconsistencies relating to a taxation measure between IIAs and DTCs (Davie 2015). However, these treaties do not generally define what is meant by 'taxation measure', nor do they explain who (investment tribunal or domestic tax authorities) should solve potential inconsistencies.

The better protection offered by IIAs has resulted in a multiplication of tax disputes before investment treaty tribunals. According to UNCTAD, between 1987 and 2021, 'investors have challenged tax-related measures in 165 ISDS cases based on IIAs' (UNCTAD 2021 at 5). These cases involve different measures, including regulatory changes to feed-in tariffs for renewable energy production, withdrawal of VAT subsidies, increase in windfall profit taxes and royalties, the initiation of tax investigations or audits, and the imposition of capital gain taxes (Tandon 2022; Ranjan 2022; Rolland 2020). The cases discussed below show how ISDS claims involving domestic tax policies have the potential to overlap with the subject matter covered by DTCs.

2.1 Cairn v India

An illustrative and recent example is the *Cairn v. India* case. This case arose out of India's decision to retrospectively amend its income tax laws and impose a tax liability of USD 1.6 billion on Cairn India Ltd. for its failure to deduct withholding tax on capital gains resulting from a series of restructuring transactions that took place among the Cairn group in 2006. Cairn UK initiated UNCITRAL arbitration proceedings under the UK-India BIT, claiming that India's measures leading to the imposition of the retroactive tax breached, among others, its obligation to accord Cairn UK and its investment fair and equitable treatment (*Cairn v. India*, Award, 2020).

India made several jurisdictional objections, including that challenges to its 'tax legislation and policy are excluded from the scope of the BIT and are not arbitrable':

> tax disputes are not capable of being resolved by arbitration under the BIT in light of an implied exception to the scope of application of the BIT, and of the fact that the Respondent and the United Kingdom have in fact specifically agreed that tax disputes should be settled in accordance with the procedure prescribed in the contemporaneous [double taxation avoidance agreements] (at para 764).

India relied, in this respect, on the UK-India DTC, 'which does not provide for arbitration, but rather for a mutual agreement procedure involving consultations between the taxation authorities of the two States' (at para 771). According to India, 'the advancement of [tax] claims under the BIT is incompatible with the [DTC], in which the Respondent and the UK seek to ensure the "avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and capital gains' (at para 773). In other words, since the measures adopted by India are

regulated by the DTC, "the BIT should be read so as to exclude such matters from its scope" (at para 801). The absence of a tax carve-out in the BIT defining the relationship between this treaty and the DTC did not alter this conclusion, India added, 'because at issue here is the existence of general limits to the scope of protection of investment treaties which exist even if they are not made explicit' (at para 767). Cairn UK should have, therefore, resorted to the MAP provided in the DTC, instead of challenging India's tax measures under the BIT.

The Tribunal disagreed with India. It observed that the UK-India DTC and the UK-India BIT 'govern different subject-matters' and that the BIT 'does not expressly specify that [it] should be considered to be incompatible with' the DTC (at paras 803–806). The Tribunal noted, in this respect, that, unlike the ISDS provision in the BIT, the MAP 'does not purport to provide a dispute resolution mechanism for situations in which an investor of one of the Contracting States considers that the host State has violated his rights as an investor' (at para 803). The Tribunal further found that the BIT did not contain a provision preventing the investor from submitting arbitration claims relating to tax measures that can potentially fall within the scope of the DTC. The Tribunal upheld jurisdiction over the dispute and held that India had failed to respect its obligations under the BIT, in particular, the Fair and Equitable (FET) standard (at paras 256–509). India was ordered to pay Cairn UK over USD 1.2 billion in compensation and challenged the award before the courts of the seat of the arbitration, the Hague. In a decision of 31 December 2021, the Hague Court of Appeal decided to set aside the award given that Cairn UK did not appear in the proceedings, presumably in response to India's decision to withdraw its retroactive tax bill (Bohmer 2020).

2.2 ConocoPhillips v Vietnam

The *ConocoPhillips v Vietnam* case is another example of how investment treaty protection can conflict with rights and obligations under DTCs. This case also relates to capital gains tax on restructuring of assets. In 2012, ConocoPhillips UK (a UK subsidiary of the US energy giant ConocoPhillips) sold two of its entities (ConocoPhillips Gama Limited and ConocoPhillips Cuu Long) to UK-based Perenco Overseas Holdings. The only assets held by ConocoPhillips Gama and Cuu Long were ConocoPhillips's oil interests in Vietnam. It was reported that ConocoPhillips sold the companies for USD 1.29 billion, making a profit of USD 896 million (Turner 2018; Alencar and Neck 2020).

Under the terms of the UK-Vietnam DTC, 'capital gains generated from transactions involving shares deriving their value from immovable property situated in one of the contracting states may be taxed in the jurisdiction where the property is located' (Alencar and Neck 2020 at 16). The Vietnamese tax administration interpreted the DTC as granting the state the right to tax capital gains on the transaction since it derived its value exclusively from oil interests located in Vietnam. Based on the current tax rate in Vietnam, ConocoPhillips would have to pay an estimated

USD 179 million to the Vietnamese government for its capital gain. ConocoPhillips refused to pay this tax, arguing that the sale was between two UK entities with no taxable presence in Vietnam.

In 2015, Vietnam signalled its intention to tax the transaction. In a move designed to prevent the Vietnamese government from collecting the capital gains tax, ConocoPhillips and Perenco initiated UNCITRAL arbitration proceedings against Vietnam under the UK-Vietnam BIT. On 20 January 2020, the journal *Finance* Uncovered reported that ConocoPhillips has settled the case with the government, noting that 'the US oil giant, has finally paid tax to Vietnam on a $896m gain from the sale of two oil fields in 2012—marking a significant climbdown amid embarrassing legal action and international critic' (Mathiason 2020). Although the settlement of the dispute has been confirmed, the exact terms of the settlement remain undisclosed.

Had the dispute proceeded, Vietnam would have likely raised a jurisdictional objection on grounds like those invoked in *Cairns v India*, arguing that any disagreement between Vietnam and ConocoPhillips as to the payment of the capital gains tax should have been resolved through the UK-Vietnam DTC. It is also probable that tribunal would have rejected the objection on the basis that the UK-Vietnam BIT does not require that investors resort to the DTC to challenge tax-related measures.

2.3 Schooner v Poland

Another case worth mentioning is *Schooner v. Poland*. This case involved a BIT claim arising out of an investment made by two US companies in the mid-1990s in a newly privatised Polish state enterprise, Kama Foods, an oil and margarine manufacturer. For fiscal years 1994 to 1997, Kama Foods recorded the payment of management fees, training and know-how as tax-deductible for tax assessment purposes. As a result of a series of inspections conducted in 1997, the Polish tax authorities took a series of tax enforcement measures that disallowed certain deductions that had been taken by Kama Foods, leading the company to become insolvent.

On 31 March 2011, the investors instituted arbitration proceedings under the ICSID Additional Facility Rules pursuant to the US-Poland BIT. The investors argued that, through its tax measures, Poland had violated the expropriation, FET and full protection and protection standards (FPS) of the Poland-US BIT as well as its provisions relating to the free transfers of investments. Poland raised several jurisdictional objections. In particular, Poland argued that 'the entire Tax Claim is covered by the tax exception provided in Article VI of the Treaty read in conjunction with Article 22 of the Poland—United States Double Tax Treaty ("DTT") and is, therefore, outside the jurisdiction of this Tribunal' (*Schooner v. Poland*, Award, 2015 at para 179). Article VI of the BIT is a tax carve-out provision which reads as follows:

> 1. With respect to its tax policies, each Party should strive to accord fairness and equity in the treatment of, and commercial activity conducted by, nationals and companies of the other Party.
>
> 2. Nevertheless the provisions of this Treaty, and in particular Article IX and X, shall apply to matters of taxation only with respect to the following:
>
> (a) expropriation, pursuant to Article VII;
>
> (b) transfers, pursuant to Article V; or
>
> (c) the observance and enforcement of terms of an investment agreement or authorization as referred to in Article IX(1)(a) or (b),
>
> to the extent that they are not subject to the dispute settlement provisions of a convention for the avoidance of double taxation between the two Parties, or have been raised under such settlement provisions and are not resolved within reasonable period of time (at para 209).

Poland first argued that 'the phrase "matters of taxation" in Article VI(2) should be defined broadly as referring to all issues related to the process or system of imposing and charging taxes' (at para 211). As such, according to Poland, the Tribunal did not have jurisdiction over the claimants' FET and FPS claims since the tax measures adopted by the state fell within the ambit of that provision. The Tribunal majority agreed, holding that 'matters of taxation' include the 'assessment and collection of taxes', which is the type of measure that triggered the claimants' BIT claims (at para 284).

Second, Poland argued that the Tribunal did not have jurisdiction over the claimants' remaining claims, expropriation and denial of free transfer, 'because the Claimants did not resort to the "dispute settlement provisions of a convention for the avoidance of double taxation" before initiating this arbitration as required under Article VI(2) of the BIT' (at para 290). Article 22 of the Poland-US DTC provides for the MAP. According to the Respondent, 'the central part of the present dispute [was] the application of income tax laws which is covered under the DTC' and thus the claims fell 'within the ambit of the mutual agreement procedure' (at para 294). More concretely, Poland pointed out that the dispute was covered under Articles 8, 11, 13, and 15 of the DTC (at para 314).

The Tribunal noted that 'the central issue in this case relates to deductibility of [management] costs for the purposes of calculating corporate income tax and the DTC is applicable to income tax' (at para 313). Despite this, after examining the DTC provisions relied upon by Poland, the Tribunal found that the dispute was not subject to the MAP. With respect to Articles 8 of the DTC, the Tribunal observed that this provision 'deals with business profits and sub-article (3) provides that in determining the profits of a business, deductions for expenses incurred for the purposes of the business shall be allowed' (at para 315). The Tribunal held that this provision was not relevant in that case at hand since, according to the 'Respondent's own formulation', the dispute was 'not whether Management Services were in fact provided, but whether [the claimants] adequately documented the provision of the Management Services for the purposes of claiming deductions' (at para 315). With respect to Article 13 of the DTC, which relates to royalties, the Tribunal found that 'there is no issue of royalties being paid to or by anyone in this case and therefore,

Article 13 of the DTC has no application to the present dispute' (at para 316). As to the Tribunal's position on Article 15 of the DTC, which deals with the taxation of income derived from the provision of services, such as management services, the Tribunal found the dispute did not concern this issue but rather 'the treatment of the expenses incurred by [the claimants] in paying for the Management Services' (at para 317).

Finally, the Tribunal decided that 'the Claimants' claim that their freedom to transfer funds was violated because they could not freely transfer the Management Fees [was] very different from the taxation of dividends covered under Article 11' and thus that provision was not applicable either (at para 319).

Based on the above analysis, the Tribunal held that it only had jurisdiction to hear the claimants' claims based on expropriation and transfers of funds pursuant to Article VI(2) of the BIT. On the merits, however, the Tribunal decided that both claims had failed, and the claimants were, consequently, not entitled to any damages. The investors have unsuccessfully tried to set aside the award at the seat of the arbitration, Paris (Charlotin 2022).

2.4 Lone Star v Korea

The last case worth discussing is *Lone Star v. Korea*, one of the latest investment awards in tax-related investment treaty disputes. In that case, the relation between the IIA and the DTC between Belgium and Korea was at issue. The issue before the tribunal concerned the application by Korea of its 'substance Over Form Principle' which resulted in the denial of tax treaty benefits under the Korea-Belgium DTC by disregarding companies incorporated and resident of Belgium in relation to capital gains. The tribunal did not consider that, as argued by Korea, the Belgian investment companies—the legal owners—had no standing simply on the basis that they had been disregarded pursuant to the substance over form principle: 'to do so would be to assume in favor of the Respondent an important point in issue, namely whether the Respondent adopted the *correct tax treatment*' (*Lone Star v. Korea*, Award, 2022 at para 366).

Although the tribunal held that it had no jurisdiction under the DTC, this did not prevent it from discussing the interaction between the substance over form principle and Korea's tax treaty obligations from the ambit of the arbitration (at paras 296 and 372). The tribunal examined whether the application of the substance over form principle by Korean tax authorities and courts was in conformity with the substantive standards of the IIA (at para 390). Relying extensively on the OECD Model Commentaries, the tribunal concluded that:

> The Tribunal concludes that Korea's application of the Substance Over Form doctrine did not violate the BIT because, as referenced by Dr.—the doctrine forms 'part of the basic rules for determining the facts that give rise to tax liability'. It is only after the facts have been determined that the tax consequences are assessed, and it is only at the tax consequence stage, not the earlier fact-determination stage, that the Treaty provisions come into

> play. Here the judicial proceedings initiated by the Lone Star companies resulted in a rejection in the relevant cases of Lone Star's ·version of facts. The Korean courts adequately explained why the application of Substance Over Form was not arbitrary but grounded in the evidence. Nor, in the opinion of the Tribunal, as will be discussed, was the application discriminatory (at para 410).

In the same vein:

> In the absence of any claim of denial of justice, the Claimants have not established any violation of the 2011 BIT in respect of the post-27 March 2011 tax treatment of their investments. Their various arguments based on Substance Over Form were properly analysed by the Korean courts to whom the Claimants had remitted the questions and the Claimants' objections were rejected for reasons with which the Tribunal agrees. In other words, in the Tribunal's view, the tax treatment violated neither national nor international standards and as such there is no wrongful act capable of supporting the Claimants' arguments on expropriation, Full Protection and Security, the Umbrella Clause, or the provision for Free Transfers. The Respondent acted well within the legal boundaries of internationally-accepted tax policy (at para 469).

As Danon notes, 'the *Lone Star* award has underscored the relevance of the Model Commentaries, as a matter of principle, for purposes of determining whether a domestic rule affecting the eligibility of an investor to tax treaty benefits is applied in conformity with the substantive standards of protection contained in an IIA' (Danon 2022 at 230).

3 Reform Options

These four cases illustrate how the investment and tax treaty regimes have the potential to interact and overlap. With the support of arbitral jurisprudence, and in the absence of a clear definition regarding the relationship between IIAs and DTCs, disputes arising from tax-related measures can fall within the scope of both treaty regimes. This can lead to the parallel use of the dispute settlement mechanisms offered in each field to resolve disputes arising out of the same measure. As UNCTAD explains:

> Potentially, a taxpayer could request the relevant competent authority for a mutual agreement procedure (MAP) and, concurrently or afterwards, pursue ISDS claims as an investor under an IIA concerning the same matter. A MAP between the competent authorities of the contracting parties or a State-State tax arbitration could be ongoing when an ISDS proceeding is initiated. The outcome of a MAP, tax arbitration or tax litigation could also give rise to ISDS cases (UNCTAD 2021 at 17).

In other words, the proliferation of overlapping and uncoordinated mechanisms to resolve tax disputes in the international plane has resulted in further fragmentation. This demonstrates, as Chaisse aptly observes, that 'there is a need for better designed international rules and policies on tax and investment, which would allow the tax and investment worlds to move from mere coexistence to cooperation' (Chaisse 2016b).

States are responding to the increasing volume of ISDS claims involving tax measures by amending investment treaty provisions. Preserving tax policy autonomy and coordinating investment and tax disputes settlement mechanisms have become an important matter for treaty negotiators. As compared to old-generation IIAs, more recent treaties contain tax carve-out provisions that aim to completely exclude tax measures from their scope of application and to avoid overlap between IIAs and the subject matters covered by DTCs. The 2016 India Model, for instance, states that the treaty shall not apply to 'any law or measure regarding taxation, including measures taken to enforce taxation obligations' (India Model BIT 2016 Art 2.4). This article further provides that a host state's decision that a particular regulatory measure is related to taxation, whether made before or after the commencement of arbitral proceedings, 'shall be non-justiciable and it shall not be open to any arbitration tribunal to review such decision' (India Model BIT 2016 Art 2.4). As Ranjan notes, 'it is evident that India has decided to keep taxation measures outside the purview of the BIT in response to Vodafone and Cairn challenging India's retrospective application of taxation law under different BITs' (Ranjan et al. 2018).

The new 2018 Dutch model BIT mostly aims at avoiding conflicts with DTCs. Article 10(3) provides that '[t]his Agreement does not affect the rights and obligations of a Party under an agreement for the avoidance of double taxation. In the event of inconsistency between such agreement and this Agreement, the agreement for the avoidance of double taxation prevails to the extent of the inconsistency' (Dutch Model BIT 2019 Art 10.3). This clause, however, does not clarify how and by whom (ISDS tribunal or domestic tax authorities) inconsistencies should be settled. This means that, as occurred in *Schooner v. Poland*, it would be for the ISDS tribunal to determine whether there is a conflict between the IIA and the DTC. The position of the tribunal regarding a potential conflict between the two regimes may be different from that adopted under domestic law.

Only a few IIAs, such as Article 14 of the Chile-Hong Kong BIT, contain a provision specifying that any determination as to the existence of an inconsistency between a DTC and an IIA shall be settled by the competent (tax) authorities of the contracting parties. This provision provides that:

> In case an issue arises as to whether any inconsistency exists between this Agreement and a tax convention between the Parties, the issue shall be referred to the designated authorities. If the designated authorities decide to make a determination as to the existence and extent of any inconsistency, they shall do so within six months of the referral of the issue. No procedures concerning the measure giving rise to the issue may be initiated under Section D (Settlement of Disputes between the Parties) or Article 21 (Submission of a Claim to Arbitration) until the expiry of the six-month period. An arbitral panel or tribunal established to consider a dispute related to a taxation measure shall accept as binding a determination of the designated authorities made under this paragraph. If the designated authorities have not determined the issue within six months from the date of the referral, the tribunal or arbitral panel shall decide the issue (Chile-Hong Kong BIT 2019 Art 14.4).

The Chile-Hong Kong BIT indeed gives a greater role to host states on taxation claims. This treaty, however, does not address a possible scenario where the

competent tax authorities do not reach an agreement within the deadline established in the treaty, leaving that decision to the tribunal. That outcome may differ from the one of the competent tax authorities if the same claim is brought under a DTC.

4 Conclusion

This paper has explored the extent to which ISDS claims involving domestic tax policies have the potential to overlap with the subject matter covered by DTCs and MAPs. The cases examined therein illustrate such potential for interaction. The paper has also proposed reforms options that states can adopt in their IIAs to regulate possible conflicts between the two regimes. Investment treaties that contain tax-carve out provisions, however, only represent the minority of the vast IIA universe. Most IIAs do not address tax issues and are silent on the relationship between their scope of protection and the subject matter covered by DTCs and MAPs. In the absence of a consistent and coherent treatment of fiscal matters in tax and investment treaties, investors will continue to challenge tax policies before ISDS tribunals that may potentially fall within the realm of DTCs. States will, in turn, continue to face the consequences of regulatory gaps, such as unintended and expansive interpretations of treaty provisions. It is thus necessary to establish a more effective safeguard for avoiding overlaps between IIAs and tax policymaking. Recent reform efforts taking place mostly at the bilateral level show how states are trying to achieve this goal.

Amending or renegotiating IIAs bilaterally or even regionally may not, however, be the most effective way to advance harmonisation between the regimes. This approach will result in continued fragmentation and will foster treaty shopping by investors that restructure their investments through companies incorporated in states that have signed IIAs that do not contain tax carve-out provisions. It is submitted that any reform efforts designed to improve coherence between IIAs and DTCs will first require the cooperation between investment and tax policymakers. They should avoid the formulation of investment and tax policymaking in vacuums. In this respect, they should seek to minimise the risk of friction between the existing uncoordinated and potentially overlapping dispute resolution mechanisms established in investment and tax treaties.

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The Intersection of Treaties on Tax and Trade: A Case Study of Australia and India

Sunita Jogarajan and Tania Voon

1 Introduction

Historically, international action to address double taxation has been separated from the regulation of international trade, ever since the League of Nations was established in 1920 (Jogarajan 2018). However, various taxation measures have long been subject to obligations under international trade law (e.g. obligations not to discriminate against imported products, including by imposing internal taxes on imports in excess of those imposed on domestically-produced products). More recently, we have seen countries threaten the introduction of retaliatory trade restrictions in response to another country's domestic tax measures (Asen 2021).

The taxation of digital or technical services poses a complex challenge in practice, particularly in attempts to address in DTCs income derived from such services (Pignatari 2021). In this chapter, we demonstrate through a recent case study (arising from an unusual DTC definition of 'royalties' with respect to such services) how trade negotiations may be used to address this and similar tax-related problems. We also show how the traditional separation between tax and trade may be gradually coming to an end.

The *Australia–India Economic Cooperation and Trade Agreement* (ECTA)[1] is a PTA between these two countries, focusing on international trade in goods and services, which was signed on 2 April 2022 and entered into force on 29 December 2022. Australia and India are now continuing negotiations towards a more

[1] *Australia–India Economic Cooperation and Trade Agreement*, signed 2 April 2022 [2022] ATNIF 6 (entered into force on 29 December 2022).

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comprehensive agreement, building on ECTA, which will include an investment chapter. ECTA includes a side letter that confirms the two countries' agreement that the Australian government would amend its 'domestic taxation law to stop the taxation of offshore income of Indian firms providing technical services to Australia' (Tehan 2022; Goyal 2022). Australia has amended its domestic tax law as promised.

As we explain in Sects. 2 and 3, the inclusion of the side letter in ECTA resolved a long-standing tax issue with significant financial implications for the two countries, which arose from a series of decisions by Australian courts made between 2015 and 2019 regarding the taxation of income from technical and consultancy services supplied remotely by an Indian company, Tech Mahindra Limited. Strangely, this resolution was achieved without the need for a formal amendment of the *Agreement between the Government of Australia and the Government of the Republic of India for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income* [1991] ATS 49 (Australia–India DTC).

The inclusion in a PTA of a commitment of a kind that would usually appear in a DTC raises complex questions regarding the interaction of international obligations on trade and tax. In Sect. 4, we take our case study further by identifying possible inconsistencies that may arise between the ECTA side letter (and its subsequent implementation through Australian tax law) and Australia's obligations as a WTO Member. This analysis provides a snapshot of the kinds of considerations under international trade law that countries need to have in mind when introducing tax measures that may adversely affect the profits of foreign entities or individuals. Our WTO example shows how the conclusion of a tax agreement in a PTA rather than a DTC may exacerbate the risk of conflicting international obligations. The potential also exists for clashes with international investment law, although in this chapter we do not examine that scenario in any depth.

2 Payments for Technical and Consultancy Services from India: The Australian Tech Mahindra Case

This section examines a series of Australian judicial decisions in the Federal Court of Australia and High Court of Australia between 2015 and 2019 regarding the taxation of payments for technical and consultancy services provided by employees of an Indian company, located in India, to customers located in Australia. The Australian courts found, at first instance and in the subsequent appeals, that the payments were taxable in Australia pursuant to the Australia–India DTC. These decisions, which we address chronologically, led to a major concern for Indian companies providing 'cross-border' services from India into Australia. The decisions also demonstrate the challenges and complexities that can arise from interpretation by domestic courts of DTCs, particularly where the DTC parties may have different international obligations, different domestic laws interacting with the DTC, and different judicial traditions and methods.

2.1 The Decision at First Instance (2015): Federal Court of Australia Holds Payments for Indian IT Services Taxable as Royalties

In *Tech Mahindra Limited v Commissioner of Taxation* [2015] FCA 1082, the taxpayer, formerly Satyam Computer Services Limited, was an Indian tax resident company. It provided software products and information technology services (IT services) to Australian customers. The taxpayer had offices in Australia. The IT services to Australian customers were provided by both employees located in Australia (the Australian services) and employees located in India (the Indian services). It was not in dispute that the taxpayer's offices in Australia constituted a permanent establishment (PE) for the purposes of the Australia–India DTC. It was also not in dispute that the *Australian* services were attributable to the Australian PE and were therefore taxable in Australia under the Australia–India DTC. At issue was whether the *Indian* services were taxable in Australia (for the income years ending 30 June 2009, 30 June 2010, and 30 June 2011).

The relevant IT services fell into 9 categories:

1. New software development;
2. New software customisation;
3. Software maintenance;
4. Problem solving involving no change to source code;
5. Problem solving involving a change in the source code;
6. Enhancements to existing software;
7. Development of test cases and test scripts;
8. Running tests of new releases; and
9. One-off consulting or advisory work relating to the customer's IT infrastructure.

At first instance, a single judge in the Federal Court of Australia (Justice Perry) found that the payments for some of the Indian services were taxable in Australia because they constituted royalties. The relevant definition of 'royalties' is in Article 12(3)(g) of the Australia–India DTC, which captures 'the rendering of any services (including those of technical or other personnel) which make available technical knowledge, experience, skill, knowhow or processes or consist of the development and transfer of a technical plan or design'. This definition of 'royalties' is rare for Australia, being broader than the definition of 'royalties' under Australian domestic law and unlike the definition of royalties in other Australian tax treaties (Explanatory Memorandum 1991).

The taxpayer and the Commissioner disagreed as to the interpretation of 'make available' in the definition of royalties in Article 12(3)(g). The taxpayer contended that the technical knowledge, etc., would be 'made available' only if the recipient could use that knowledge independently of the taxpayer. In contrast, the Commissioner considered it sufficient if the technical knowledge was applied to the recipient's project (i.e. by developing and maintaining software for customers and

consulting on a customer's IT infrastructure, the taxpayer was making the relevant technical knowledge available to the customer).

The Court agreed with the taxpayer's interpretation of 'make available', stating (at [93]):

> To say that the contractual arrangements make available the technical knowledge of the applicant's employees to the customer gives no content to the requirement that the technical knowledge must be made available by the rendering of the services, as opposed to comprising the service that is rendered.

Her Honour considered this interpretation consistent with both the 'ordinary meaning' of Article 12(3)(g) and the other payments constituting royalties in Article 12, and supported by the explanation and examples in the Explanatory Memorandum.[2]

Nevertheless, the Court found that the relevant payments were 'royalties' because they related to the 'development and transfer of a technical plan or design'. The taxpayer argued that 'plan or design' necessitated a forward-looking aspect to the work, which did not encompass the development of a computer program. This interpretation was not accepted by Justice Perry, who found that 'source code on which software is based may also be described … as a plan' (at [105]) and 'the ordinary meaning of "design" is also apt to embrace computer software' (at [106]). Referring to the 9 categories of IT services mentioned above, the Court found that payments related to categories 1, 2, 5, and 6 constituted 'royalties' as they related to the 'development and transfer of a technical plan or design'. Payments related to categories 7 and 8 were also found to be royalties as they were ancillary to the provision of services in category 6.

The Court also considered the Commissioner's alternative argument that the payments for the Indian services were taxable in Australia under Article 7 on business profits. The parties agreed (see [83]) that the payments for the Indian services were not 'attributable to' the Australian PE within the meaning of Article 7(1)(a) and therefore were not taxable in Australia on that basis. The Commissioner argued that the payments were nevertheless captured by Article 7(1)(b), which refers to 'other business activities of the same or a similar kind as those carried on, through that permanent establishment'. The Court found that the 'force of attraction' rule in Article 7(1)(b) was of limited application in 'international custom and practice' and did not capture the payments for the Indian services (at [137], [142]).The Court also rejected the taxpayer's argument with respect to Article 12(4) of the Australia–India DTC, as we explain further in Sect. 2.2. The taxpayer had pursued a novel argument, based on the wording of Articles 7 and 12, that the payments were not captured by Article 12 on royalties (as they were 'effectively connected' with the Australian PE) but they were not taxable in Australia under Article 7 (as they were not 'attributable' to that PE).

[2]The Court also considered the relevance of the Explanatory Memorandum in interpreting the Australia–India DTC.

2.2 *Full Court of the Federal Court of Australia Dismisses Taxpayer's Appeal (2016)*

The taxpayer appealed Justice Perry's decision to a Full Court of the Federal Court of Australia (constituted by Justices Robertson, Davies, and Wigney) in *Tech Mahindra Limited v Commissioner of Taxation* [2016] FCAFC 130, which concerned a single issue, being the operation of Article 12(4) of the Australia–India DTC. On appeal, the taxpayer conceded that the payments for the Indian services were 'royalties' but argued that those royalties were 'effectively connected' with the Australian PE and therefore not taxable in Australia as royalties.

Article 12(4) stipulates that where royalties are 'effectively connected with [a] permanent establishment', Articles 12(1) and 12(2) do not apply, and the payments are instead to be taxed under Article 7 on business profits. As noted above in Sect. 2.1, the parties had agreed that the payments were not taxable in Australia under Article 7(1)(a), and Justice Perry had determined that the payments for the Indian services were not taxable in Australia under Article 7(1)(b) on business profits. This finding by Justice Perry was not appealed. Therefore, if the taxpayer was successful in demonstrating on appeal that the royalties were 'effectively connected' with the Australian PE and were not taxable under Article 12 on royalties due to the operation of Article 12(4), the payments would have escaped Australian taxation entirely.

The taxpayer's argument on appeal was that the Indian services were so intrinsically connected to the provision of Australian services that the provision of Indian services, and the payments for those services, were 'effectively connected' with the Australian PE (see [17]). The taxpayer further argued that Justice Perry's interpretation of 'effectively connected' was based on an assumption regarding the purpose of Article 12(4) rather than the wording of the provision (see [14]).

The Commissioner had argued at first instance, and Justice Perry had accepted (at [76]), that the purpose of Article 12(4) was to give the source country the right to tax payments connected to a PE at the 'more generous rates' available for the taxation of business profits under Article 7(1), rather than the limited rates available for the taxation of royalties under Articles 12(1) and 12(2). Therefore, her Honour found that the words 'effectively connected' in Article 12(4) 'are intended to encapsulate in a short-hand way the different tests of connection under Articles 7(1)(a) and 14' (the former test being 'attributable to'), and 'Article 12(4) gives priority to Article 7 [only] where the criteria in Article 7(1)(a) are met', which was not the case here (see [73], [77], [83]).

The Full Court of the Federal Court agreed with Justice Perry's interpretation of 'effectively connected' and therefore dismissed the taxpayer's appeal, stating (at [31]):

> [T]he evident purpose of Art 12(4) is to relieve the source State from the limitation on taxing rights imposed under Art 12 by taxing such royalties under Art 7, not to disentitle the source State from any taxing rights where otherwise Art 7 would not give such taxing rights. Such a construction gives effect to the language of Art 12(4) and is consistent with the extrinsic materials.

In reaching this conclusion, the Full Court noted that a 'holistic approach' is required in interpreting the Australia–India DTC, pursuant to Article 31 of the *Vienna Convention on the Law of Treaties* (VCLT):[3] '[t]he written text has primacy but the Court must also have regard to the context, object and purpose of the treaty provisions' (at [22]). Applying this approach, the Full Court relied on 'extrinsic materials' including the explanatory memorandum to the relevant domestic legislation and the commentary on the UN Model Convention.

Australia is a party to the VCLT. Although India is not, several aspects of the VCLT (including Articles 31 and 32 on treaty interpretation) are widely understood as codifying or having attained the status of customary international law (Kulick and Waibel 2024; Gardiner 2015), meaning that they would also apply to India. Nevertheless, this example of a slight difference in the situation of Australia and India as a matter of public international law foreshadows the possibility of different countries interpreting the DTC between them in different ways, for the purposes of their domestic law. Later in this dispute, the Full Court commented indirectly on that potential for conflict, as we explain in the following section.

2.3 Further Appeals Declined (2017–2019): DTC Prevails Over Domestic Tax Provisions

The High Court of Australia (Australia's highest court) declined the taxpayer's application for special leave to appeal (*Tech Mahindra Limited v Commissioner of Taxation* [2017] HCATrans 58 (10 March 2017)), leaving the taxpayer with no further avenue of appeal in respect of the issues discussed in Sects. 2.1 and 2.2. However, under special rules of the Federal Court of Australia, the taxpayer appealed to the (identically constituted) Full Court of the Federal Court on one further issue: *Satyam Computer Services Limited (Now an Amalgamated Entity Named Tech Mahindra Limited) v Commissioner of Taxation* [2018] FCAFC 172.

The taxpayer challenged Justice Perry's decision at first instance that payments that are royalties under the Australia–India DTC but fall outside the definition of 'royalties' in Australian domestic law are Australian sourced income due to Article 23 of the Australia–India DTC and therefore taxable in Australia under Australian domestic law. In essence, the taxpayer contended that Australia had no right to tax an amount due to the operation of the Australia–India DTC if it would not otherwise have had the right to do so under Australian domestic law.

Under Article 23(1) of the Australia–India DTC, '[i]ncome … derived by a resident of one of the Contracting States which, under [Article 12] may be taxed in the other Contracting State, shall for the purposes of the law of the other State relating to its tax be deemed to be income from sources in that other State'.

[3] *Vienna Convention on the Law of Treaties* opened for signature on 23 May 1969, 1155 UNTS 331 (entered into force on 27 January 1980).

The Full Federal Court accepted that the royalties were Australian sourced due to the operation of Article 23, even though they were not Australian sourced under the relevant domestic tax assessment legislation. As such, the royalties were taxable in Australia. The primary reason for this conclusion was that all Australian DTCs are incorporated into domestic law in Australia. The Australia–India DTC is incorporated into Australian tax law by virtue of Sect. 5 (and previously section 11Z) of the *International Tax Agreements Act 1953* (Cth) (Agreements Act), which gives that treaty 'the force of law according to its tenor'. Therefore, the Court explained (at [16]) that 'the deeming of source effected by Art 23 is given the force of law for Australian tax law purposes'.

Moreover, to the extent of inconsistency with Australian domestic tax provisions regarding the source of royalties, the Court held that Article 23 prevails: 'the provisions of Art 23 are the "leading" provisions and the definition of "Australian source" in [the relevant domestic tax provision] is the "subordinate provision" which "must give way" to' Article 23 (at [19], citing Agreements Act s 4(2); *Project Blue Sky Inc v Australian Broadcasting Authority* [1998] HCA 28, [70]). This conclusion reflects the fact that, in general under Australian law, DTCs take precedence over domestic tax law provisions, other than the domestic anti-avoidance provisions.

As noted by the Full Court, the courts in India have taken a different approach to the hierarchy between a DTC and domestic tax law, concluding that a DTC does not create a taxing right if an amount is not taxable under the domestic law. However, the Court maintained (at [21]) that any inconsistency in the approach of the two countries on this question arises not from an inconsistent interpretation of the Australia–India DTC 'but [from] the effect of Australia's domestic law in ss 4 and 5 of the Agreements Act'. This reasoning of the Court dismisses, in relation to this particular example, the potential concern about Australia and India interpreting the Australia–India DTC in different ways, because the difference is explained by the domestic laws of the two countries rather than the DTC itself.

The taxpayer appealed this decision to the High Court but was not granted special leave to appeal: *Satyam Computer Services Limited (Now an Amalgamated Entity Named Tech Mahindra Limited) v Commissioner of Taxation* [2019] HCASL 87. As such, the decisions of the Full Federal Court stood and the relevant payments for the provision of services in India to Australian customers were taxable in Australia. That outcome, covering income years ending in 2009–2011, was unaffected by the subsequent resolution of the broader dispute between the two countries, to which we now turn.

3 Resolution of a Tax Dispute Through a Trade Agreement: ECTA (2022)

This section demonstrates how the Australian judicial decisions addressed in Sect. 2 resulted in a substantial problem for the Indian IT industry (and consequently the Indian government). We first explain how that problem manifested itself and came to be a priority for resolution by both governments, due to the circumstances of their economic relationship at the time. We then show how the problem was resolved, not through amending the DTC but through a PTA (ECTA), containing a promise by the Australian government that was then given effect through Australian domestic law. Finally, we consider the legal status of the relevant 'side letter' to ECTA reflecting the agreement on this tax issue, and what it means as a matter of DTC amendment and interpretation, for example if Australia were later to repeal the change. We show how India would have legitimate grounds for contesting such a move, based on its legal rights under tax, trade, and investment treaties with Australia.

3.1 Intersecting Interests of Australia and India

The *Tech Mahindra* caselaw had an overwhelming effect on Indian industry. The Indian IT industry's total annual revenues from the Australian market were estimated at approximately AUD $2–$3 billion, 50% of which was expected to be outsourced to India (Majumdar and Ishwarbharath 2022). At a withholding tax rate of 15%, approximately AUD$225 million would be 'lost' by the Indian IT industry to the Australian tax authority annually. For the ten-year period commencing 2011–12, the cumulative loss was estimated at over $1 billion. The Indian National Association of Software and Service Companies (NASSCOM) lobbied the Indian government for several years to address the issue (Seth and Mishra 2022).

Despite these concerns from India's perspective, the Australian government had no real incentive to reopen negotiations on the Australia–India DTC. The Australia–India DTC was more than 30 years old but was amended by Protocol in 2010 and fairly captured the two countries' economic interests but for this one issue. Although Australia may not have been interested in revisiting the Australia–India DTC, it was keen to secure a trade agreement with India to access the fast-growing Indian market of over 1.4 billion people. This confluence of events presented an opportunity (and a bargaining tool) for the Indian government to push for change to the Australian taxation of Indian IT services, through negotiations towards ECTA, which began in 2021.

3.2 The ECTA Side Letter and Changes to Australian Tax Law

As a result of Indian pressure on this issue, as noted in the introduction, an ECTA side letter confirmed the agreement by India and Australia that the Australian government would amend its domestic law, 'in a similar time period as' ECTA, to 'stop the taxation of offshore income of Indian firms providing technical services to Australia' in order to 'resolve the issue that the Indian Government has raised about the' Australia–India DTC. The side letter (taking a duplicate form signed by a representative of each country to the other) characterised itself as constituting 'an integral part' of ECTA.

Thus, this extended tax dispute arising between India and Australia from the Australian judicial decisions in *Tech Mahindra* was resolved, not through direct amendment of the Australia–India DTC, but through agreement reached in trade negotiations towards ECTA, and as part of that trade-focused treaty. The use of side letters in general (but not with this particular tax content) is a common feature of Australia's PTAs. They likely form part of the treaty to which they are attached and would be enforceable within the bounds of their terms. Under Article 2(1) of the VCLT, a 'treaty' means 'an international agreement concluded between States in written form and governed by international law, whether embodied in a single instrument or in two or more related instruments and whatever its particular designation'. This description would extend to the ECTA side letter, whether as part of or separate from ECTA itself.

Australia effected the promised amendment by enacting the *Treasury Laws Amendment (Australia–India Economic Cooperation and Trade Agreement Implementation) Act 2022*, which received royal assent on 23 November 2022. As of 29 December 2022 (being the date of entry into force of ECTA), that Act inserted into the Agreements Act section 11J, which states that the Australia–India DTC:

> does not have the effect of subjecting to tax any payments … to the extent to which they
>
> (a) are made as consideration for the rendering of any services covered by paragraph 12(3)(g) … and
>
> (b) are not royalties (within the meaning of [Australian domestic law]); and
>
> (c) would … not [otherwise] be subject to Australian tax.

For the taxpayer in the *Tech Mahindra* case, this domestic provision (if existing at the relevant time) would have meant that the payments for the Indian services would not have been taxable in Australia. Although the DTC by its terms may appear inconsistent with this approach, when properly interpreted as shown in the next section it no longer precludes it, following the introduction of the ECTA Side Letter.

3.3 Legal Status and Implications of the ECTA Side Letter for the Australia–India Economic Relationship: Tax, Trade, and Investment

Does the ECTA side letter amend the Australia–India DTC? Probably not. As that DTC has no specific provisions regarding its amendment, the 'general rule' in VCLT Article 39 would apply, such that it 'may be amended by agreement between the parties'. Although India and Australia agreed on the ECTA side letter, it is not framed (in its terms) as an amendment to the Australia–India DTC.

Nevertheless, the ECTA side letter is likely to be relevant in interpreting the Australia–India DTC from the date of entry into force of ECTA. Under VCLT Article 31(3)(a), the ECTA side letter might constitute a 'subsequent agreement between the parties regarding the interpretation of [the Australia–India DTC] or the application of its provisions'. Pursuant to VCLT Article 31(3)(b), the ECTA side letter might be regarded as 'subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation', such that a treaty interpreter should take it into account in interpreting the Australia–India DTC. Moreover, under VCLT Article 31(3)(c), ECTA (including the ECTA side letter) would almost certainly constitute 'relevant rules of international law applicable in the relations between the parties' and should therefore be taken into account in interpreting the Australia–India DTC on that basis.

These interpretative materials may be particularly relevant in resolving any future disputes about the interaction between Articles 7 and 12 of that DTC. Specifically, if Australia repealed section 11J (while ECTA and its side letter remained in force), India might successfully contend that this action was contrary not only to ECTA (which provides for dispute settlement under its Chap. "The Interaction Between IIAs and DTCs: Potential for Overlap and Reform Proposals") but also to the Australia–India DTC, as properly interpreted pursuant to the VCLT as discussed in the previous paragraph.

Investment obligations fall largely outside the scope of this chapter. However, an Indian investor in Australia might also seek to bring an investment treaty claim against Australia in these hypothetical circumstances (repeal of section 11J of the Agreements Act). Australia and India signed a Bilateral Investment Treaty (BIT) in 1999.[4] The treaty entered into force in 2000 but was terminated unilaterally by India in 2017 (one of 58 such terminations by India at the time) (Hepburn 2017). Like Australia's other BITs in force (as well as those now terminated), the Australia–India BIT includes an Investor–State Dispute Settlement (ISDS) mechanism that could allow such a claim, subject to jurisdictional requirements (which might depend on the connection between the company's Australian assets and these services and payments). Significantly, the termination of this BIT does not prevent all

[4] *Agreement between the Government of Australia and the Government of the Republic of India on the Promotion and Protection of Investments*, signed on 26 February 1999, 2116 UNTS 145 (entered into force on 4 May 2000, terminated on 23 March 2017).

future claims. Article 17(3) of the BIT provides that the terminated treaty will continue to apply and provide protection to investments made or acquired before 23 March 2017, for a further 15 years from the treaty's termination on that date. Such protections could be enforced through either 'state to state' dispute settlement under Article 13 of the BIT or ISDS under Article 12.

An Indian investor in Australia might contend, for example, that the repeal of section 11J constituted unlawful 'expropriation' contrary to Article 7 of the BIT or a failure to accord 'fair and equitable treatment' as required by Article 3(2). Such claims would likely face some jurisdictional and substantive difficulties.

4 Consistency of the ECTA Side Letter with Australia's Tax-Related WTO Obligations: Potential Complaints by Other WTO Members?

Australia (like India) is a founding Member of the WTO, since its creation in 1995. In this section, we consider section 11J of the Agreements Act and the ECTA side letter in the context of Australia's WTO obligations with respect to WTO Members other than India. We begin by outlining some of the many WTO provisions that relate to tax. We then turn to Australia's General Agreement on Trade in Services (GATS) obligations, which are more relevant to the taxation of services at issue here. In particular, we explain how Australia's GATS Most-Favored Nation (MFN) obligation could give rise to complaints by other WTO Members of Australia's preferential treatment of Indian services and service suppliers with respect to taxation.

We then identify the exceptions that Australia might rely on to justify this preferential treatment, most notably GATS Article V, which relates to economic integration. The application of that exception is uncertain and difficult to predict as compared to the exceptions and exclusions that would apply to preferential tax arrangements contained in a DTC (which would be the more usual approach) rather than a PTA, as we then explain. The inclusion of the relevant side letter in ECTA rather than the Australia–India DTC therefore increases the risk of breaching Australia's WTO obligations.

Our brief analysis demonstrates the absence of a clear-cut answer as to whether the preferential tax treatment that Australia has granted to India is consistent with WTO law. As for whether it is consistent with Australia's other trade and investment obligations with respect to its other trade and investment partners under other treaties is beyond the scope of this paper but equally complex and unclear.

4.1 Australia's WTO Obligations Related to Tax

Many WTO obligations relate to tax. For example, in the goods context, the first sentence of the national treatment obligation in Article III:2 of the GATT 1994 precludes WTO Members from subjecting imported products 'to internal taxes or other internal charges of any kind in excess of those applied … to like domestic products'. The MFN obligation in GATT Article I:1 requires Members to accord 'any advantage, favour, privilege or immunity granted … to any product originating in or destined for any other country … immediately and unconditionally to the like product originating in or destined for the territories of all other WTO Members'. That obligation applies, inter alia, 'with respect to all matters referred to in paragraphs 2 and 4 of Article III', hence including internal taxes. In the investment context, Article 2.1 of the WTO's *Agreement on Trade-Related Investment Measures* (TRIMS) similarly draws on GATT Article III by disallowing 'investment measures related to trade in goods' that are inconsistent with that provision.

4.2 Potential Conflict Between Australia's Tax Law Change and Its GATS Obligations

The WTO agreement that is most clearly related to the ECTA side letter on 'the taxation of offshore income of Indian firms providing technical services to Australia' is GATS. That agreement covers four modes of service supply, defined in Article I:2, including 'commercial presence' (mode 3, corresponding to FDI), which involves the supply of a service 'by a service supplier of one Member, through commercial presence in the territory of any other Member' (e.g. by way of a subsidiary company). However, more relevant to the side letter is mode 1, known as cross-border supply, involving the supply of a service 'from the territory of one Member into the territory of any other Member'. The side letter applies to cross-border supply of technical services from Indian firms (the service suppliers, located and established in India) into Australian territory (where the service consumers are located).

The ECTA side letter, as now implemented in Australian domestic law, could raise concerns of conflict with GATS. Some GATS obligations such as national treatment (Article XVII) depend on individual Members' commitments in particular sectors, as set out in their GATS schedules. Those schedules are sometimes helpful in interpreting particular terms, such as 'technical services' in the ECTA side letter (although that letter forms part of a different treaty). Australia's GATS schedule refers to 'Other business services' (sector F), a subset of which is 'related scientific and technical consulting services' (subsector (m)), in which Australia has made full national treatment commitments for modes 1 to 3.[5] However, this subsector

[5] *Australia—Schedule of Specific Commitments*, WTO Doc GATS/SC/6 (15 April 1994) 20 (note also subsequent supplements to this document, e.g. for telecommunications and financial services).

includes a cross-reference to the corresponding sectors in the UN's 1991 CPC, which makes clear that 'technical … services' in Australia's GATS schedule has a specific meaning, likely much narrower than that intended in the ECTA side letter, relating to 'subsurface surveying services', in the context of administering land and sea.[6] Other sectors may be more likely intended by 'technical services' in the ECTA side letter, such as computer and related services or telecommunications services.

The MFN obligation in GATS Article II:1 requires, with respect to measures covered by that agreement, that WTO Members:

> accord immediately and unconditionally to services and service suppliers of any other Member treatment no less favourable than that it accords to like services and service suppliers of any other country.

Australia has amended its domestic tax law to 'stop the taxation of offshore income of Indian firms providing technical services to Australia' (to use the description in the ECTA side letter) in certain circumstances. Pursuant to current practice, Australia would not be taxing the offshore income of firms of other WTO Members providing technical services to Australia in those circumstances either, because Australia's other DTCs do not generally define 'royalties' to incorporate these kinds of payments in the way the Australia–India DTC does. However, the definitions in other Australian DTCs could be amended in future to align with the Australia–India DTC approach, for example in the context of resolving ongoing tensions regarding the taxation of digital services. That would mean Australia could begin taxing these payments. Without an equivalent to the ECTA side letter, those other Members might therefore complain of a breach of GATS MFN. Although that obligation is subject (under Article II:2) to Australia's negotiated list of MFN exemptions, that list is currently limited to audiovisual services (co-production agreements and responses to unreasonable measures imposed on Australian services or service suppliers by other Members).[7] These exemptions would therefore apply, if at all, only to a small subset of technical services provided by Indian firms.

4.3 Australia's Defence Under GATS Article V: Economic Integration

Certain other GATS exceptions might assist Australia in defending section 11J and the ECTA side letter against an MFN claim. Most obviously, the exception for economic integration under GATS Article V might apply, provided that ECTA meets the requirements of Article V:1. Those requirements are (a) 'substantial sectoral coverage' (in terms of 'number of sectors, volume of trade affected and modes of

[6] *Statistical Papers: Provisional Central Product Classification* (United Nations 1991) 8672, 8673.

[7] *Australia—Final List of Article II (MFN) Exemptions*, WTO Doc GATS/EL/6 (15 April 1994); *Australia—List of Article II (MFN) Exemptions, Supplement 1*, WTO Doc GATS/EL/6/Suppl.1 (26 February 1998).

supply') and (b) 'elimination of substantially all discrimination … between or among the parties, in the sectors covered … either at the entry into force … or on the basis of a reasonable timeframe, except for measures permitted under' GATS general exceptions (Article XIV), security exceptions (Article XIV*bis*), or allowed restrictions: on international transfers and payments (Article XI); or to safeguard the balance of payments (Article XII).

Whether ECTA qualifies as such under GATS Article V is difficult to assess because of the lack of substantive WTO caselaw on this provision,[8] as well as the limited information available through the WTO Committee on Regional Trade Agreement's assessment of individual agreements. Under the ECTA services chapter (Chap. "Competition and Complementarity of EU and FATF Beneficial Ownership Transparency Orders"), Australia adopts a negative list approach (committing to provide national treatment, MFN treatment, market access, and local presence except to the extent specified), while India adopts a positive list approach (committing to provide national treatment, MFN treatment, and market access only in the sectors and to the extent specified). Despite this difference in approach, in its summary of ECTA outcomes, Australia's Department of Foreign Affairs and Trade (DFAT) implies that ECTA does have substantial sectoral coverage within the meaning of GATS Article V, indicating that 'Australian service suppliers will benefit from full or partial access across more than 85 Indian service sectors and subsectors' (DFAT 2022), as reflected in India's schedules of specific commitments.[9]

4.4 Unlikely Defences: Exclusion of Dispute Settlement with Respect to Avoidance of Double Taxation; GATS General Exceptions Regarding Tax

Two GATS provisions relate specifically to the interaction of WTO obligations with DTCs. In contrast to GATS Article V (which depends on the extent to which a given PTA 'qualifies' for the exception on economic integration by being sufficiently extensive), a respondent in a WTO dispute (in our example, Australia) could more easily and objectively demonstrate that these provisions apply to measures contained in or clearly arising from a DTC.

Under GATS Article XXII:3, a WTO Member may not invoke the national treatment obligation in Article XVII in consultation or dispute settlement procedures 'with respect to a measure of another Member that falls within the scope of an international agreement between them relating to the avoidance of double taxation'.

[8] See, e.g., Panel Report, *Canada—Certain Measures Affecting the Automotive Industry*, WTO Doc WT/DS139/R, WT/DS142/R (circulated on 11 February 2000, adopted on 19 June 2000) ('*Canada—Autos*') [10.268]–[10.272]. This Panel Report was modified on appeal and these findings were rendered moot because the Appellate Body reversed the Panel's finding that Canada had breached GATS Article II (the MFN obligation).

[9] ECTA, annex 8E (schedules of specific commitments: India).

Australia's new section 11J of the Agreements Act might constitute such a measure, to the extent that it is seen as falling within the Australia–India DTC (a difficult question that could be resolved through arbitration as provided for in GATS Article XXII:3 and its footnote 11, if both countries consented). However, although Article XXII:3 might prevent another WTO Member from raising a national treatment concern with section 11J or the ECTA side letter, it would not preclude a claim of violation of the MFN obligation in Article II:1.

In contrast to GATSA article XXII:3, which focuses on the national treatment obligation, GATS Article XIV(e) focuses on the MFN obligation. Article XIV(e) provides, as one of the GATS 'general exceptions' (which correspond broadly with those contained in GATT Article XX) that GATS is not to be 'construed to prevent the adoption or enforcement by any Member of measures' inconsistent with the MFN obligation in GATS Article II:

> provided that the difference in treatment is the result of an agreement on the avoidance of double taxation or provisions on the avoidance of double taxation in any other international agreement or arrangement by which the Member is bound.

That exception, like the other general exceptions, is subject to the 'chapeau' of GATS Article XIV, which imposes a 'requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where like conditions prevail, or a disguised restriction on trade in services'.

The general exceptions in GATT and GATS are the subject of extensive WTO caselaw, which in most instances leads to a finding of WTO-inconsistency, on the basis that the challenged measure does not meet the requirements of either the specified subparagraph or the chapeau. Compliance with the chapeau is not easily attained. However, focusing on paragraph (e), the question arises whether the 'difference in treatment' (effected through section 11J of the Agreements Act) is 'the result of' the Australia–India DTC. Arguably, it's not. Instead, section 11J is the result of ECTA and, more specifically, the ECTA side letter. Does the ECTA side letter constitute an 'international agreement or arrangement by which [Australia] is bound'? Yes, probably. But does the ECTA side letter contain 'provisions on the avoidance of double taxation'? Australia might (somewhat weakly) argue that it does because it states that the promised amendment 'would resolve the issue that the Indian Government has raised about' the Australia–India DTC.

GATS Article XIV(d), another general exception (and therefore also subject to the chapeau), applies to measures inconsistent with the national treatment obligation in Article XVII, 'provided that the difference in treatment is aimed at ensuring the equitable or effective imposition or collection of direct taxes in respect of services or service suppliers of other Members'. Article IVIII(o) defines 'direct taxes' as comprising:

> all taxes on total income, on total capital or on elements of income or of capital, including taxes on gains from the alienation of property, taxes on estates, inheritances and gifts, and taxes on the total amounts of wages or salaries paid by enterprises, as well as taxes on capital appreciation.

Although the payments for Indian services in this dispute would likely constitute 'direct taxes' within the meaning of GATS Article XIV(d), this provision addresses national treatment and so, like Article XXII:3, would not assist in justifying a breach of the MFN obligation. Whether the differential treatment 'is aimed at ensuring the equitable or effective imposition or collection of direct taxes' in respect of Indian services or service suppliers, as required by Article XIV(d), would also be contentious.

In 2016, the Appellate Body pointed out that these two exceptions related to tax in GATS Article XIV are absent from GATT 1994, stating:

> The two exceptions relating to taxation, in particular, reflect the fact that the GATS covers service suppliers, as the imposition of direct taxes and agreements on the avoidance of double taxation are particularly relevant for juridical and natural persons, and thus service suppliers.[10]

5 Conclusion

The *Tech Mahindra* case demonstrates the possibility of using withholding taxes to tax income from digital or technical services (Christians and Magalhães forthcoming). The Argentine government has recently flagged the possibility of introducing a withholding tax mechanism on digital service providers if progress on Pillar 1 is stalled (Soong 2023). However, as the subsequent Indian response to Australia's judicial decisions demonstrates, any unilateral measures to tax digital service providers or technical services are unlikely to succeed, as economic actions are intertwined, and countries typically adopt a holistic view of their bilateral relationships. Thus, India took the opportunity to resolve the problem created by Australian tax caselaw when Australia sought to strengthen the two countries' trade relationship.

The historical separation of tax policies from trade relationships may be coming to an end, a century after its creation. Our case study of Australia and India shows how countries may in future seek to resolve tax disputes through trade negotiations, specifically in conjunction with the conclusion of PTAs. Such an approach may increase the potential for preferential tax treatment (agreed within the context of a PTA and implemented in domestic law) to create breaches of other areas of international economic law: specifically international trade law (through the WTO and other PTAs) and international investment law (through BITs and investment chapters of PTAs).

Our case study focuses on the potential for the ECTA side letter to lead to complaints by other WTO Members against Australia about the tax advantages provided to Indian services and service suppliers. We show how these advantages could conceivably lead to future breaches of Australia's MFN obligation under GATS Article

[10] Appellate Body Report, *Argentina—Measures Relating to Trade in Goods and Services*, WTO Doc WT/DS453/AB/R and Add.1 (circulated on 14 April 2016, adopted on 9 May 2016) ('*Argentina—Financial Services*') [6.113].

II:1. In addition, the preferential treatment would likely be more easily justified under GATS exceptions relating to DTCs (specifically, Article XIV(e)), if the side letter or its equivalent was contained in the Australia–India DTC, rather than in a PTA such as ECTA. As the side letter is attached to ECTA, Australia would instead have to rely on the exception for economic integration under GATS Article V, leading to a less certain outcome depending on a WTO Panel's assessment of the comprehensiveness of the ECTA as an agreement liberalising trade in services.

Complex questions and possible inconsistencies arising from the ECTA side letter may be multiplied by considering Australia's obligations to other trading partners under its 17 other PTAs in force, most of which replicate, and some of which extend, Australia's WTO obligations. The potential for unknown ramifications is further heightened by the fact that these other trade agreements generally include extensive investment obligations, mostly including an ISDS mechanism (under which an investor may bring an arbitral dispute directly against the state hosting their investment). Moreover, Australia has in force 15 BITs, all of which include ISDS mechanisms (Voon and Merriman 2022). The Australia–India case study therefore provides insight into the scale and nature of the potential interactions between tax and trade policies in international economic law should other countries seek to address tax concerns through PTAs rather than DTCs in future.

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The Legal Transplant of EU Standards in Taxation: A Case Study of the ACP Post-Cotonou Agreement

Irma Mosquera and Filip Debelva

1 Introduction

The aim of this contribution is to study the legal transplant of EU Standards in non-EU countries. These standards are either voluntarily implemented by the country or, alternatively, imposed by the EU as part of the *acquis communautaire* or when concluding agreements (e.g. trade, economic, or partnership) with these countries. Watson's definition of legal transplants ("*As the moving of a rule or a system of law from one country to another, of from one people to another*") will be applied throughout this chapter (Watson 1974, p. 21).

The import and export of standards has been addressed by scholars in other areas than tax law.[1] These Standards can be developed by the EU itself and subsequently exported (e.g. the EU data protection rules) or imported from international law (e.g. international environmental standards).

Some of the reasons why the EU has exported norms have been discussed by (mainly EU law) scholars. For instance, as explained by Scott (2014) the EU measures are based on international standards, and when not, the standards tend to be

[1] See, e.g., a comparative analysis of the import and export of EU norms by several EU countries and some non-EU countries (Australia, China, New Zealand, and Russia, as well as ASEAN countries) including how the norms are adopted, adapted, resisted, or rejected in those countries (Björkdahl et al. 2015; Cremona 2010, p. 664).

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"characterized by a contingent quality that flows from the provisionality and substantive openness of the measures concerned. This contingent quality injects a dynamic dimension into EU law, whereby the EU intervenes not with a view to exporting its standards but with a view to launching interactive processes to identify and evaluate the different approaches that may adopted to ensure that shared regulatory objectives can be met".

More recently, in her analysis of the "Brussels Effect" Bradford (2015) addressed the regulatory power of the EU. This author stated that '*without resorting to international institutions or seeking other nations' cooperation, the EU is able to promulgate regulations that become entrenched in the legal frameworks of developed and developing markets alike, leading to the "Europeanization" of important aspects of global commerce*'.

In taxation, the study of legal transplant of EU Standards is a relatively recent phenomenon. For instance, in 2018, the present authors have discussed the implementation of the Data Protection Directive by countries to protect taxpayer's right to privacy and confidentiality (Debelva and Mosquera Valderrama 2017). Another example is the study of the transplant of the EU Standard of Tax Good Governance in economic, trade, and partnership agreements concluded by the EU with non-EU countries. This EU Standard provides for transparency, exchange of information, fair taxation, and implementation of BEPS 4 Minimum Standards (Mosquera Valderrama 2019). This contribution aims to follow up on these studies by introducing a framework for the study of legal transplants in the EU and beyond. The findings of this analysis can be useful for policymakers in tax, trade, and investment in the EU and outside the EU when seeking solutions to tackle global challenges, e.g. tax evasion, climate change, big data, governance, and sustainability.

The first part of this contribution will address the theory of legal transplants, explaining what legal transplants are, and why and how they take place. This theory has been developed by one of the authors elsewhere; hence this part will provide the main elements that any policymaker should be aware of when considering whether to transplant rules or concepts developed elsewhere. Investigating the reasons why legal transplants take place can help to understand the changes (if any) of the rules upon transplantation into a specific country's legal system.

The second part will address the study of EU Standards in agreements that have been concluded by the EU with non-EU countries. Some of these agreements have been addressed elsewhere by one of the authors,[2] therefore, this part will focus on the recently negotiated 2021 post-Cotonou Agreement concluded by the EU with ACP (African-Caribbean and Pacific) countries (European Commission 2021). This agreement has not yet entered into force. However, as will be demonstrated in the following sections, a study of this agreement will yield interesting results.

This agreement is broader in scope since it uses the EU Standard of Tax Good Governance to deal with issues such as good governance and fairness of tax systems, among others. Therefore, this agreement can constitute a new way for the EU

[2] For instance: economic, trade, and partnership agreements. Ibid.

to influence the development of international law by setting up the application of their own standards (for instance, fair taxation) in their relationships with non-EU countries.

However, the precise contours of the EU standard are unclear in several ways. In this agreement reference is made to a group of four core criteria: efficiency, effectiveness, transparency, and fairness. In order to meet these criteria, reference is made to international and/or EU tax standards, e.g. exchange of information, repeal of harmful tax practices, fair taxation, fair tax competition, standards to prevent base erosion and profit shifting (BEPS 4 Minimum Standards) among others. As we will elaborate in the second part, in our view it is uncertain how these four criteria fit within the standard of EU Tax Good Governance, and the provisions in the text of the agreement do not provide further explanation of this link.

Furthermore, it is uncertain how this Standard will contribute to enhance effective international tax cooperation which has been questioned by regional tax organizations (ATAF), civil society (Cobham 2022), and scholars (Azam 2017; Christians and van Apeldoorn 2018; Mosquera Valderrama 2023), stating that there is a lack of participation of developing countries in the agenda setting and the content of these initiatives. These concerns of legitimacy and inclusiveness have resulted in two recent developments initiated by (i) Latin America and Caribbean countries, i.e. the creation in July 2023 of a Regional Tax Cooperation Platform for Latin American and the Caribbean and by (ii) the African Group at the United Nations, i.e. the adoption in November 2022 of a UN Resolution to develop a globally inclusive new tax framework and in November 2023 of an UN Resolution to develop an international tax framework Convention under the auspices of the UN.[3]

The use of this EU Standard conflicts with the current developments at international level that criticizes the usefulness of international and/or EU Standards to enhance effective tax cooperation, to prevent tax evasion, to enhance domestic resource mobilization, and to achieve the 2030 Sustainable Development Agenda. Therefore, the question that we also address in this contribution is in light of the concerns of legitimacy, inclusiveness, and effective tax cooperation, why countries (in this case, African, Caribbean, and Pacific countries) are committing to the introduction of this EU Standard in their agreements. To find out the reason, we will be using the legal transplant theory developed in part one of this contribution.

In light of the title of this book, the analysis in this contribution will aim to shed light on how the EU influences international tax, trade, and investment policy around the world. The final part of this contribution will provide some conclusions and recommendations for further research.

[3] UN Resolution A/C.2/78/L.18/Rev.1 Promotion of inclusive and effective international tax cooperation at the United Nations available at https://documents-dds-ny.un.org/doc/UNDOC/LTD/N23/356/75/PDF/N2335675.pdf?OpenElement

2 Legal Transplant[4]

2.1 Study of Legal Transplants

In 1974, Alan Watson was the first scholar who pointed out that the possibility and the success of legal transplants stands or falls with similarities of differences in the legal culture of the recipient country (Watson 1974). This might occur due to the influence of the changes of society in the development of law based on the premise that "*law is not static…It exports and imports institutions and itself changes and creates new forms*" (Örücü 1995, p. 5 and 7).

The approach to legal transplants has been used by comparative law scholars mainly to explain the development of law for instance: (i) in the relation between Russia and Eastern Europe (Ajani 1995, pp. 93–117), (ii) in Turkey (Örücü 1995), (iii) with regard to the requirements imposed on Eastern European countries in order to join the European Union (ibid.), and (iv) the development of transplants in the field of corporate law (Pistor et al. 2003). Recently, scholars in other fields have also discussed issues of law and culture, diffusion of governance structures, and the social processes involved in transnational lawmaking (Goldbach 2019).

In taxation, the concept of legal transplants has been used either to study the legal transplant of a specific rule or concept in one or more countries or to study the general theories of comparative law and its usefulness to study legal transplants, for instance, to understand the legal transplant of leasing (Mosquera Valderrama 2010); the legal transplant of corporate tax systems in Vietnam (Le 2006); tax transplants and corporate tax models (Garbarino 2009); transplant of the general anti-avoidance rules (Li 2010, 2013). More recently, the legal transplant of the 4 Minimum Standards to Tackle Base Erosion and Profit Shifting (BEPS) (Mosquera Valderrama 2020); and the legal transplant of the Anti-Tax Avoidance Directive in EU countries (Mosquera Valderrama 2021).

However, to the best of the authors' knowledge, similar studies have not yet taken place in the fields of investment and trade law.[5] The findings of this contribution will contribute to develop a framework so that policymakers but also scholars can study the use of legal transplants in investment and trade law, as well as to be aware of the challenges that non-EU countries can face when introducing (transplanting) either voluntarily or by the imposition of EU standards through binding norms (i.e. international agreements).

[4] This section is based on previous research carried out by one of the authors on the topic of legal transplants. See Mosquera Valderrama (2010).

[5] One exception is Erie and Do Ha (2021). In this article, the authors analyse the role of China in formulating Vietnam's 2018 Special Economic Zones SEZ Bill.

2.2 What: Object of Legal Transplants

In general, the object of legal transplants is broad. Specific rules, institutions, legal concepts and structures can be borrowed (Watson 2000). Even a whole legal system, a whole code, or a whole branch of law of the foreign country, or only individual legal rules or institutes can be transplanted (Zongling 1999). However, comparative law scholars warn that transplanting the rules does not imply that the spirit of a legal system is transplanted as well.

The study of legal transplants can contribute to understand what has been transplanted and how and why the rule has been transplanted. For this purpose, one of the authors has argued elsewhere that in addition to studying the theory of legal transplants it is also important to study the theory of legal and tax culture to understand the differences ('local tuning') in rules among recipient and donor countries or institutions.[6] The proposed approach to legal and tax culture takes into account that the differences in attitudes and beliefs in a country's legal and tax system require the study of the way that the development of law takes place is "law in action" and not only the introduction of a concept in the formal law of the country "law in the books".[7] The following section will address the reasoning of legal transplants.

2.3 Why: Justifications for Legal Transplants

Legal transplants may take place because of authority (Watson 2004), prestige/imposition (Sacco 1991), chance, necessity (Örücü 1995), efficacy of law (Berkowitz et al. 2000) and due to political, economical, and reputational incentives (Schauer 2000).

These examples have been discussed elsewhere, but for EU law and for the purposes of this article, we can also argue that for non-EU countries, legal transplants can take place because of prestige (introduction of "*acquis communaitaire*" in order to become a member of the European Union); chance and necessity (e.g. use of the

[6] This concept is borrowed from comparative law and it is described by Örücü (2002) as follows: 'If the old models are abandoned with "optimistic normativism" while new legal models are looked for, a transplanted legal system not compatible with the culture in the receiving country, without the appropriate transposition and tuning, will create only a virtual reality. In answer to the question, how do legal ideas, institutions and structures find their way from one location to another, it has been aptly put that "laws do not have wings". This alone highlights the importance of those who move the law and help in its internalization, and hence, what I call "tuning"'. See also Mosquera Valderrama (2020).

[7] The discussion in the legal scholarship regarding the relationship between law and society refers to the contextualist approach to the study of law. For this purpose, Ewald has referred that law is not an autonomous discipline, insulated from the surrounding society; rather, if one wishes to study a foreign legal system, one should view the law in its wider context and study its social function. Not law in books, but law in action is the proper object of study for the contextualist' (Ewald 1998; Mosquera Valderrama 2020).

1995 EU Data Protection Directive when introducing data protection laws in their countries); political and economic incentives (due to the introduction of the EU Standard of Tax Good Governance to conclude trade/economic/partnership agreements, to receive EU funding, and to be excluded from the list of non-cooperative jurisdictions).

For this contribution, we will address the legal transplant of EU standards and more specifically the EU Standard of Tax Good Governance in the 2021 post-Cotonou Agreement.

3 Legal Transplant of EU Standards in International Agreements: A Case Study of the ACP Post-Cotonou Agreement

3.1 ACP Post-Cotonou Agreement and the EU Standard of Tax Good Governance

This section will focus on the use of the EU Standard of Tax Good Governance as described in the text of the recently (2021) negotiated African, Caribbean, and Pacific Countries (ACP) Post-Cotonou Agreement. This new agreement is pending ratification by EU countries and ACP countries.[8] When ratified this agreement will replace the current 2000 ACP Cotonou Agreement.

According to the EU, the Cotonou Agreement "is the widest and most comprehensive binding partnership agreement between the EU and third countries: it connects one-fifth of the world's population and covers trade, development and political cooperation between the EU and 78 countries in Africa, the Caribbean and the Pacific (ACP)" (European Parliament Research Service 2023).

However, unlike the 2000 ACP Agreement, the Post-Cotonou Agreement provides a comprehensive approach to tax including the introduction of the Standard of EU Tax Good Governance (the 'Standard'). In the 2000 ACP Agreement, taxation was referred mainly in the context of the carve-out clauses (exclusion of bilateral tax treaties of the ACP Agreement).[9]

[8] However, there are already problems, for instance, regarding the position of South Africa that has decided to withdraw from this new agreement to focus on another agreement between the EU and South Africa (ECDPM 2022, p. 3).

[9] Art. 52 Tax Carve-out Clause, 2000/483/EC: Partnership agreement between the members of the African, Caribbean, and Pacific Group of States of the one part, and the European Community and its Member States, of the other part, signed in Cotonou on 23 June 2000—Protocols—Final Act—Declarations. *OJ.L.* 15 December 2000, Iss. 337.

3.2 Reasoning

The following paragraphs will address the reasoning of the EU to use this Standard in its relationship with third (non-EU) countries.

The Post-Cotonou Agreement includes the common value and interests of ACP countries and the EU which also includes good governance in tax matters. For instance, some of the strategic priorities in the June 2018 negotiating Directives stated that:

> The Agreement will include provisions to support legislation and initiatives addressing all forms of corruption, introduce more transparency and accountability over public funding and in the delivery of public services, improve revenue collection, tackle tax evasion and avoidance, money laundering and illicit financial flows and meet **global tax governance standards**. In this regard, particular attention will be given to the proper use of financial external assistance (Council of the European Union 2018).

The Negotiating Directives in Title I ('Human rights, fundamental freedoms, democracy, rule of law, and good governance') address two important goals on the rule of law, justice, and good governance involving concrete measures including:

- ensure sustainable, accountable and transparent management of natural resource revenues and adopt reforms to ensure fair, just and sustainable tax policies;
- tackle tax fraud, tax evasion and aggressive tax planning, paying particular attention to increasing tax transparency, exchange of information and fair tax competition, in line with relevant international standards and frameworks (ibid.).

This is also in line with the 2016 Action Plan for fair and Effective Taxation in the EU[10] and the 2016 EU External Strategy with non-EU countries that address in the 2016 Anti-Avoidance Package the need to have a fairer, simpler, and more effective corporate taxation in the EU. Both documents aim to have a common approach to third country jurisdictions on tax good governance matters. The Communication refers to an External Strategy for Effective Taxation stating that:

> In order to ensure a level playing-field, the EU also needs stronger instruments to respond to third countries that refuse to respect tax good governance standards. The European Parliament, many Member States and stakeholders have expressed strong support for a single EU framework for addressing tax good governance concerns with third countries. A common EU approach in this area would have a powerful dissuasive effect and prevent companies from abusing mismatches between the different national systems. It would also give international partners greater clarity on the EU's expectations in this field and would reduce unnecessary administrative burdens for businesses. It will also ensure that the specific situation of third countries, particularly developing ones, is consistently taken into account.[11]

One of the measures to ensure this level playing field is the introduction of the EU Standard of Tax Good Governance. This Standard was first introduced in 2008 comprising of transparency, exchange of information, and fair taxation. Since 2018, the

[10] Communication from the Commission to the European Parliament and the Council on an External Strategy for Effective Taxation, 2016, Section 5.

[11] Ibid. at 1.

Standard also includes the BEPS 4 Minimum Standards to tackle aggressive tax planning. This Standard is included in *formal trade and partnership agreements* and as a condition for the country to receive EU development funds.

Another consequence is the use of the criteria of the EU Standard of Tax Good Governance by the Code of Conduct Group to decide on the blacklisting of non-cooperative jurisdictions outside the EU (third countries). For countries that have been blacklisted, there could be (legal) consequences such as denying access to EU funds, and the imposition of additional transparency requirements (schemes automatically reported to tax authorities) and prioritization for screening in EU's money laundering listing.[12]

Some of the reasons mentioned by the EU to include developing countries in this Standard is to encourage countries including developing countries to abide by international tax standards and to join international standard setting bodies. The EU also states that 'By raising the global level of tax good governance, the EU list offers important benefits to developing countries too, as they are disproportionately impacted by international tax abuse and illicit financial flows'.[13]

3.3 Analysis

The content of the EU Standard of Tax Good Governance is addressed in different provisions of the negotiated EU-ACP Post-Cotonou Agreement.[14] In some provisions reference is made to the principles of good governance in the tax area, and in others to fairness, transparency, efficiency, and effectiveness of their tax systems. The interpretation of these provisions can be very extensive if the wording of the agreement is broader. This is the case, for instance, for fairness that has been discussed extensively by scholarship without having a definitive conclusion on the meaning of fairness (Burgers and Mosquera Valderrama 2017; Debelva 2018).

The table below will provide an overview of the main provisions in the agreement to illustrate how the EU introduces these principles of tax good governance, fairness, transparency, efficiency, and effectiveness in the EU-ACP Post-Cotonou Agreement.

[12] https://www.consilium.europa.eu/en/policies/eu-list-of-non-cooperative-jurisdictions/ Accessed 27 November 2023.

[13] Ibid.

[14] Partnership agreement between the [European Union and its Members Sates], of the one part, and Members of the Organization of African, Caribbean, and Pacific States, of the other part (hereinafter Negotiated Agreement). https://international-partnerships.ec.europa.eu/system/files/2021-04/negotiated-agreement-text-initialled-by-eu-oacps-chief-negotiators-20210415_en.pdf Accessed 27 November 2023.

Provisions of EU-ACP Post-Cotonou Agreement
Art. 12 Good governance *6. The Parties recognize and commit themselves to implement the principles of **good governance in the tax area**, including the global standards on transparency and exchange of information, fair taxation and the minimum standards against base erosion and profit shifting (BEPS). They shall promote good governance in tax matters, improve international cooperation in the tax area, and facilitate the collection of tax revenues. They shall cooperate to enhance capacity to comply with these principles and standards and reap the benefits of a thriving rules-based financial sector. They agree to engage in timely partnership dialogue at bilateral and international levels on tax matters.*
Art. 32. Public finance and financial governance *3. The Parties shall take measures to combat illicit financial flows, tax fraud and tax evasion, and reduce opportunities for tax avoidance, including through bilateral and multilateral consultations. The Parties shall apply the **principles of good governance in the tax area** in,* inter alia*, enacting legislation, developing comprehensive policies, adopting concrete measures, and strengthening relevant institutions and mechanisms.*
Art. 41 Financial governance *3. The Parties shall cooperate to combat tax evasion, tax avoidance, and illicit financial flows, and ensure the efficiency, effectiveness, transparency, and **fairness of tax systems.***
Art. 72 Financial governance *3. The Parties shall combat tax fraud, tax evasion, tax avoidance, and illicit financial flows and shall strengthen asset recovery. They shall work towards ensuring the efficiency, effectiveness, certainty, transparency, and **fairness of tax systems**.* *4. The Parties shall take concrete measures, including by enacting legislation, and shall strengthen relevant institutions and mechanisms to implement the principles of **good governance in the tax area**.*
Art. 83 Domestic public resources *2. The OACPS Members that are parties to this Agreement shall endeavour to enhance revenue collection through modernized tax systems, improved tax policy, more efficient tax collection, and strengthened and reformed tax administration. They shall work towards improving the **fairness, transparency, efficiency, and effectiveness of their tax systems**, including by broadening the tax base and continuing efforts to integrate the informal sector into the formal economy in line with country circumstances. They shall strengthen fiscal legitimacy by enhancing the efficiency and effectiveness of their public expenditure.* *3. The Parties agree to increase efforts to combat illicit financial flows with a view to eradicating them, to cooperate in the recovery of lost assets and capital, and to strengthen good practices on assets return in order to foster sustainable development. They shall promote anti-corruption, anti-fraud, and anti-money laundering measures and **undertake measures to tackle tax avoidance, tax evasion, and other harmful tax practices**, through increased international cooperation, improved domestic regulation as well as strengthened capacities and exchange of information.* *4. The Parties shall enhance and cooperate to strengthen **good financial and tax governance**, transparency, and accountability. They commit to scaling up international tax cooperation in an inclusive, fair, and transparent manner.*

3.4 Some Observations

On the basis of the provisions cited above, several observations can be made in terms of scope of the EU Standard of Tax Good Governance. It should, however, be noted that the observations below are made without prejudice to the goal of ensuring

good tax governance. They should thus be seen as observations and recommendations from a purely legal (and hence not ideological or political) perspective.

First, given its nature of a multilateral agreement, it is in line with expectations that the provisions are directed towards both groups of contracting parties (i.e. the EU countries and the ACP countries).[15] The introduction *casu quo* adherence to the Standard is thus negotiated on a reciprocal basis. It is, however, to be expected that in practice, due to the status of their respective legal systems, the main burden will fall on the legislator and/or tax administrations of the ACP countries. The provision on Domestic Public Resources does, however, contain a subjective qualification of the standard, by making the efforts to integrate the informal sector into the formal economy dependent on the "*country circumstances*".[16]

The second main comment concerns uncertainties and divergences in the material scope of the treaty. In other words: the precise contours of the standard are unclear in several ways. First, throughout the text of the agreement, reference is repeatedly made to a group of four core criteria: efficiency, effectiveness, transparency, and fairness. These core obligations are further supplemented by several other—admittedly related—criteria and good practices, such as: implementation of the global standards on exchange of information, capacity enhancement in the hands of the (tax) administration, enhancing legitimacy, combatting tax fraud/evasion/avoidance and other harmful tax practices, strengthening fiscal legitimacy, etc. It is uncertain why these criteria differ among the provisions in the agreement and whether they are to be seen as *"acquis"* in terms of the Standard.

A third comment is with respect to the precise contours of the abovementioned obligations. Even among the four core criteria (efficiency, effectiveness, transparency, and fairness), there is considerable amount of discussion among authors on the precise content of these norms. In fact, the authors submit that it would be nearly impossible for a tax system to reach these goals simultaneously. For example, a very simple and efficient tax system that is easy to administer (by, e.g., applying a single tax rate for all types of income and all taxpayers) may not adequately consider all personal factors of taxpayers and therefore might not comply with the criterion of fairness. On the other hand, if a tax system includes highly complex rules to accommodate all personal circumstances that could potentially influence the tax burden, this system is likely to be too intricate to be practically executable.

Lastly, complying with all these requirements, which are drafted as "open norms" or even as performance indicators would arguably require a complete overhaul of some of the countries' (tax) systems involved. Despite the nature of the agreement as an international treaty, for which it is essential that the parties' reciprocal obligations are clear-cut in order to avoid disputes, there are several uncertainties and inconsistencies in the way these obligations are formulated.

[15] Article 12.6. of the Agreement *supra* n. 53.

[16] Article 83.2. of the Agreement *supra* n. 53.

4 Conclusions and Recommendations for Further Research

The aim of this contribution was to study the legal transplant of EU Standards in non-EU countries. These standards are either voluntarily implemented by the country or, alternatively, imposed by the EU as part of the *acquis communautaire* or when concluding agreements (e.g. trade, economic, or partnership) with these countries.

The first part of this contribution addresses the theoretical background of legal transplants, explaining what legal transplants are, why and how legal transplants take place.

The second part contains an analysis of the 2021 post-Cotonou Agreement; it seems that the EU has imposed several standards on the treaty partners. However, it seems that diverging wording is used throughout the treaty. In addition, several requirements are drafted as "open norms" which would arguably require a complete overhaul of some of the countries' (tax) systems involved. Despite the nature of the agreement as an international treaty, for which it is essential that the parties' reciprocal obligations are clear-cut in order to avoid disputes, there are several uncertainties and inconsistencies in the way these obligations are formulated.

It is evident that there is a need for further research on the legal transplant of EU standards in non-EU countries. To guide future researchers, the authors propose exploring the following topics, which could be of relevance:

(i) Comparing different methods of legal standard transplantation in various types of agreements (tax, trade, and investment).
(ii) Conducting an empirical analysis of the practical impact of such agreements and how they are implemented by relevant stakeholders.
(iii) Evaluating the effectiveness of transplanted norms in their practical application.
(iv) Examining how norms in international agreements are interpreted, monitored, and enforced in practice.
(v) Conducting a historical analysis of the evolution of legal transplants in the realms of tax, trade, and investment over time.
(vi) Assessing the impact of legal transplants on the economic development of the countries involved.
(vii) Investigating the voluntary adoption of legal transplants in these areas by third countries and exploring the reasons behind such decisions.

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Part IV
Reforming Global Governance

Introduction to Part IV

Irma Mosquera

This Part addresses the reform of global governance that is currently taking place at international, regional, and domestic level. In this Part, attention is given to tax incentives, green transition, and to the design of new regional (i.e., Africa) and international (United Nations) governance structures.

The topic of tax incentives influences global governance since countries are in the process of revisiting their own rules to align their tax incentives with the global minimum tax (Pillar Two) and their compatibility with countries' investment and trade commitments. These changes present new challenges to policy makers when revisiting or drafting new provisions in their bilateral investment treaties and trade agreements.

The topic of green transition also influences global governance since countries are now in the process of introducing new rules to deal with climate change and to otherwise facilitate this transition. Policy makers will need to consider the current developments at the level of the European Union Carbon Border Adjustment Mechanism (CBAM) as well as the introduction of tax incentives by countries meant to facilitate the green transition.

The topic of taxation of the digital economy has resulted in countries introducing domestic rules (e.g., Digital Service Taxes) and participating in international initiatives such as the taxation of highly digitalized business (Pillar One). The introduction of Digital Service Taxes has trade implications that will need to be considered by policy makers.

To address all these topics, new governance structures have been proposed, for instance centering the African Union as a united front on the taxation of the digital

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economy. Another proposal is to elevate the United Nations as the international organization legitimized to serve the needs of developing countries and to provide an inclusive and effective participation in agenda setting and decision-making process.

By calling to strengthen the role of the United Nations and the African Union as the institutions that can contribute to enhance governance in developing countries, this part addresses a change of paradigm in international tax law making which, as we saw in prior Parts of the book, has been dominated by the OECD and the G20 when dealing with international tax initiatives to tackle base erosion profit shifting, to facilitate exchanges of information, to tax highly digitalized business, and to introduce a global minimum tax.

This is also the result of regional and international developments that questioned the role of the OECD and advocated for strengthening regional cooperation as well as giving a more important role to the United Nations in international tax law making. At the regional level, two examples are the creation in 2020 of a Special Technical Committee within the African Union under the theme "Securing Africa's Taxing Rights, Stemming Illicit Financial Flows and developing payment system for AfCFTA" and the introduction in July 2023 of a Regional Tax Cooperation Platform for Latin American and the Caribbean (CEPAL).

At international level, one example is the adoption by the UN in November 2022 of a resolution to develop a globally inclusive new tax framework. This resolution was followed in November 2023 by another UN Resolution to develop an International Tax Framework Convention under the auspices of the UN. This Resolution was initiated by the African Group and supported by a majority of developing countries. As a result, an ad hoc intergovernmental committee has been mandated to develop the terms of reference for the development of such convention with finalization expected by mid-2024.

All these developments show that global governance is being reformed, and that these reforms need to take a holistic approach to deal with tax, trade, and investment, to take into account the differences between developed and developing countries. The chapters in this Part contribute to provide solutions to policy makers at international, regional, and country level to address these new changes.

Chapter "Optimizing Policy Energies: The Role of Tax Incentives in International Trade and Investment" by Julien Chaisse addresses tax incentives and their impact on trade and investment. In this chapter, the author provides an analysis of the topic of tax incentives within the current international framework governed by Bilateral Investment Treaties and World Trade Organization Agreements. The aim is to provide insights into designing tax incentives regimes that strike a balance between promoting investments, safeguarding trade interests, and ensuring equitable outcomes. This author concludes with some recommendations when introducing changes to tax incentives in order to take into account the interplay among international legal frameworks, national policy objectives, and strategic choices in economic development paths.

Chapter "Tax, Trade and Investment for Green Transition" by Suranjali Tandon addresses the need to balance the introduction of tax incentives and the implementation of carbon pricing, in order to encourage green transition. For this purpose, the author provides an analysis of two instruments, the EU's CBAM and the Inflation Reduction Act (IRA). The chapter starts with analyzing whether the Paris Agreement is binding, and thereafter, the main features of design of the CBAM as adopted in the EU Emission Trading System Directive. In addition, this chapter addresses the introduction of tax incentives to encourage green sectors and its compatibility with Pillar 2. By analyzing the topic of tax incentives, this contribution provides a critical reflection to the policy choices when introducing tax incentives to encourage green transition, including also the introduction in the United States of the Inflation Reduction Act and its consequences for developing and developed countries. This chapter concludes with a warning to countries to be careful in their policy design to ensure that the shift to renewables is not at the costs of economic growth, and to keep in mind when introducing measures that developing countries need to receive their fair share of climate finance due to the changes in the industrial policy.

Chapter "Breaking the Cycle of Domination in Global Tax Governance: Africans Defying Asymmetries and Seizing Opportunities" by Lyla Latif addresses the current changes in international tax law making by discussing the role of the United Nations and the long-standing historical inequalities and asymmetries (technical, capacity, and resource) faced by African nations. This chapter addresses the new role of African Nations that challenge these inequalities by proactively participating in global tax discussions as it has been seen in the adoption of the UN Resolution to develop a global inclusive new tax framework. This chapter addresses some of the international tax challenges faced by African countries but also applicable to developing countries in general such as the current rules for reallocation of taxing rights, the arm's length principle, the automatic exchange of information, the proposed rules for digital taxation, and the rules introducing a global minimum tax. In addition, this chapter addresses the demanding need of developing countries to increase administrative capacity and resources to implement these rules. Finally, this chapter concludes with an analysis of the three options provided in July 2023 in the "Promotion of inclusive and effective international tax cooperation at the United Nations" Report addressed to the UN Secretary General before adopting the UN Framework Convention option.

Chapter "Decision Making in a Proposed African Union Tax Governance Structure" by Afton Titus argues for the creation of an African Structure within the African Union to address the international tax challenges and to coordinate the implementation of policies to deal with these challenges. The focus is on the taxation of the digital economy as an illustrative example on how regional tax organizations such as the African Tax Administration Forum, Regional Economic Agreements such as the East African Community and the Southern African Development Community can contribute to build continental coherence to improve the participation of African countries in the international tax system, and to build a common

continental position in Africa. The author also highlights the recent creation of the African Continental Free Trade Area (AfCFTA) Agreement which can facilitate greater integration in Africa without erasing the good work that regional economic agreements have made across the continent.

Optimising Policy Synergies: The Role of Tax Incentives in International Trade and Investment

Julien Chaisse

1 Introduction

There is increasing competition among nations to attract foreign direct investment (FDI) and strategic industries through incentives. The latest data underscore the scale of the United States' incentives, with over $54 billion granted since 2020, surpassing any other country (Irwin-Hunt 2017).[1] The transparency and accessibility of information on incentives have contributed to the success of the United States in attracting FDI and creating a competitive investment environment. These data underscore the importance of understanding the dynamics of tax incentives and their impacts on trade and investment, particularly in the context of redefining global governance.

In the broader context of international trade and investment, understanding how fiscal tools such as tax incentives influence global economic dynamics is crucial. This chapter discusses this critical topic in detail. As part of a comprehensive exploration of the legal, economic, and strategic aspects of international commerce, this chapter focuses on the nuanced and intricate relationship between tax incentives and FDI, the international legal framework governing them, and their practical

[1] The data also reveals the global trend of governments offering increased support to strategic industries, particularly in response to supply chain disruptions caused by the Covid-19 pandemic. As countries vie to capture investments in critical sectors like electronics, semiconductor, and green technologies, tax incentives have become crucial tools in attracting and retaining investments. The magnitude of incentives offered highlights the importance placed on stimulating economic growth, job creation, and technological advancements.

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implications for nations. It takes into account the multi-faceted role tax incentives play in shaping global trade and investment patterns, and the balancing act that countries must comply with international regulations while meeting domestic economic objectives. By dissecting complex international trade laws and conventions and their interactions with national tax-incentive policies, this chapter aims to provide insights into tax incentives as a powerful tool in the intricate game of global trade and investment.

The complex dance of global trade and investment is governed by a number of regulatory organisations and legal frameworks, each of which has a different weight on the moves and countermoves of states. Tax incentives are a key component of this dance, because they are fiscal tools frequently used to catalyse FDI (Kerner 2018). These incentives not only aid in bringing in and keeping investment, but also work as tactical tools for attaining macroeconomic objectives and promoting economic growth.

The concept of tax incentives encompasses a wide array of fiscal tools, from direct tax breaks and credits to indirect subsidies and grants, all of which aim to make investment propositions more attractive. The role of tax incentives in trade and investment cannot be overstated. They can serve as potent tools for nations to navigate the complex and ever-evolving landscape of global trade and investment. While tax incentives can significantly influence investment decisions, their effectiveness often depends on a variety of factors, such as the stability of the policy environment, the competitiveness of the incentives offered, and the broader economic and business climate of the offering nation. By carefully crafting and deploying tax incentives, countries can not only attract capital and technology, but also stimulate job creation, drive economic growth, and even influence the behaviour of investors.

The complexity of designing and implementing tax incentives extends beyond traditional frameworks. While Bilateral Investment Treaties (BITs), the World Trade Organization's Agreement on Subsidies and Countervailing Measures (ASCM), and Trade-Related Investment Measures (TRIMs) dictate much of the international legal landscape, national tax rules and stabilisation contracts add another layer of intricacy. This discussion diverges from the contemporary focus on Pillar 2, offering a fresh perspective. Understanding this broader context is crucial for policymakers and tax administrations, especially those primarily exposed to discussions centred around Pillar 2. This chapter aims to broaden the discourse, encouraging consideration of a wider range of factors influencing the effectiveness and strategic deployment of tax incentives in achieving policy objectives.

The methodology of this study harnesses a qualitative approach, entailing an interpretive analysis of international legal texts such as BITs, TRIMs, and ASCM. A comparative lens was applied to examine national practices, leading to a richer, contextually nuanced understanding of how different countries utilise and balance tax incentives and performance requirements. The historical analysis further refines this methodology, as demonstrated by the examination of the Republic of Korea's tax-incentive policies and their effects on trade and investment. This fusion of conceptual frameworks and methodological tools provides a robust foundation for a

comprehensive exploration of the complex interplay among international legal frameworks, national policy objectives, and strategic choices in economic development paths.

This chapter provides an in-depth and comprehensive analysis of the role and impact of tax incentives on trade and investment. It delves into the international legal framework governing tax incentives, explores the concept of performance requirements and their role in tax-incentive policies, and examines how countries can navigate the complex interplay between investment, tax, and trade policies. The chapter also contemplates the future of tax incentives and performance requirements in trade and investment, and proposes ways for countries to develop robust, country-specific tax incentive regimes that balance global trade norms with local economic needs and priorities. The goal is to provide a rich, nuanced, and practical understanding of tax incentives and their role in the broader context of international trade and investment.

2 The International Legal Framework Governing Tax Incentives

Regulation and protection of foreign investments are paramount in the realm of international investment relations. BITs serve as a crucial legal framework for safeguarding investments by providing standards of protection, promoting investment, and facilitating dispute resolution. However, the delicate balance between protecting investor rights and preserving the policy autonomy of host states, particularly regarding tax incentives, presents a complex challenge. Similarly, TRIMs under WTO and ASCM provide further insight into the interplay between trade, investment, and domestic policy objectives, including tax incentives.

This section explores the international legal framework governing tax incentives, focusing on the complexities and tensions arising from the BITs, TRIMs, and ASCM. The main legal thesis reconciles the objectives of investment protection and host countries' policy needs regarding tax incentives. This emphasises the need for legal innovation to strike a balance between safeguarding investors' rights and enabling host countries to adapt their tax-incentive policies in accordance with their evolving development objectives. To effectively address these complex issues, this study follows a logical progression. First, it provides a descriptive account of the international legal framework established by the BITs, TRIMs, and ASCM, elucidating the purpose and inherent tensions within each instrument. Second, it undertakes an analytical exploration of the challenges posed by tax incentives, focusing on the potential conflict between investment protection and the policy autonomy of host countries. Third, it proposes legal innovations and solutions that could reconcile these conflicting objectives, such as including explicit provisions in BITs or developing a nuanced understanding of TRIMs and ASCM. Finally, it will consider the broader implications and future prospects for international investment law and

the design of tax incentives, acknowledging the need for dynamic and responsive frameworks that align with evolving global demands.

2.1 Deciphering BITs: Implications for Tax Incentives

BITs play an integral role in regulating international investment relations by establishing a legal framework to protect foreign investments. Broadly speaking, these treaties typically contain provisions that stipulate standards for investment protection, investment promotion, and mechanisms for the settlement of disputes between investors and host states. The fundamental premise of these treaties is to foster an investment-friendly environment, instilling confidence and predictability in investors by ensuring legal protection against expropriation and guaranteeing fair and equitable treatment.

However, it is essential to acknowledge the innate tension within the architecture of BITs, where the delicate balance between safeguarding investors' rights and allowing host nations to regulate the public interest comes into sharp focus. This aspect is particularly salient when scrutinising the dynamics of tax incentives as a tool to attract FDI. On the one hand, BITs are expected to provide a stable, transparent, and secure investment climate that invariably includes the predictability of tax policies. On the other hand, host nations, especially those that are still developing, must retain their sovereign rights to adapt their tax policies in accordance with their domestic economic needs and development objectives.

The ambivalent nature of BITs, particularly in relation to tax incentives, necessitates a deeper legal analysis of the treaty framework. For instance, the "fair and equitable treatment" clause prevalent in many BITs can be construed as safeguarding investors against abrupt modifications in tax incentives, considering such alterations could undermine their legitimate expectations of the investment environment in the host state. Nonetheless, this expansive interpretation might constrain the host state's autonomy, impeding its ability to leverage tax incentives for economic development, job creation, or technological transfer. To balance investor protection with state policy flexibility, it might be prudent to explore the incorporation of a specific clause in BITs that explicitly permits alterations in tax incentives without breaching the "fair and equitable treatment" standard, thus ensuring coexistence of investor rights and state policy objectives. A cutting-edge legal approach to address the tension between the "fair and equitable treatment" clause in BITs and the flexibility of states to modify tax incentives could involve crafting a "dynamic incentive adjustment" (DIA) clause. For instance, "1. *Recognizing the dynamic nature of economic and social conditions, the Host State reserves the right to modify tax incentives, provided such modifications are made in accordance with the principles of transparency, predictability, and non-discrimination. 2. Prior to implementing changes to tax incentives, the Host State shall engage in a consultative process with affected investors, providing reasonable notice and an opportunity to submit comments. Any changes to tax incentives shall be implemented in a gradual manner, allowing*

sufficient time for affected investors to adapt their operations accordingly. 3. The Host State shall ensure that modifications to tax incentives do not constitute arbitrary or discriminatory treatment of investors. 4. This provision aims to balance the legitimate expectations of investors with the Host State's need to respond to evolving policy requirements. 5. Disputes arising from the modification of tax incentives under this Article shall be subject to arbitration in accordance with the dispute resolution provisions of this Treaty").

This DIA clause would explicitly recognise the state's right to adapt tax incentives in response to evolving economic and social needs, while simultaneously ensuring that such changes are conducted in a transparent, predictable, and reasonable manner. This approach would legally formalise the expectation that tax incentives may evolve, subject to certain safeguards that protect investors from arbitrary or discriminatory changes. This clause could include mechanisms for prior consultation with affected investors, clear guidelines for changes, and possibly a phased implementation to mitigate sudden impacts. The key is to strike a balance that respects the legitimate expectations of investors while preserving the policy space of states. This approach would necessitate careful legal formulation to avoid undermining the treaty's protective essence while allowing necessary policy adjustments.

The extent of their influence on the global investment environment and the careful equilibrium maintained between investor protection and host state policy autonomy is significant. This inherent complexity indicates that the formulation of bilateral investment treaties (BITs) must be attuned to the evolving relationship between investment law and the domestic policy priorities of states, particularly regarding tax incentives.

2.2 TRIMs: Understanding Its Scope and Impact

TRIMs under the purview of WTO provide an essential framework for understanding the interactions between trade, investment, and domestic policy objectives. A detailed analysis of TRIMs offers insight into the scope and limitations of these measures and their implications for national policies on tax incentives.

The Agreement on TRIMs prohibits investment measures that are inconsistent with the principles of national treatment and quantitative restrictions under the General Agreement on Tariffs and Trade (GATT). Specifically, it proscribes measures that require foreign investors to purchase or use domestic goods—known as "local content requirements"—and those which limit the importation of products based on the level of exportation, often referred to as "trade balancing requirements".

However, this broad prohibition raises several legal and policy questions, particularly regarding tax incentives aimed at promoting domestic development objectives. Many countries use tax incentives to encourage foreign investors to contribute to local economic development through activities such as training local employees or conducting research and development (R&D) (Perrone 2023). However, these performance requirements, even though they may serve legitimate policy

objectives, could potentially run afoul of the TRIMs Agreement if they are deemed to discriminate against foreign goods or constitute a disguised restriction on trade.

This dilemma reflects a broader tension within the international trade and investment regime—the need to reconcile the liberalisation objectives of the WTO with the right of countries to regulate the public interest (Calamita 2020). One possible legal innovation to navigate this tension could be to carve out specific exceptions in the TRIMs Agreement for certain types of performance requirements linked to tax incentives, especially in developing countries.

For instance, the TRIMs Agreement could be amended or interpreted in a way that allows countries to impose performance requirements related to training local employees or R&D, provided that these requirements do not constitute arbitrary or unjustifiable discrimination. Such an approach would recognise the crucial role that foreign investment can play in promoting local economic development and technological advancement.

Another possible approach could be to develop a more nuanced understanding of what constitutes "discrimination" under the TRIMs Agreement. For example, performance requirements linked to tax incentives might be considered non-discriminatory if they apply equally to domestic and foreign investors or if they aim to address market failures or promote public goods.

In conclusion, the TRIMs Agreement presents an interesting and complex legal landscape that involves balancing the imperative of trade liberalisation against the rights and policy needs of individual nations. Understanding and interpreting this balance, particularly in the context of tax incentives and performance requirements, provide fertile grounds for novel and creative legal thinking in the realm of international trade and investment law.

2.3 Analysing the ASCM: Tax Incentives and International Trade

ASCM forms a core part of WTO institutional structure, establishing rules on the use of subsidies and the application of countervailing measures to counter the negative effects of those subsidies. As such, ASCM is an instrumental legal instrument for understanding the permissible scope and boundaries of tax incentives under international trade law.

ASCM distinguishes between prohibited, actionable, and non-actionable subsidies, with the latter category removed since 2000. Prohibited subsidies are contingent upon export performance or the use of domestic goods over imported goods. Meanwhile, actionable subsidies, which are not explicitly prohibited, can still be challenged if they adversely affect the interests of other WTO members (Crochet and Hegde 2020).

At the intersection of tax incentives and the ASCM, the question emerges: to what extent can tax incentives constitute subsidies that might fall a foul of the

ASCM? ASCM defines a subsidy as a financial contribution by a government that confers benefits. In many respects, tax incentives can easily fit this definition, particularly if they significantly reduce an enterprise's tax burden in a manner that is not typically available to other entities. However, the nuanced interpretations of "financial contribution" and "benefit" in the context of tax incentives can lead to different legal conclusions. Different legal conclusions can arise because the interpretation of "financial contribution" and "benefit" in the context of tax incentives hinges on complex criteria, such as the specificity of the incentive to certain enterprises or industries, and the degree of economic advantage conferred, making the assessment under ASCM highly contextual and variable.

One innovative approach would be to argue that tax incentives linked to performance requirements, such as R&D, may be justified under a broad interpretation of ASCM's provisions relating to the development of disadvantaged regions and the correction of market inefficiencies (Shadikhodjaev 2021). Arguably, R&D tax incentives can be seen as a tool to correct market failures due to underinvestment in innovation caused by firms' inability to fully capture the benefits of their R&D activities.

Furthermore, a comprehensive interpretation of ASCM must consider its interface with other international obligations, notably the international tax regime and BITs. Legal issues may arise if the use of tax incentives under these regimes conflicts with obligations under ASCM. As such, legal reconciliation between these disparate yet interconnected regimes is necessary, potentially calling for a new legal paradigm or normative framework.

In conclusion, the legal complexities of the ASCM and its interplay with tax incentives provide a rich terrain for legal exploration and innovative thinking. The evolving nature of global trade and the corresponding demand for nuanced policy measures requires a dynamic understanding of these legal instruments. A more holistic understanding of ASCM could guide the design of future tax incentives, ensuring compliance with international trade law while effectively serving domestic policy objectives.

3 Performance Requirements and their Role in Tax-Incentive Policies

Performance Requirements play a crucial role in shaping the dynamics of FDI and the effectiveness of tax-incentive policies. These requirements, often embedded in BITs, impose certain conditions on investors regarding their investment operations. However, the presence of performance requirements can present legal challenges as they may conflict with the principles of free trade and non-discrimination. Defining and interpreting performance requirements within the context of BITs requires innovative legal thinking to strike a balance between investors' rights and the policy objectives of host countries.

The objective of this section is to understand the nature and implications of performance requirements in BITs and to explore their role in tax-incentive policies. The main legal thesis views performance requirements as potential leverage points for host countries to negotiate more favourable investment conditions. It advocates a rethinking of performance requirement clauses, aiming for more flexible and adaptable formulations that align with the economic and social objectives of host countries while remaining within the bounds of international law. To effectively address the complexities surrounding performance requirements and their interplay with tax incentives, this article follows a logical progression. First, it provides a descriptive account of performance requirements in BITs, explaining their purposes, potential conflicts, and legal uncertainties. Second, it undertakes an analytical exploration of innovative approaches to performance requirements, highlighting the need for more flexible formulations that better balance the rights and obligations of investors and host countries. Third, it examines the interdependence of tax incentives and, emphasising the importance of an integrated approach to their design and implementation. Finally, it discusses the lessons learned and the implications for modern BITs, including the need for greater flexibility, periodic review clauses, and enhanced transparency and public participation in treaty negotiations.

3.1 Understanding Performance Requirements in BITs

Performance Requirements in BITs are legal clauses that require investors to meet certain conditions related to the operation of their investments. This can include mandates on domestic content, technology transfer, export quotas, and specific levels of employment. Their presence in BITs can shape the pattern of FDI, balance the benefits between the host and home countries, and have a profound impact on the effectiveness of tax incentives designed to promote investment.

However, these requirements can lead to a significant legal quandary. Certain types of performance requirements may potentially contradict the principles of free trade and non-discrimination embedded in BITs and the broader investment law architecture and could also infringe upon rules set by the WTO or other international agreements. Legal uncertainties may also arise regarding what constitutes a performance requirement, as the definition is subject to interpretation and varies among different BITs.

One innovative approach to address these challenges is to conceive performance requirements not as impediments to investment but as potential leverage points for host countries to negotiate more favourable investment conditions. To this end, a rethinking of typical performance requirement clauses within BITs may be needed, with an emphasis on more flexible and adaptable formulations. This could include specifying particular scenarios or conditions under which certain performance requirements can be invoked, or designing performance requirements that align more closely with the host country's economic and social objectives while ensuring that they remain within the bounds of international law.

Furthermore, the performance requirements and tax incentives should not be viewed in isolation. The effectiveness of tax incentives can be significantly influenced by the presence and design of performance requirements. For instance, tax incentives aimed at promoting local industry could be undermined if the corresponding BIT allows investors to import all their materials from abroad without any restrictions. The interplay of tax incentives and performance requirements necessitates a more integrated approach to designing these measures, keeping in mind their mutual influence and overall investment policy objectives.

In the final analysis, a more nuanced understanding of performance requirements in BITs and their interplay with tax incentives can open new horizons in the legal and policy discourse on international investment. Through innovative legal thinking, performance requirements can serve as effective tools for balancing the rights and obligations of foreign investors and host countries, thereby contributing to more equitable and sustainable investment practices.

3.2 Shaping Modern BITs: Lessons and Future Directions

As we venture into the intricacies of BITs and their embedded performance requirements, it becomes imperative to extract lessons and discern the implications that can shape the fabric of contemporary BITs. The synthesis of tax incentives with performance requirements in BITs, although complex, provides fertile ground for innovation in international law and investment policy.

While BITs have historically been celebrated for fostering FDI, there is an emerging consensus on the necessity to update their traditional models. These classic BIT formulations, with their extensive investor protections, may no longer align with the evolving economic and social priorities of host countries. This reassessment becomes particularly relevant when considering the complexities of tax incentives, performance requirements, and broader societal goals. Aligning with the earlier discussions on modernising clauses related to "fair and equitable treatment" and "indirect expropriation", this reevaluation of BITs suggests a holistic approach to revamping their text to better serve contemporary global investment governance. This perspective advocates for BITs that not only protect investors but also respect the dynamic policy objectives of host states.

A central lesson is the need for greater flexibility and adaptability in BITs. In many BITs, the legal language often leans towards investor protection, with less consideration given to the policy space required by host countries to implement their economic strategies, including the use of tax incentives and performance requirements. Modern BITs could adopt more balanced provisions that recognise the legitimate rights of host states to regulate investments alongside the rights of investors (Henckels 2016). Such adaptations could provide a more conducive legal framework for countries to design and implement effective tax incentives without infringing on their BIT obligations.

Another innovative idea is the integration of periodic review clauses into BITs. This would allow for the amendment of certain terms in light of evolving economic circumstances or policy priorities. This could involve rethinking performance requirements and tax incentives based on their efficacy, economic impact, and compliance with international commitments. A dynamic review process could inject much-needed fluidity into the rigid structure of BITs, enhancing their relevance in the rapidly changing economic landscape.

Finally, there is a growing call for transparency and public participation in BIT negotiations. The implications of BITs on domestic policy, including tax incentives and performance requirements, necessitate broader societal input in their formulation. Incorporating stakeholder consultations into BIT negotiations could ensure that the resulting treaties are not only legally sound, but also politically sustainable and socially acceptable (Sauvant and Nolan 2015). Transparency and tax expenditure are currently of great importance. The work conducted by Agustin Redonda and CEP highlights the significance of not only transparency in negotiations but also the publication of tax expenditure reports in reformulating tax incentives.

In conclusion, experiences with performance requirements and tax incentives in the context of BITs provide valuable lessons for modern treaty-making. By adopting a more flexible, dynamic, and inclusive approach, BITs can better serve their role in fostering sustainable and mutually beneficial investment relationships.

4 Developing the Right Institutions for Tax Incentives and Performance Requirements

Developing effective institutions for tax incentives and performance requirements is crucial in international trade and investment (Meyer and Park 2018; Avi-Yonah 2023). Recognising the diverse legal, economic, and social characteristics of each nation, a country-specific approach is needed to tailor the incentives and requirements to specific contexts. This requires innovative legal thinking and a comprehensive understanding of international legal obligations to strike a balance between state interests, investor rights, and global commitment.

The objective of this section is to explore the development of right institutions for tax incentives and performance requirements. The main legal thesis advocates for a country-specific approach that aligns tax incentives and requirements with each nation's unique economic objectives, developmental needs, and global commitments. This involves innovative ideas, such as outcome-based incentives, ESG integration, transparent evaluation mechanisms, and a comprehensive legal and economic mapping tool. To effectively address the challenges and opportunities surrounding the development of institutions for tax incentives and performance requirements, this study will follow a logical progression. First, it provides a descriptive account of the need for country-specific tax incentive regimes, explaining the limitations of a one-size-fits-all approach, and highlights the importance of

aligning incentives with national goals. Second, it undertakes an analytical exploration of innovative legal ideas, including outcome-based approaches, ESG integration, and transparent evaluation mechanisms. This analysis emphasises the potential benefits and challenges associated with each idea. Finally, we discuss the implications and consequences of implementing these innovative legal concepts considering their impact on investment practices, sustainable development, and the overall balance between state and investor interests.

4.1 Crafting Incentives for Local Economic Contexts

Identifying appropriate incentives and requirements for local economies requires a nuanced understanding of the legal and economic ecosystems within which these policy tools operate. In the realm of international trade and investment, a single size does not fit all. The articulation of bespoke tax incentives and performance requirements demands a granular appreciation of local socio-economic realities and strategic national objectives, as well as a thorough understanding of the overarching international legal obligations.

Under the current regime of international law, there is legal tapestry of bilateral, regional, and multilateral agreements, each bearing on the formulation of tax incentives and performance requirements. As such, a novel proposal is to develop a comprehensive legal and economic mapping tool that integrates various facets of international law (BITs and WTO agreements) and national policies (Roberts 2018). This tool can help governments identify the optimal mix of incentives and requirements that aligns with their broader socio-economic objectives while ensuring compliance with international commitments.

Appropriate incentives and requirements must also transcend the usual considerations of attracting FDI and enhancing trade competitiveness. In the contemporary context, there is an emerging need to reorient tax incentives and performance requirements towards achieving Sustainable Development Goals (SDGs) and other global commitments (Calamita 2020). Therefore, a ground-breaking legal notion would be to institutionalise the integration of SDGs into the design of these policy measures. This could involve setting legal requirements for impact assessments of the proposed incentives and requirements on SDG-related indicators, thus providing a legal impetus for policy coherence and sustainability (Voon 2017).

Furthermore, in an era of economic digitalisation and the rise of new business models, traditional forms of tax incentives and performance requirements may no longer be as effective (Avi-Yonah 2023). Innovative legal thinking is required to redefine these instruments to respond to the new realities of global business. For instance, legal scholars and policymakers could explore how digital taxation principles could be factored into the design of tax incentives to ensure that they remain relevant and effective in the digital age.

Finally, there is an untapped potential in the use of "smart" performance requirements that are tailored to the specific characteristics and development stage of

industries (Shan and Zhang 2014). This requires a more in-depth legal and economic analysis of different sectors, which could lead to the creation of a new generation of performance requirements that are not only WTO-compliant, but also more effective in fostering sustainable development (Mbengue and Schacherer 2017).

In summary, identifying appropriate incentives and requirements for local economies necessitates a multidimensional approach that combines legal insights, economic analysis, and innovative thinking. By doing so, policymakers can better navigate the complexities of international law and domestic realities, thereby creating a conducive environment for sustainable trade and investment.

4.2 Developing Country-Specific Tax Incentive Strategies

The development and implementation of country-specific tax-incentive regimes are of paramount importance in the realm of international trade and investment. A country-specific approach recognises the unique legal, economic, and social characteristics of each nation and acknowledges that a one-size-fits-all approach is inadequate for addressing the complex dynamics of global commerce (Meyer and Park 2018). To foster sustainable trade and investment, it is imperative to employ innovative legal ideas that effectively balance the interests of the state, investors, and global community.

One innovative legal idea is the introduction of tailored tax incentives that align with a country's economic objectives and development stage. Instead of adopting generic incentives, a country-specific approach would involve a careful analysis and understanding of the nation's economic landscape, industry strengths, and developmental needs. By tailoring tax incentives to address these specific factors, countries can strategically attract investments that align with their growth goals, while ensuring compliance with international legal obligations.

Another innovative legal approach involves the implementation of outcome-based tax incentives, departing from the traditional criteria-based approaches. Conventionally, tax incentives have been granted based on predetermined factors, such as the amount of investment or achievement of specific job creation targets. However, an outcome-based approach shifts emphasis towards evaluating the tangible impact and outcomes generated by the investment itself. By linking tax incentives to measurable results such as technology transfer, innovation advancements, or progress towards sustainable development goals, countries can create a powerful incentive for investors to make meaningful contributions to the economic and social advancement of the host nation. In practice, an outcome-based tax incentive system requires clear and quantifiable metrics to assess the desired outcomes. For instance, a country may establish benchmarks for technology transfer by specifying the minimum level of knowledge and technology that should be shared with local industries. The tax incentives can then be tied to the extent to which the investor achieves or surpasses these predetermined benchmarks. Similarly, innovation-focused tax incentives can be designed to reward investors based on the number of patents filed

or the successful commercialisation of research and development outcomes within the host country. Sustainable development goals (SDGs) can provide a comprehensive framework for outcome-based tax incentives (Schill and Djanic 2018). Countries can identify specific SDGs that align with their national priorities and develop corresponding indicators to measure progress. By incorporating these indicators into tax incentive programmes, investors can be incentivised to contribute to the achievement of these SDGs (Selivanova 2018). For example, an investor who actively supports renewable energy projects or implements environmentally friendly practices could be eligible for enhanced tax incentives based on their measurable contributions to SDG targets, such as clean energy production or carbon emission reduction (Rubini 2012). Robust monitoring and evaluation mechanisms are necessary to implement outcome-based tax incentives effectively (Leal-Arcas 2012). Countries would need to establish transparent reporting requirements and obligate investors to provide evidence of their progress towards predetermined outcomes (Rubini 2012). Regular assessments are conducted to measure the degree of achievement and determine the corresponding tax incentive benefits. This data-driven approach ensures that tax incentives are aligned with real-world impacts and enables policymakers to fine-tune incentive programmes based on empirical evidence and emerging trends. By adopting an outcome-based approach to tax incentives, countries can foster a meaningful and impactful investment environment. Investors are motivated to go beyond fulfilling mere quantitative requirements and instead focus on generating substantial contributions to technological advancement, innovation, and sustainable development. This approach facilitates the alignment of investor interests with the host nation's broader economic and social progress, creating a mutually beneficial relationship and promoting long-term sustainable growth.

Furthermore, the integration of environmental, social, and governance (ESG) principles into tax-incentive regimes represents an innovative legal approach. As sustainability becomes an increasingly important consideration in global trade and investment, aligning tax incentives with ESG objectives can encourage responsible investment. This could involve rewarding companies that demonstrate environmental stewardship, social responsibility, and good governance practices, with enhanced tax incentives. By integrating ESG criteria into tax-incentive regimes, countries can attract investors who prioritise sustainability and contribute positively to the host country's sustainable development goals.

Another legal idea is to establish clear and transparent guidelines for the evaluation and monitoring of tax incentives. By providing transparent criteria to evaluate the effectiveness and impact of tax incentives, countries can ensure that these measures achieve their intended goals. Regular monitoring and evaluation can facilitate adjustments to tax-incentive regimes based on empirical evidence, ensuring their continued relevance and effectiveness in supporting desired policy objectives. Additionally, establishing an independent body responsible for monitoring and reporting tax incentives can enhance accountability and strengthen the legitimacy of these measures.

Thus, the importance of country-specific tax-incentive regimes cannot be overstated in the context of international trade and investment. Innovative legal ideas

that embrace tailoring incentives, outcome-based approaches, ESG integration, and transparent evaluation mechanisms can contribute to the development of effective and sustainable tax-incentive regimes. By adopting these ideas, countries can attract investments that align with their goals, promote responsible business practices, and foster long-term economic and social development.

5 Navigating the Interplay Between BITs, the WTO, and National Policies

Navigating the complex interplay between BITs, WTO, and national policies is critical in the field of international trade and investment. The interaction between these legal frameworks shapes the design and implementation of tax incentives and requires a comprehensive understanding of their dynamics. Balancing the promotion of investments, the protection of trade interests, and compliance with international obligations is essential for creating effective and equitable tax-incentive regimes (Calamita 2020).

This section explores the interplay between BITs, the WTO, and national policies and their impact on tax incentives. The main legal thesis advocates for innovative legal approaches that enable countries to effectively navigate this interplay, ensuring compliance with international obligations while creating robust tax-incentive regimes that support economic development and attract foreign investment. To effectively address the interplay between BITs, the WTO, and national policies in shaping tax incentives, this article follows a logical progression. It begins by providing a descriptive account of the dynamics between BITs, TRIMs, and ASCM, emphasising their influence on tax incentives. This section analyses the implications and challenges of the interplay between these legal frameworks.

5.1 Analysing BITs, TRIM, and ASCM Dynamics in Tax Policy

The dynamics of BITs, TRIMs, and ASCM play pivotal roles in shaping tax incentives within the international legal landscape. Understanding the intricate relationship between these legal frameworks is essential for developing innovative approaches that strike a balance between promoting investments, safeguarding trade interests, and ensuring equitable outcomes.

BITs serve as a foundation for investor-state relations and provide a framework for foreign investment protection. They establish the rights and obligations between states and investors, including provisions related to tax incentives (Alschner and Skougarevskiy 2016). One unique legal idea is to explore the potential for BITs to incorporate provisions that explicitly recognise and support country-specific tax

incentives. Such provisions could encourage investment in specific sectors or regions identified as critical for national development, while ensuring compliance with international investment standards. This approach would enable states to design tax-incentive regimes that align with their economic goals, foster sustainable growth, and attract foreign investment in a manner that respects sovereignty.

The interplay among BITs, TRIM, and ASCM requires careful consideration when shaping tax incentives. TRIM is particularly relevant because it addresses trade-related investment measures, including performance requirements, which can affect the utilisation of tax incentives (Chaisse and Ji 2020). Innovative legal approaches could involve leveraging TRIM provisions to create synergies with tax-incentive policies. For example, establishing clear guidelines that allow performance requirements to be linked to tax incentives in a manner that balances the interests of promoting local industries while ensuring compatibility with international trade rules. In doing so, states can design tax-incentive regimes that promote both investment and trade objectives, fostering economic integration and sustainable development.

ASCM, which focuses on subsidies and countervailing measures, also influences the scope and design of tax incentives. While ASCM primarily regulates subsidies related to trade in goods, its principles can provide guidance on avoiding distortions in international trade caused by excessive or discriminatory tax incentives. An innovative legal concept is to explore the application of ASCM principles to tax incentives that directly or indirectly affect international trade, particularly in cases in which tax incentives create unfair advantages for certain industries or undermine the competitiveness of trading partners. This approach would help ensure that tax incentives are crafted in a manner consistent with the principles of fair competition and non-discrimination, preserving a level-playing field in the global marketplace.

An in-depth understanding of the complex interplay between BITs, TRIMs, ASCM is of paramount importance when it comes to shaping tax incentives that effectively promote investment, facilitate trade, and foster equitable outcomes (Shadikhodjaev 2021). Delving into these dynamics enables the exploration of innovative legal ideas that can pave the way for the development of comprehensive frameworks that not only acknowledge the importance of country-specific tax incentives but also ensure their harmonisation with performance requirements and compliance with international trade regulations (Crochet and Hegde 2020). By comprehending the intricate dynamics between BITs, TRIM, and ASCM, policymakers can identify opportunities to create robust frameworks that recognise and accommodate the unique tax incentive needs of individual countries. Such frameworks would strike a delicate balance between the autonomy of states to design targeted tax incentives that bolster their economic growth and the legal obligations and protections offered by international investment agreements. This approach acknowledges the significance of tailoring tax incentives to specific economic sectors or regions, enabling nations to strategically attract investment and stimulate the desired areas of development. To align performance requirements with tax-incentive policies, innovative legal ideas can be explored within the frameworks of BITs, TRIM, and ASCM. By leveraging the provisions and principles outlined in these

legal instruments, policymakers can establish clear guidelines linking performance requirements to tax incentives in a manner that advances both investment and trade objectives. This approach fosters economic integration and sustainable development by encouraging investments that contribute to the growth and competitiveness of local industries, while ensuring compatibility with international trade rules. By aligning performance requirements with tax incentives, countries can strike a balance that facilitates the transfer of technology, skills, and knowledge, while minimising potential distortions in global trade flows. Additionally, the principles enshrined in ASCM can serve as a valuable reference point when shaping tax incentives. While ASCM primarily focuses on subsidies and countervailing measures related to trade in goods, its fundamental principles of fair competition and non-discrimination can be extended to tax incentives that directly or indirectly impact international trade (Shadikhodjaev 2021). This broader application of ASCM principles helps ensure that tax incentives are structured in a manner that avoids unfair advantages for specific industries or regions, and maintains a level-playing field for all market participants. By adhering to the principles of fair competition and non-discrimination, countries can promote a transparent and predictable investment climate, while upholding their international trade obligations (Rubini 2012). In conclusion, a nuanced understanding of the dynamics between BITs, TRIM, and ASCM is pivotal for shaping tax incentives that effectively promote investment, facilitate trade, and contribute to equitable outcomes. Exploring innovative legal ideas within this framework offers opportunities to develop comprehensive and robust frameworks that recognise country-specific tax incentives, align performance requirements with tax-incentive policies, and ensure compliance with international trade rules. By striking a balance between the unique needs of individual nations and their international legal obligations, policymakers can design tax-incentive regimes that foster sustainable economic development and contribute to a fair and inclusive global trading system.

5.2 Harmonising Tax Incentives with International Legal Prohibitions

In the context of tax incentives and compliance with the prohibitions outlined in BITs, it is crucial to establish effective tax-incentive regimes that strike a balance between promoting economic development and adhering to international legal obligations. This requires innovative legal approaches to navigate the complexities of BITs and craft robust frameworks for tax incentives.

To comply with the prohibitions under BITs, it is essential to carefully analyse the specific provisions of each treaty and understand their implications for tax-incentive policies. By conducting a comprehensive assessment, policymakers can identify the boundaries within which tax incentives must operate to avoid contravening the obligations set forth by BITs. This analysis should consider the scope of

the prohibitions, the language used in the treaty provisions, and any exceptions or carve-outs that may be applicable.

Creating effective tax-incentive regimes involves designing mechanisms that align with the objectives of BITs, while maximising the benefits for both host countries and foreign investors. One innovative legal idea is the concept of "smart incentives", which entails tailoring tax incentive programmes to specific economic sectors, regions, or developmental goals. This approach requires a thorough understanding of the country's unique circumstances and objectives as well as careful consideration of the potential impact on international trade and investment flows (Cai 2012). By aligning tax incentives with the broader policy objectives of the host country, such as promoting sustainable development, innovation, or job creation, a more targeted and effective incentive regime can be established.

Another innovative legal approach that can be adopted in shaping tax incentives is the concept of "conditional incentives". Under this framework, tax benefits are directly tied to the attainment of predetermined and measurable outcomes, or performance benchmarks. By establishing clear criteria and implementing robust monitoring mechanisms, conditional incentives provide foreign investors with a strong incentive to actively contribute to the host country's developmental goals (Gabor 2021). With conditional incentives, the granting of tax benefits becomes contingent on the achievement of specific economic, social, or environmental targets that align with the host country's priorities. These targets can vary depending on the desired outcomes such as job creation, technology transfer, local supplier development, environmental sustainability, and regional development. By linking tax incentives to these objectives, countries can ensure that the benefits provided are directed towards activities that contribute to their broader development agendas (Cotula 2010). One of the key advantages of conditional incentives is that they promote transparency and accountability in the utilisation of public resources. By establishing clear and measurable eligibility criteria, countries can ensure that tax benefits are granted, based on tangible and verifiable results. This approach minimises the risk of misuse or misallocation of incentives, as beneficiaries must demonstrate their contribution to specified targets. Moreover, conditional incentives encourage foreign investors to engage actively in the host country's developmental agenda. By aligning their activities with predetermined targets, investors gain access to tax benefits and become key partners in achieving the goals of the host country. This promotes a collaborative approach between the government and foreign investors, fostering mutually beneficial outcomes, and enhancing the overall impact of tax incentives on the host country's development. Furthermore, conditional incentives facilitate the efficient use of public resources by ensuring that tax benefits are directed towards activities that generate desired results. By closely monitoring the progress and outcomes of incentivised projects, governments can make informed decisions about the continuation, modification, or termination of incentives based on their effectiveness in achieving set targets. This adaptive approach allows for the optimisation of incentives over time and enables policymakers to adjust their strategies to address changing economic and developmental needs.

Furthermore, it is essential to emphasise the significance of incorporating mechanisms for periodic reviews and evaluations into tax-incentive regimes. By conducting regular assessments of the impact and effectiveness of these incentives, policymakers can ensure that regimes remain responsive to changing economic conditions and align with the host country's evolving development priorities. Monitoring and evaluating tax incentive programmes is crucial for maintaining their relevance and maximising their positive impact. Through a systematic and rigorous evaluation, policymakers gain valuable insights into the outcomes of these programmes, allowing them to identify areas for improvement and make evidence-based decisions to optimise their effectiveness. A key benefit of periodic reviews and evaluations is their ability to fine-tune tax-incentive regimes. As economic conditions shift and development goals evolve, it is imperative to assess whether existing incentives are still meeting their intended objectives. By closely monitoring their impact, policymakers can identify any gaps or shortcomings and make necessary adjustments to ensure that incentives remain effective and efficient. Moreover, regular evaluations provide an opportunity to address any unintended consequences of tax incentive programmes. While these incentives are designed to stimulate investment and economic growth, there is a possibility of unintended outcomes that may negatively affect other sectors or create market distortions. Through systematic evaluation, policymakers can identify and mitigate any adverse effects, ensuring that incentives strike the right balance and deliver the desired outcomes without causing unintended harm (Sharma 2022). Evidence-based decision-making is critical for optimising the outcomes of tax incentives. By conducting rigorous evaluations, policymakers can gather data on the performance of these programmes, assess their cost-effectiveness, and determine their contributions to the host country's developmental goals. This empirical evidence serves as a solid foundation for informed decisions regarding the continuation, modification, or termination of specific incentives. In addition to improving the overall effectiveness of tax-incentive regimes, periodic reviews and evaluations contribute to transparency and accountability. By publicly reporting the evaluation findings, policymakers demonstrate their commitment to responsible governance and ensure that the public is informed about the impact and value of tax incentives. This transparency fosters trust and confidence in the government's approach towards promoting investment and economic development.

Incorporating mechanisms for periodic reviews and evaluations is essential for maintaining the effectiveness and relevance of tax-incentive regimes. Through regular assessments, policymakers can fine-tune incentives, address unintended consequences, and make evidence-based decisions to optimise their outcomes. This practice not only ensures that tax incentives align with the host country's development priorities but also promotes transparency, accountability, and informed decision-making. By embracing periodic reviews and evaluations, countries can foster a dynamic and responsive environment that maximises the positive impact of tax incentives on investment and economic growth.

In conclusion, complying with prohibitions under BITs while creating effective tax-incentive regimes requires innovative legal approaches that strike a balance

between promoting economic development and upholding international legal obligations (Avi-Yonah 2023). By exploring concepts such as smart incentives, conditional incentives, and incorporating mechanisms for review and evaluation, policymakers can design tax-incentive regimes that not only attract foreign investment, but also contribute to sustainable and inclusive growth (Heitmüller and Mosquera 2021). These innovative legal ideas enable countries to harness the potential of tax incentives while ensuring compliance with BITs, fostering a favourable investment climate, and advancing their developmental goals within the framework of international law.

6 The Future of Tax Incentives and Performance Requirements in Trade and Investment

The future of tax incentives and performance requirements in trade and investment is an area of increasing importance in the global economy. As countries strive to attract investment, promote sustainable development, and balance their international obligations, innovative approaches are being explored to shape tax-incentive policies. This section delves into the concept of naturally attractive tax incentives, and examines the factors of stability, predictability, transparency, and accountability that contribute to creating a conducive investment environment.

The objective of this section is to explore the future direction of tax incentives and performance requirements for trade and investment. The main legal thesis is centred on the concept of naturally attractive tax incentives, which involves designing incentives that appeal to investors organically. This section highlights the importance of stability, predictability, transparency, and accountability in tax-incentive regimes as the foundations for attracting investment and fostering sustainable economic growth. To effectively address the future of tax incentives and performance requirements, this study will follow a logical progression. It begins by providing a descriptive account of the concept of naturally attractive tax incentives and its significance in the evolving landscape of trade and investment. This section explores the idea of designing competitive tax systems based on fairness, efficiency, and simplicity as well as the importance of aligning tax incentives with the specific needs and priorities of host countries.

6.1 Towards Naturally Attractive Tax Incentives

In the pursuit of effective tax-incentive policies, there is growing recognition of the need to move towards naturally attractive tax incentives. This concept entails designing incentives that are inherently appealing to investors, making them an organic choice, rather than a forced necessity. By creating a business environment

that naturally attracts investment, countries can foster sustainable economic growth and maximise benefits for both domestic industries and foreign investors.

An innovative approach in this realm is the development of competitive tax systems based on the principles of fairness, efficiency, and simplicity. A well-designed tax regime with reasonable tax rates, broad tax base, and transparent tax rules can generate confidence and predictability for investors (Jusoh et al. 2017). By minimising complexities and reducing administrative burdens, countries can enhance the attractiveness of their tax systems and create favourable investment climates (Chi 2022).

Another crucial aspect of naturally attractive tax incentives lies in aligning them with the host country's specific needs and priorities. Each jurisdiction has unique economic, social, and environmental objectives, which should guide the design of tax incentives (Sullivan and Kirsey 2017). By tailoring incentives to address these needs, countries can ensure that they contribute to sustainable development, job creation, technology transfer, and other desired outcomes. This approach not only enhances the value of tax incentives but also promotes harmonious integration between investment promotion and national development strategies.

6.2 Ensuring Stability and Predictability in Tax Regimes

Moreover, in pursuit of naturally attractive tax incentives, promoting stability and predictability has emerged as a pivotal factor. Investors, both domestic and foreign, crave a tax environment that offers certainty and reliability, enabling them to make informed investment decisions with confidence. To meet this demand, countries must establish robust legal frameworks that safeguard themselves against sudden and disruptive policy shifts. By enshrining the principles of stability and predictability in their legal systems, countries can provide a solid foundation for investments (Montanaro and Violi 2020). This can be achieved through legislative measures that ensure the continuity of tax incentives over an extended period, giving investors assurance that their expected benefits will not be subject to arbitrary changes. Such measures may include statutory provisions that protect existing contractual obligations and commitments under tax incentive schemes. To strengthen the investment climate further, countries can also establish effective dispute resolution mechanisms that swiftly address conflicts or disagreements that may arise between investors and the government. Clear and efficient procedures for resolving disputes can instil confidence in investors, assuring them that their rights and interests will be protected in the event of disputes related to tax incentives. This not only contributes to a stable investment environment, but also fosters a positive perception of the host country's commitment to promoting fair and equitable treatment. In addition to legal frameworks, proactive communication and engagement with investors are vital for promoting stability and predictability (Sharma 2022). Governments can engage in regular dialogue with investors and relevant stakeholders to discuss any proposed changes to tax-incentive policies, ensure transparency, and provide

opportunities for meaningful input (Chi 2022). By actively involving investors in the decision-making process, countries can mitigate uncertainties and gain valuable insights into the potential impacts of policy adjustments. It is worth noting that stability and predictability in tax-incentive regimes not only attract immediate investments, but also have a long-term impact on sustainable economic growth (Montanaro and Violi 2020). Investors are more likely to commit to long-term projects and contribute to the host country's development when they are confident in the stability of the tax environment. This can lead to job creation, technology transfer, and increased productivity, thereby fostering a virtuous cycle of economic progress.

6.3 Advancing Transparency and Accountability in Tax Policies

In terms of tax incentives, transparency and accountability are vital components of naturally attractive regimes. Countries can promote transparency by providing clear guidelines, publishing relevant information, and ensuring that the criteria for accessing incentives are accessible to all the stakeholders (Gabor 2021). Moreover, establishing mechanisms for monitoring and evaluating the impact of tax incentives allows accountability and provides evidence-based insights to continually enhance their effectiveness (Kawharu 2015). By demonstrating transparency and accountability, countries can foster trust and credibility between investors and the wider public (Gabor 2021).

The concept of moving towards naturally attractive tax incentives represents a shift towards designing incentives that are inherently appealing to investors (Avi-Yonah 2023). This approach involves developing competitive tax systems, aligning incentives with national priorities, promoting stability and predictability, and embracing transparency and accountability. By adopting these principles, countries can create an investment climate that naturally attracts investment and maximises positive economic development outcomes. This forward-thinking approach not only ensures the effectiveness of tax incentives, but also positions countries as attractive investment destinations in an increasingly competitive global landscape.

7 Conclusion

From the perspective of international law, this chapter reveals key findings regarding the role of BITs, TRIM, and ASCM in shaping tax incentives. It has highlighted the various provisions and exceptions within these legal frameworks that impact permissibility and restrictions on tax incentives and performance requirements. Furthermore, it has emphasised the need for developing countries to understand the mechanics of these provisions during BIT negotiations to effectively protect their

development potential and tailor their tax-incentive policies. The analysis also underscores the importance of compliance with international trade rules and the implications of violating the performance requirements outlined in BITs.

In addition to the aforementioned points, this study has yielded several unique major legal lessons that further contribute to the understanding of tax incentives and their impact on trade and investment.

First, it is evident that the interplay between BITs, TRIM, and ASCM necessitates a careful balancing act. While BITs provide countries with the flexibility to design tax-incentive policies that align with their specific development objectives, they must also be mindful of their obligations under ASCM, and the potential distortions that may arise in global trade. This requires a nuanced approach to ensure that tax incentives are structured in a manner that fosters domestic economic development while minimising adverse effects on international trade relations.

Second, the analysis emphasises the need for transparency and accountability in tax-incentive regimes. By providing clear guidelines, publishing relevant information, and establishing mechanisms for monitoring and evaluation, countries can enhance their transparency and accountability (Cho and Kurtz 2018). This not only builds trust and confidence among investors, but also allows for the identification of any unintended consequences or inefficiencies in the use of tax incentives. Regular assessments and reviews enable policymakers to make informed decisions and to continuously improve the effectiveness of these incentives (Jusoh et al. 2017).

Furthermore, the importance of stability and predictability in tax-incentive regimes cannot be overstated. Investors require a stable and predictable investment climate to make long-term commitments and to contribute to the host country's development goals. Therefore, countries should establish legal frameworks that protect against abrupt policy changes and provide mechanisms for dispute resolution. In doing so, they can instil confidence in investors, enhance the overall investment climate, and attract sustainable investments that generate long-term benefits.

Finally, the analysis underscores the significance of tailored and context-specific approaches to tax incentives. Recognising that each country has unique economic, social, and environmental circumstances, policymakers should identify the appropriate incentives and requirements that align with their local economies. This requires an in-depth understanding of the country's development priorities and careful consideration of the potential impact of tax incentives on various stakeholders. By tailoring tax-incentive regimes to local conditions, countries can maximise their positive impact on economic development and ensure that the benefits are distributed equally.

The major legal lessons derived from this analysis emphasise the need for a balanced and nuanced approach to tax incentives. Transparency, stability, and tailored approaches are essential for designing effective tax-incentive regimes that promote investment, trade, and equitable outcomes. Considering these lessons, policymakers can navigate the complex landscape of tax incentives and contribute to the development of sustainable and inclusive economies.

The fundamental implications of the legal analysis conducted in this study are numerous. First, it highlights the need for a nuanced and context-specific approach

to tax incentives, considering the unique circumstances and development priorities of each country. This emphasises the importance of stability, predictability, and transparency in tax-incentive regimes to attract long-term investment and foster sustainable economic growth. Additionally, the analysis underscores the significance of the effective monitoring, evaluation, and periodic review of tax incentives to ensure their continued relevance and alignment with policy objectives. Finally, the findings emphasise the critical role of negotiation and cooperation among nations in shaping tax-incentive policies, balancing the interests of host countries and foreign investors, and advancing the objectives of economic development and fair global trade relations.

In conclusion, this analysis of international law's intersection with tax incentives underlines several pivotal recommendations for policymakers.

1. Balanced Approach to BITs, TRIM, and ASCM: Ensure tax incentives align with development goals while complying with international trade obligations.
2. Transparency and Accountability: Establish clear guidelines and monitoring for tax incentives to build investor trust and assess policy effectiveness.
3. Stability and Predictability: Create stable legal frameworks to protect investors from abrupt policy changes and provide dispute resolution mechanisms.
4. Tailored Tax Incentives: Design incentives specific to local economic, social, and environmental conditions to maximise developmental impact.
5. Context-specific Approach: Tailor tax incentives to country-specific priorities, ensuring relevance and alignment with policy objectives.
6. Effective Monitoring and Periodic Review: Continuously evaluate tax incentives to maintain their alignment with evolving economic goals.
7. Negotiation and Cooperation: Foster international collaboration in shaping tax-incentive policies, balancing host country and investor interests.

These recommendations are designed to harmonise the competing interests of international trade, investment protection, and host countries' development goals.

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Tax, Trade, and Investment for Green Transition

Suranjali Tandon

1 Introduction

Tax policy confronts the dual challenge of digitalisation and green transition. Coping with the new reality, developed countries have made a head start by implementing carbon pricing as well as offering fiscal incentives. In this context two legislations—the EU's Carbon Border Adjustment Mechanism (CBAM) and the Inflation Reduction Act (IRA) are relevant. The two are levers to encourage green transition in the developed countries. However, these will have ramifications for developing countries. First, the CBAM has entered into effect and the measure is in its transitional phase, emission monitoring and reporting on limited products is required from October 1, 2023. A full tax will be implemented in 2026. When the tax becomes applicable it will be implemented, it will impose the EU's climate ambition on the trading partners. As the rate of levy will be linked to the EU emission trading system (ETS), this raises concerns of adverse economic impact and therefore its tenability given the prevailing legal standards. It is expected that there is an immediate impact on the flow of goods covered under the tax while also reversing some of the flow of investments to developed countries in sectors covered by the CBAM. That is, the investments in countries without a carbon price will be reduced to the extent that it makes it more costly to import the products into the EU. While the tax will impose a higher level of ambition to decarbonise, the scope for making it possible to do so at the pace would be challenging with the global minimum tax that restricts the kinds of incentives that can be made available. This chapter discusses the compatibility of these measures with global equity.

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2 Climate Policy and Equality: Is the Paris Agreement Binding?

Countries have committed to reduction in emissions as well as increase the share of non-conventional in their nationally determined contribution under the Paris Agreement. While the United Nations Framework Convention on Climate Change describes the Agreement as a 'legally binding international treaty on climate change' experts argue otherwise (UNFCCC 2023). It does not impose penalties, such as fees or embargo on parties that violate the agreement; neither is there an international court or governing body to enforce compliance. There are political reasons for the non-binding nature of the treaty even though they have committed to nationally determined contributions. The United States—being a large emitter—would have only been able to back the treaty where it was not held accountable for specific outcomes (MacLellan 2021). For the treaty to be binding, it would require two-third approval of the US Senate, which at the time was controlled by Republican lawmakers opposing the deal. To bring consensus, therefore, the drafters conceded the penal ramifications of non-compliance for a softer requirement to legally fulfil process requirements. Therefore, the treaty compels countries to update their Nationally Determined Contributions (NDC) regularly. Although the Paris Agreement is limited in its legal ramification, it creates pressure among countries to lower the carbon footprint. There have been instances where the treaty's legal nature has been accepted as non-optional by Courts and Nation states.

A few countries such as the EU and Japan have gone further to adopt Paris Agreement's goals domestically through legislation (MacLellan 2021). However, there are a diverse set of countries, at different levels of income, emissions, and historical context. The expectation that the countries will be able to meet their environmental obligations at the same pace would be unfair and enshrined in Article 3(1) of the 1992 UNFCCC as 'Common but Differentiated Responsibility and Respective Capabilities' (CBDR). The application of the principle that entails taking historical responsibility which was later diluted by developed economies and emphasised future responsibilities (Zhang and Zhang 2022). The US, for example, was opposed to the non-binding nature of the principle to countries like India and China (Maguire 2013, 260, 263, 266; Harris 1999, 27–28). Therefore, the historical emissions, though central to defining fairness and equity, are not explicitly incorporated in the treaty (Pauw et al. 2014). Just as there are questions on the binding nature of the Paris Agreement, there are also questions related to that of the CBDR principle.[1] More quantified differentiated responsibilities for the developed countries have meant that the application of the principle has progressed in international law and applied to domestic law (Chen 2021). For example, the *Urgenda* vs. *the Netherlands* national court uses the principle of international economic law (CBDR)

[1] In order to operationalise, these countries have been divided into Annex I and Non-Annex I countries.

as a complementary tool to interpret a State's climate obligations under domestic law[2] (Ferreira 2016).

The US-China declaration at Glasgow in 2021, indicated softening of their stance as they committed to 'tackling the climate crisis by strengthening implementation of the Paris Agreement, reflecting common but differentiated responsibilities and respective capabilities, in the light of different national circumstances' (US Department of State 2021). However, with intensification of geo-political tensions, it is not clear whether such commitment remains intact and even for such declaration it is important to delineate the meaning of responsibility. An issue that has been flagged by leaders of developing countries such as Mia Motley, advocating the reform of multilateral development banks and providing concessional finance under the Bridgetown Initiative (Reuters 2023). The question then is whether CBDR can be legally implemented, even though it is enshrined within the Paris agreement or is it just the basis for determination of emission reduction targets, that is, the Paris Agreement only affords differential treatment to Non-Annex I countries is the right to pollute over a longer time frame.

A more recent development has been the passing of a carbon border adjustment mechanism by the European Union. This is seen as a burden on developing countries that will be required to tailor their carbon pricing in order to export to the EU. This seemingly contradicts the CBDR but it is less clear whether this would contradict the WTO rules. Trade agreements do not make explicit reference to CBDR, however they do include provisions related to the most favoured nation (MFN) and national treatment (NT). The next section deliberates the inherent tensions between the application of the CBAM and the CBDR that underpins the green transition.

3 Design of CBAM

3.1 Carbon Pricing and EU ETS

The EU adopted the ETS directive in 2003 and introduced the cap and trade or emission trading mechanism in 2005. The first phase of the ETS was a pilot to meet EU's Kyoto obligations; this phase helped build the infrastructure for carbon pricing but this was also a phase where all the allowances were free (Directive 2003/87/EC 2003). In 2008, the second phase of the ETS work began to progress, as the cap on allowances increased and free allowances declined to 90%. As a supporting mechanism to the ETS, the EU also set up the single EU registry for allowances and the

[2] The Court interpreted the leadership role of developed countries in addressing climate change. In the case the Court concluded that in order to meet the standard duty of care towards the plaintiffs the Dutch government was ordered to limit the joint volume of greenhouse gas emissions or have them limited, so that this volume will have reduced by at least 25%–40% at the end of 2020 compared to the level of year 1990.

aviation sector was brought under the ETS. In the third phase, 2013–2020 the EU shifted to an EU wide cap rather than national caps on emissions, auctioning became the default method of allocation and more sectors were included. Therefore, the EU took 15 years to make the emission trading system effective in pricing carbon. Although the system was not without shortcomings—it gave away too many free allowances rendering price discovery less than perfect.

The EU's is the only carbon market there is, but it holds a large share in the global volumes and value. There are 30 compliance markets for carbon across the world which are national and sub-national (BloombergNEF 2022). As per Refinitiv, the EU carbon market accounted for 87 percent of the Euro 850 billion in carbon permits in 2022 (Zelljadt 2023). The EU now proposes to reorient the ETS as it targets a 50% net reduction in greenhouse gas emissions by 2030. It is proposed that the annual allowances will be reduced at an annual rate of 2.1% starting 2021 and strengthen the market stabilisation reserve (European Commission 2023b, *Our ambition…*,). As a result, the price of carbon permits has increased during the period. From close to Euro 20 in mid-2008, to prices remaining flat between 2011 and 2018, at lower than or close to Euro 10, the prices touched EUR 100 in 2023 with the launch of the third phase prices. The surge in prices is linked to further tightening of the market with the announcement of the 'Fit for 55' package alongside the rise in energy prices that fuelled demand for energy permits (Fig. 1).

As the price of carbon rises for the EU, even touching EUR 100 in February 2023, the CBAM can be costly for developing countries as the expectations of decarbonisation in the EU may be very different from the countries that export to it. The underlying premise for applying CBAM is that there is carbon leakage. The CBAM regulation specifically mentions that the Union's partners 'pursue policy measures that do not help achieve the same level of ambition'. It is feared that in such a case companies subject to carbon pricing may decide to move production to countries with lower or no carbon price and export the products back to the EU. This arbitrage would undermine the intent of pricing. However, the evidence on carbon leakage is not definitive or conclusive, especially since the distribution of allowances has not been as strict. One way to check this would be to assess the flow of foreign direct investment in fossil fuel sectors, particularly competing industries, to other countries after the introduction of ETS. There are few studies that document

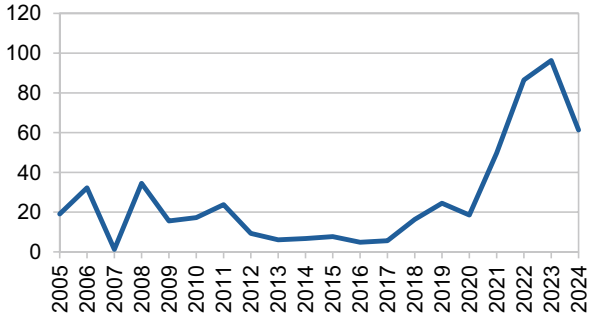

Fig. 1 EU ETS Permit price (US$/CO2). Source: the author, based Carbon Pricing Dashboard, World Bank

this impact; for example, Koch and Basse Mama (2019, 479–492) find that the evidence does not support EU ETS regulated German firms relocating to other countries. Branger et al. (2016, 109–135) do not find any evidence of carbon leakage in the steel and cement sector. The EU ETS has also been less than perfect so the evidence on carbon leakage for the trade exposed sector may be low (Sato and Burke 2021). Therefore, with insufficient evidence on the extent of leakage, the EU has imposed a standard on trade that compels countries to respond with comparable levels of taxation. The approach raises multiple questions for international relations.

One, is this compliant with WTO, as the EU claims, or are there ways in which this may be challenged. Two, what does this mean for trade with developing countries and third, how do their pricing strategies compare with that of the EU.

3.2 Is CBAM Compatible with CBDR?

EU's approach is observed to be incompatible with common but differentiated responsibility and respective capabilities but is it compliant with trade law needs to be established. The EU sees the application of the CBAM as an internal measure where the domestic goods, already priced under the ETS, are treated at par with the imported goods and for that reason would be WTO compliant (Venzke and Vidigal 2022). Further, CBAM could fall under the general exceptions under Article XX and not violate the WTO rules (Jouanjean et al. n.d.). Venzke and Vidigal (2022) suggest through their analyses that preferential treatment under the CBAM can be maintained even though the criteria for differentiation as well as their practice are highly contested. This differentiation in treatment may not necessarily be through an exemption of countries from application of CBAM but in fact, could be achieved through compensating mechanisms. The EU proposes in its legislation a compensation mechanism. Para 71 states that 'The Commission should strive to engage in an even-handed manner and in line with the international obligations of the Union with the third countries whose trade to the Union is affected by this Regulation, in order to explore the possibility for dialogue and cooperation regarding the implementation of specific elements of the CBAM. The Commission should also explore the possibility of concluding agreements that take into account the carbon pricing mechanism of third countries. The Union should provide technical assistance for those purposes to developing countries and at least developed countries as identified by the United Nations (LDCs)' (Regulation(EU) 2023/956 2023). The language, though heavily caveated by 'even-handed' and 'in line with international obligations' offers scope for recognising that the current carbon pricing practices may differ widely across countries and the EU has been ambitious. Therefore, an important manner in which the CBDR may be reconciled with the EU's CBAM is to agree on ways to equate the differential pricing. However, it is understood that the EU is only able to negotiate, through agreements, to the extent that a certain carbon pricing mechanism is to be considered compatible with CBAM and if technical assistance is to be extended on implementing a similar system of cap and trade. It is

critical to inquire if countries can then negotiate based on their fuel taxes to say that it is a pricing mechanism to be recognised by the EU. Even if the CBAM is challenged before the WTO it does not mean that its appellate jurisdiction will ensure resolution of disputes arising from CBAM. As it is the appellate body has been in crisis for some time (Lester 2022). Therefore, the remedy through trade law is limited.

3.3 Pricing of Emissions Under CBAM

CBAM is linked to EU ETS and as seen in Fig. 1 the price of emissions increased. A price of EUR 80 can be applied without adversely impacting the output in these sectors in developing countries. The EU regulation also mentions the use of revenues for technical assistance although that does not take away the pressures among countries to adapt their prices. There are also compliance costs associated with CBAM which are discriminatory between domestic and foreign jurisdictions. As per the regulation, the CBAM goods importers are required to submit quarterly reports on quantities of goods imported in the quarter as well as the country of origin per production site. Then there is also a need to report information on embedded direct and indirect GHG emissions along with carbon price due in the country of origin. At the production site there will be a need to measure the emissions and track through the supply chain. Initially, CBAM will apply to cement iron and steel, aluminium, fertilisers, electricity, and hydrogen. At the same time free allowances will gradually be phased out and would be completely done away with by 2034 (Kahmann et al. 2023). The CBAM certificates will need to be purchased and surrendered. The price of the certificate will be calculated based on the weekly auction price of EU ETS allowance (European Commission 2023a). Although the compliance costs may be higher, especially in the transitional phase, these are not considered non-tariff measures per se. Even though the 'burden of complying with non-tariff measures (NTMs) and associated procedural obstacles is especially felt in the economies of developing and least developed countries (LDCs), where facilities necessary to achieve compliance with technical measures are often lacking or inadequate' (ESCAP 2019). The fact that the EU in its regulation proposes that the revenues are employed towards technical assistance could also safeguard against the criticism that the measure is discriminatory. Carbon pricing varies widely across countries and the imposition of a CBAM at that rate would have economic repercussions. It is therefore important to compare carbon prices across geographies to understand their repercussions.

3.4 What Is the Effective Rate of Carbon?

The OECD formed the Inclusive Forum on Carbon Mitigation Approaches (IFCMA) to support climate mitigation work. It is agreed that the IFCMA will not set standards or rank countries (OECD 2023b). Although, the OECD at the same time suggests that it will explore building methodologies for measuring carbon intensity and through its Module II will help develop and apply a common approach to assess the effectiveness of these policies (OECD 2022). Therefore, while it does not want to set standards for the development of a common approach, it is in some ways an attempt at defining a standard. Countries are not in agreement on approaches. OECD convened high level meetings where the members expressed their concern with labelling developed country practices as best and urged that the pricing mechanisms be just and inclusive.

The OECD recently released a report that measures the net effective carbon rate across countries (Garsous et al. 2023). The report finds that countries such as Argentina, Colombia, Greece, Indonesia, and Ukraine are estimated to have high negative carbon prices. As per Fig. 2, there are developing countries with effective carbon rates that are a fourth or further less than the rates prevailing in the EU. What is interesting is that nearly 50% (for most countries) of the price is based on the fuel taxes even in the EU. The prices are also not equivalent among the EU members. As per an assessment EU's CBAM could violate commitments because it gives special treatment to countries that already have a carbon price (Smith 2023). This is estimated to benefit South Korea and Singapore by allowing them to deduct the carbon price when sending products to the EU. It is also likely that some countries, such as Switzerland, Norway, Iceland, and Liechtenstein, could be fully exempt from the CBAM because they all have an ETS that is tied to the EU's, even though pricing wise they are different (Yanovich et al. 2023; Bond et al. 2022). As can be seen from OECD's data, the permit prices were different across EU countries in 2021.

Therefore, the composition of a carbon price is a controversial matter. It consists of the tax policy and permit pricing. This amounts to exposing developing countries to sovereign decisions to tax while exposing their pricing decisions to external market volatility. In fact, the latter is more relevant as the ETS touched EUR 80 and this means developing countries will have to tether their pricing policies to the geopolitical stance of the EU. For example, the rise in EU permit prices in 2022 was not only on account of the regulatory changes but also the rise in gas prices, at the back of the Russia–Ukraine war. The switch from gas to coal fuelled demand for permits, as a result, countries that export to the EU would have to adjust their processes in accordance with the political and economic conditions of the EU (Ampudia et al. 2022).

It is not as if there are not any taxes on emissions at the moment. In fact, fuel taxes account for a large share of price across the world, including in developed countries such as the Australia and US may be treated as equivalents of the price. Although theoretical work suggests that cap and trade and carbon taxes can be equivalent in terms of revenue, it is the prerogative of the countries if they wish to

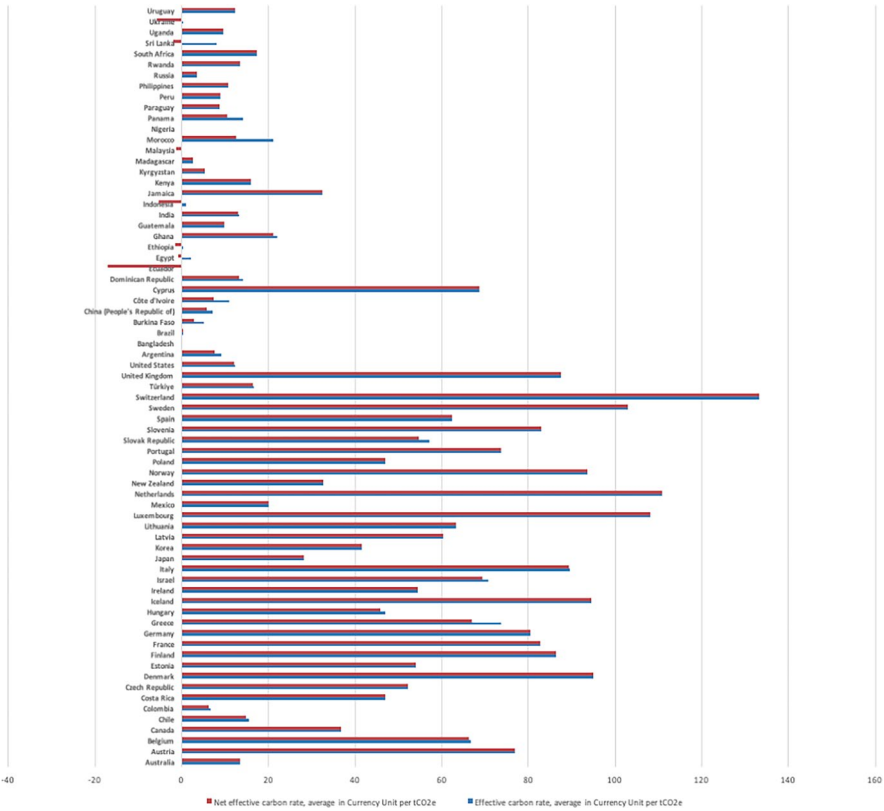

Fig. 2 Effective rate of carbon in 2021. Source: the author, based on data from OECD Net Effective Carbon Rates Dataset

impose a tax that contributes to the revenue of the government rather than permits that only provide one time revenue at the time of auction (that may be low in early phase) and capital gains tax, where applicable, on transfer (Keohane 2016, 162). Although the CBAM allows carbon taxes, levies and cap and trade based prices to be used as reference price for carbon.

It is seen in Fig. 3 that the countries with higher GDP per capita also tend to have higher carbon prices. Further, the range of carbon pricing differs even among developed countries. The question then is how can the CBAM fit within such an unequal order.

European Union often take Incentives given through indirect taxes are s a 'dogmatic view towards the primacy of its regulatory approaches and its extension to imported goods. In fact it is an approach analogous to conformity assessment procedures for EU eco-design standards that often rely on design characteristics delineated in technical regulations rather than the environmental performance of imported products' (Hinman 2022). However, it applies not only to developing countries but also to trade with developed countries such as the US. Therefore, to adapt the US

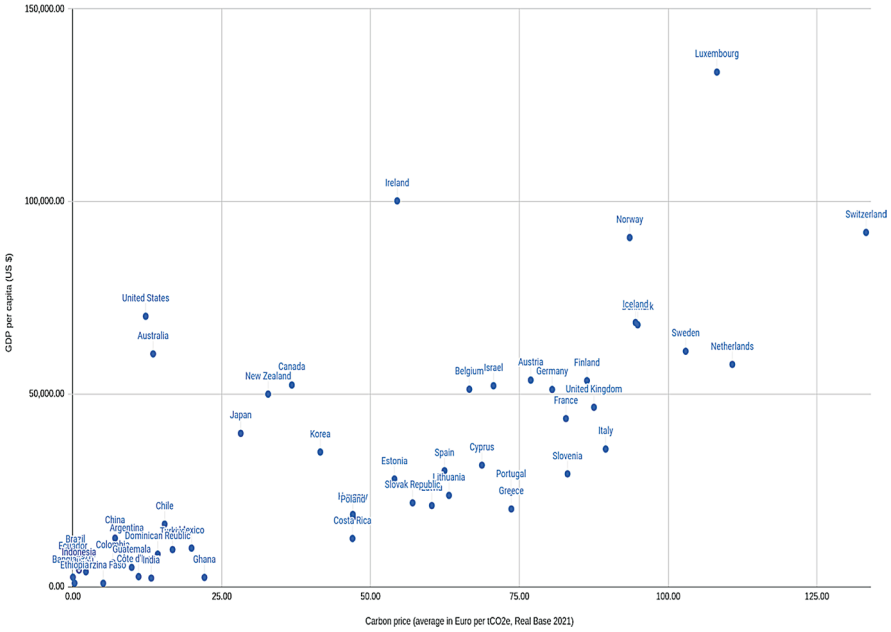

Fig. 3 Effective carbon rate and per capita GDP. Source: the author, based on data from OECD and World Development Indicator, World Bank

too is considering a 'polluter fee' and carbon border adjustment (Taylor 2021). It is interesting that the US would consider the border carbon adjustment (BCA) while its own pricing strategy is rather weak with no national ETS[3] and taxes that amount to less than EUR 20. There have been propositions of the carbon levy on trade in India (Mint 2023). At the same time, China even has a national ETS (priced at US$ 8) and yet has expressed its concern on the proposal being discriminatory.

The critical point is that how does the EU imagine such convergence in pricing is possible given that the countries are at different levels of development and even the 3 year transition period is not enough to align prices without an adverse impact on developing economies. As it is seen, the pricing today varies widely (Fig. 2) and even the IMF's work suggests that bearing in mind different levels of economic development, an international floor price may be suitable allowing countries to fix their own carbon price above such floor price (Chateau et al. 2022). Yet, even if the EU's approach is calibrated or limited at the moment, it imposes a single rate that is prohibitive. There are also growth and inflation effects depending on the level and pace of pricing adopted by countries. It is likely then, the EU may disrupt the trade

[3] California's cap-and-trade system and the Regional Greenhouse Gas Initiative (RGGI) covering 11 north-eastern states (Connecticut, Delaware, Maine, Maryland, Massachusetts, New Hampshire, New Jersey, New York, Rhode Island, Vermont, and Virginia. Pennsylvania is considering joining RGGI). Further, the price of carbon that covers power sectors is $18 in California and $6 in RGGI.

in sectors and of its trading partners' attempt to address the problem by imposing a tax on imports so as to use that to calculate the CBAM levy applicable. It is likely that firms begin to pass on costs of the levy to consumers. It may also be possible that the tax is anti-competitive as it shifts incentives for large MNEs to operate in the EU, which is akin but opposite of carbon leakage.

3.5 Redistribution of CBAM Revenues

As mentioned earlier there are questions of whether the tax collected can be redistributed to counter some of the effects of CBAM. The EU relies on member country contributions for its revenue and the multiannual financial framework (MFF) sets the budgetary heads of expenditure that are divided under six categories for the latest MFF—natural resources and environment, cohesion and values, single market innovation and digital, European public administration, neighbourhood and the world, migration and border management and security and defence. The largest expenditures are on agriculture, cohesion, and values, and external action is about 6% of the budget (Deutsche Bundesbank 2020). With the current EU budget size of EUR 1.2 trillion, EUR 600 billion would be allocable to external action (European Commission n.d.). Noting that this has been a politically strained year, not all of it would be available in the near terms for climate action. It is estimated that EU CBAM, 75% of which will be allocated to the EU Budget, is expected to raise EUR 1.5 billion per year as of 2028 (European Commission 2023c). While CBAM is seen as a source of revenue for the next generation of its own resources, it is not permanent or significant. Comparing the budgetary room available it is possible to redistribute a fraction from the external action, even though there is no scope for ear-marking, as had been seen from the experience of revenues of ETS permit auctions that divided member states (Müller 2008). A more significant aspect is if the revenue effects are exceeded by economic feedback to developing economies dependent on exports of these products, then the redistribution based purely on revenues collected may be insufficient.

Another kind of effect that is expected to unfold after the application of CBAM is that large MNEs will withstand better, as they have cross border presence. For example, one of the larger steel manufacturing companies in India—Tata Steel—has a production facility in the EU and may be better prepared, whereas small and medium enterprises may not have the wherewithal to respond to such levy. Beyond the transnational issue it also raises the issue of competitive forces within the domestic economy as the pressure to price internally may increase. The impact of CBAM therefore will play out in different ways depending on the kinds of companies in the sector and is summarised in Table 1. This in turn will have interactions with tax policies across countries, as discussed in the following section.

Table 1 Effects of CBAM

	EU	In a country that does not price	In a country that prices by less than EU ETS price
Small and medium enterprise	– Disruption of supply chain or full pass forward of costs to EU customers where inputs are imported from non-pricing or low price country – Already covered and transitioned to EU ETS	– Exports to EU impacted to the extent wages and costs do not allow for price increase	– Exports to EU impacted to the extent wages and costs do not allow for price increase
Large MNE	– Disruption of supply chain or full pass forward of costs where inputs are imported from non-pricing or low price country – Already covered transitioned to EU ETS	– Relocation of activity to EU to the extent cost advantage is less than cost of CBAM	– Relocation of activity to EU o EU to the extent cost advantage is less than CBAM

4 Pillar 2 and Reforming Corporate Taxes

Another tax policy that is critical for energy transition is the provision of incentives to encourage 'green' sectors. As the OECD, World Bank, and UN encourage countries to reform their tax systems that are fit for the twenty-first century, countries are now looking for alternatives to stimulate industries aligned with green transition. While Pillar Two aspires to raise the minimum tax rate to 15 per cent, this is on the tax base that is covered under GloBE. It is argued that the Pillar 2 proposal sets the end date on incentives. However, there are two important aspects to this, which in turn would have implications for green transition—there is substance-based income exclusion based on employee and tangible assets. This has been fixed at the moment at 10 per cent for payroll cost and 8 per cent for tangible assets (OECD 2023a). Once these exclusions are made for substance-based presence in the jurisdictions, there is also potential for accommodating domestic level minimum taxes.

While it is possible all of these measures still allow for incentives to continue, it is not certain to what extent. It is suggested that two kinds that may still survive despite the claw back—those which lead to timing differences between income and tax such as accelerated depreciation, carry forward to losses and non-refundable tax credits may still allow for a lower effective tax rate. Then there are incentives related to other taxes such as VAT, property, energy, or payroll tax that may also be unaffected (Baert 2023). Therefore, there will be limited scope for incentives under Pillar 2 and as mentioned in Table 1, some of these would have to be offered to large companies covered by Pillar 2, as a CBAM like measure would have minimal impact at the MNE level but will have macroeconomic consequences. Therefore, countries will have to explore alternatives available also given that climate mitigation would require a significant ramp up in country investments that go beyond the impact of the CBAM.

Today there are 144 tax incentives offered around the world by 17 countries (PwC n.d.). This is far outweighed by 183 cash grants that are made available. Cash grants are prevalent in the EU, China, India, South Africa, and Canada. The distribution of tax incentives across countries is also interesting. The US provides all of the 33 incentives as taxes, whereas the UK provides 16 cash grants and 10 tax incentives, Netherlands (8 cash grants and 10 tax incentives) and interestingly Australia offers 39 cash grants, 14 soft loans, and 1 tax incentive. The large number of incentives that are reported for the United States under the head of tax incentives have been introduced through the Inflation Reduction Act 2022. The measurement of effective carbon rates is as of 2021, and it may be of interest to assess what the level may be after the introduction of tax incentives. While the IRA addresses the issue of MNEs filing low or no taxes, it also extends tax credits to businesses and individuals to scale up the use of renewable energy. These tax credits will be covered under Pillar 2 but there are complications on how these may pan out for calculation of taxable incomes.

The GloBE rules distinguish between qualifying and non-qualified refundable tax credits. The difference between the two being that the credit is refundable within 4 years. Even though the qualifying refundable tax credits, similar to government grants, are added back to the GloBE income for purposes of calculating the effective tax rate. Adding back may not impact a negative income where it applies specifically to one activity (Liotti et al. 2022). Non-refundable tax credits are treated as a reduction in covered taxes. The impact of the two is similar, the impact of refundable tax credits will be smaller as it affects denominator (Baert 2023). That is non-qualified refundable taxes will not be included in income but will reduce the tax paid. Then there are transferable tax credits, the amount received in exchange would be excluded from seller's income and will not be deducted from recipient's income (Congressional Research Services 2023). It is suggested that the credits claimed, for example, by project developers are treated less favourably than those tax equity investors in the project. In fact, it is suggested that if the model rules remain the same, countries could consider recasting tax incentives as government grants or QRTCs, facilitate the use of tax benefit transfers through tax equity investments and leasing, increasing the use of accelerated cost recovery, allowing deferral of income recognition and allowing elective carryforward and carryback tax credits. Some of the energy tax credits under the IRA are refundable or transferable. For example, the carbon capture and sequestration credit, clean hydrogen production tax credit, advance production tax credit are all refundable and transferable. At the same time there are renewable energy production tax credit, clean electricity production tax credit, energy investment tax credit to name a few that are transferable (Tax Notes 2023). The OECD has clarified that the transferable credits will be treated as refundable credits if sold and therefore reduce income of the seller while for the purchaser the difference in sales price and value of credit will be taken as a reduction in tax expense.

Even in Europe there are plans to offer reductions and exemptions for different parts of the energy transition. Many countries such as Spain and Italy offer higher deduction for capital investment in renewable energy capacity. Germany introduced

in August 2023 the Bill for Growth Opportunities, which was approved by the Cabinet and provides incentives for investments designed to limit the impact of climate change which includes up to 15% of the cost of the qualifying capital investment capped at EUR 30 million per company.

Therefore, credits and deductions that result in timing differences between financial and tax treatment may continue. The EU and US have experience in implementing such incentives and have interestingly quickly gravitated towards more of these to support the transition.

Exemptions are observed to be a preferred form of tax expenditures, particularly in developing countries. As is seen in Fig. 4, there is higher preference for deductions among developed countries. It is expected exemptions may taper while the race may be to extend benefits to businesses through deductions and credits against the income tax. It is observed in the tax expenditure dataset that Puerto Rico offers the maxium number of tax credits (105).

As can be seen in Table 2 the tax systems are bifurcated whereby the incentives to small companies or below the Pillar 2 threshold survive irrespectively. But the transition involves fossil fuel companies that will have to think of their transition plans, or else result in financial shocks where the transition plans are nationally binding, the incentives may be directed at large corporations. For example, Shell Corporation, Chevron, PetroChina, TotalEnergies, BP, Sinopen, and Reliance Industries all feature in the Forbes 2000 list with revenues upwards of $5 billion

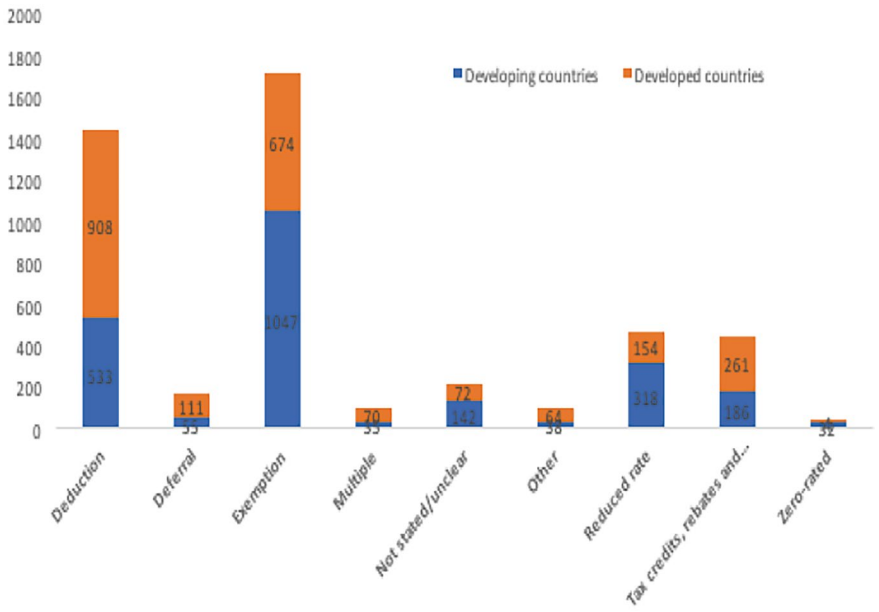

Fig. 4 Types of tax expenditures offered by countries in 2023. Source: the author, based on data from Global Tax Expenditure Database (Redonda et al. 2024)

Table 2 Matrix of tax incentives

	Red tax incentives[a]—tax holiday, exemption of income,	Green tax incentives—tax credits, accelerated depreciation
Company with revenue equal to or more than EUR 750 million	Impacted by Pillar 2	Not impacted by Pillar 2
Company with revenue less than EUR 750 million	Not impacted by Pillar 2	Not impacted by Pillar 2

[a]See Liotti, Belisa Ferreira, Joy Waruguru Ndubai, Ruth Wamuyu, Ivan Lazarov, and Jeffrey Owens. 'The Treatment of Tax Incentives under Pillar Two' UNCTAD, July 28, 2022

(Murphy and Tucker 2023). Thus, many incentives may be availed by these corporations in various jurisdictions. The tax credit mechanism in the US and the super deductions in Europe can act as a shield against taxing back of low ETRs and in some ways the tax systems of developed countries may be prepared for Pillar 2. Irrespective, the EU and US have swung in full action with industrial policy as their focus. The European Green Deal and IRA among the many other (CHIPS, BRI) initiatives launched to create jobs (Shih 2023). The response among countries to counteract such policy seems antithetical to the call for global minimum tax but in fact it seems to suggest that the tax incentives be designed in a certain way and for some companies.

Tax expenditures can be transformative for green transition and these can be offered through direct and indirect taxes. Incentives given through indirect taxes are used more to shift consumers to newer technology (von Haldenwang et al. 2023, 10). Yet, there is a need to build capacity to produce equipment and generate power within the economies. Yet, as countries begin to enact minimum tax the scope and scale of these incentives will change. Developing countries may find it harder to compete to attract the estimated deficit in annual investment insofar as large companies with transnational operations choose to locate in the jurisdictions that have strict pricing mechanisms alongside incentive mechanisms.

5 Concluding Remarks

Green transition is a macroeconomic challenge that will require careful policy design to ensure that the shift to renewables is not at the cost of economic growth. The EU has taken lead on the pricing mechanisms to ensure that it is on the path to Net Zero. However, in the process, trade-related impacts are expected to unfold. While the EU disagrees that this is a trade measure, the response of developing countries makes it amply clear that it is such a measure and the critical point is that despite the efforts to tax they may fall short of the rates in the EU leading to revenue and output loss (ATAF 2023). This comes at a time when there is talk of Global minimum tax and interestingly there are companies that will respond to CBAM and

developing countries may find themselves in a bind to offer incentives that are within the 'green' list of incentives under Pillar 2. At the same time the domestic resources may have to be diverted to encourage production and investment within developing economies in order to meet the challenge of the transition. This may be possible for smaller firms through exemptions and tax holidays, yet the new industrial policy can shift incentives to send capital even to smaller firms where the incentives are in capital exporting countries, particularly because of the better credit ratings. As a result developing countries that have thus far struggled to find their fair share of climate finance may find themselves in a bind trying to price carbon at prohibitive rates while offering incentives to compete with the new industrial policy of the proverbial North.

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Breaking the Cycle of Domination in Global Tax Governance: Africans Defying Asymmetries and Seizing Opportunities

Lyla Latif

1 Introduction

This chapter offers a comprehensive understanding of the intricate dynamics of global tax governance, especially concerning Africa. It begins by delving deep into the historical legacy of international taxation, tracing its origins to colonial economic exploitation and its subsequent role in perpetuating economic disparities between nations. The norms and frameworks that shape international taxation, such as those advanced by the OECD, have often failed to adequately represent the interests and priorities of the African continent. This misalignment threatens to undermine Africa's aspirations for sustainable growth, self-reliance, and prosperity.

Thus, as it stands, the dominance of the OECD has propagated tax norms that often disproportionately benefit capital-exporting countries while exacerbating challenges for capital-importing nations. This reality misaligns trade, investment, and tax frameworks, stymieing Africa's growth aspirations. This foundational understanding sets the stage for a discussion on the challenges of the present-day global tax system, particularly the aggressive tax planning strategies adopted by multinational corporations and their repercussions on developing nations.

The chapter then transitions to spotlight the transformative shift in Africa's stance within the global tax discourse. As the chapter progresses, the narrative underscores various collaborative initiatives and measures taken by African nations to challenge and rectify historical asymmetries. The recent United Nations resolution (A/C.2/788/L.18/Rev.1) on Promotion of Inclusive and Effective International Tax Cooperation, introduced by the African Group, represents a decisive effort to challenge historical asymmetries in global tax policymaking. As this chapter illustrates, the resolution underscores the urgent need to reconfigure global tax

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governance in a manner that empowers African countries and enables them to pursue tax, trade, and investment frameworks aligned with their development goals.

In its concluding sections, the chapter advocates for a reformed, inclusive, and equitable global tax system, emphasising the intertwined relationship between tax, trade, and investment and the need to align them for sustainable economic growth. The exploration of the global tax system offers valuable insights into contemporary challenges and opportunities in the spheres of trade and investment. Understanding the intricacies of international taxation is crucial because tax policies are a key determinant of the economic landscape within which trade and investment decisions are made (Mosquera et al. 2023). An equitable tax system can create an environment that fosters fair trade and encourages robust investment by levelling the playing field for all countries, especially those that have traditionally been marginalised in global economic discourse.

The implications of such a tax system extend to the enhancement of Africa's trade capabilities, providing a foundation for the continent to engage more fully in the global market. Moreover, by addressing the biases inherent in the current tax norms, the potential for increased investment in African nations rises, as a fair tax framework is likely to attract investors seeking markets with transparent and stable fiscal policies. The lessons from examining the global tax challenges thus are instrumental in shaping strategies that could transform Africa's role in international trade and investment, ultimately contributing to sustainable economic development and self-reliance.

2 Historical Inequalities: The Beginning of Tax Domination

The historical legacy of international taxation is marked by a complex evolution that has seen the formulation of tax norms at various stages and through different global institutions. From its origins rooted in colonial economic exploitation to the present day, international taxation has served as a tool for domination, enabling wealthier countries to assert control over the economic affairs of less powerful nations (Vital 1967; Henrikson 1996). During the colonial era, major powers imposed extractive tax regimes on their colonies, siphoning off resources and capital to fuel their own development while stifling economic growth in the colonised territories (Okanga and Latif 2021). This asymmetrical tax framework, coupled with unfair trade practices, laid the foundation for the economic disparities that persist in the world today. Even after the formal end of colonialism, the legacy of unequal taxation remained intact (Latif 2022). The international tax architecture, largely shaped by Western powers, favoured the interests of multinational corporations, and facilitated tax avoidance and profit shifting.

Aggressive tax planning strategies, facilitated by tax havens and opaque financial systems, allowed corporations to exploit loopholes and shift their profits to low-tax jurisdictions, depriving developing nations of much-needed revenue (Ndikumana and Boyce 2022). Moreover, international tax rules, predominantly based on the

arm's length principle, have proven inadequate in capturing the economic realities of an interconnected global economy (Parks 2020). Multinational corporations, through transfer pricing and other mechanisms, have manipulated their financial flows to minimise tax liabilities, exacerbating the revenue shortfalls experienced by developing countries. The historical legacy of international taxation also reflects a power imbalance in decision-making processes. Institutions such as the OECD have wielded significant influence in shaping global tax norms, with limited representation and participation from developing countries (Fung 2017). This lack of inclusivity has perpetuated a system where the interests of powerful nations and multinational corporations take precedence over the needs and priorities of the most vulnerable.

In the early twentieth century, the League of Nations established financial and fiscal committees, which played a crucial role in formulating early international tax norms.[1] The Geneva Model of 1927,[2] the Mexico Model of 1943, and the London Model of 1946[3] were significant milestones in shaping international tax principles during that time. However, Africa, along with many other developing regions, was not adequately represented in these discussions and decision-making processes. The voices and perspectives of African nations were largely ignored, perpetuating the historical exclusion and power imbalances within the international tax arena. The focus shifted to the OECD, which became the primary platform for the development of international tax rules and standards. The OECD Model Tax Convention, first established in 1963, has served as a blueprint for bilateral tax treaties and influenced the tax policies of nations worldwide (OEEC Council 1955; OECD 2019). However, the lack of representation from Africa and other developing regions in the OECD has limited their influence in shaping these norms, leading to a system that largely caters to the interests of the most economically powerful nations.

Undoubtedly, the Africa Union High Level Panel on Illicit Financial Flows (AU HLP on IFFs) has been a significant catalyst for Africa's push against the OECD-centric international tax system (AU/ECA Conference of Ministers of Finance, Planning and Economic Development 2015). Chaired by former South African President Thabo Mbeki, the panel was established in 2012 to address the issue of illicit financial flows from Africa, which were severely affecting the continent's development and governance. The AU HLP on IFFs shed light on the pressing issue of illicit financial flows and their detrimental impact on African economies. It highlighted the severe loss of revenue due to aggressive tax avoidance strategies by multinational corporations and the exploitation of tax treaties. Prompted by the

[1] Letter from Hill to Gerig, 11 March 1943, UNOG:PO—C.1633/529/17/3 (proposing that the 'World Economic Council' would have the scope to deal with, inter alia, 'double taxation, fiscal evasion and other fiscal problems'); Preparatory Commission of the United Nations, *Report by the Executive Committee to the Preparatory Commission*, UN Doc PC/EX/113/Rev.1 (12 November 1945).

[2] Committee of Technical Experts on Double Taxation and Tax Evasion, *Double Taxation and Tax Evasion: Report*, League Doc C.216.M.85.1927.II (April 1927) 6, 9 ('*1927 Report*').

[3] Fiscal Committee, *London and Mexico Model Tax Conventions: Commentary and Text*, League Doc C.88.M.88.1946.II.A (November 1946) 6, 26.

findings of the AU HLP on IFFs, African nations have become more assertive in international tax discussions, challenging the norms and practices established by OECD countries that disproportionately favour wealthier nations and multinational corporations.

Parallel to these developments, the establishment of the African Tax Administration Forum (ATAF) in 2009 represented a significant milestone for Africa in asserting its voice in international taxation matters.[4] ATAF, an organisation composed of tax authorities from various African nations, has played a pivotal role in promoting cooperation between African countries on tax matters, providing a platform for African countries to articulate their positions in international tax debates and influence tax policy both at a continental and global level. The establishment of the First African Fiscal Policy Forum in 2021 and the formulation of its recommendations represent a continuation of this momentum (CODA/South Centre 2021). Africa is no longer a passive observer but an active participant in shaping international tax norms. The Forum echoes the sentiments expressed by the AU HLP on IFFs, calling for a radical rethinking of the international tax system to rectify historical injustices and imbalances.

The recent passage of the United Nations resolution (A/C.2/788/L.18/Rev.1) on Promotion of Inclusive and Effective International Tax Cooperation at the United Nations, championed by the African Group, represents a watershed moment in the history of international tax governance, particularly highlighting the evolving role of African nations in this domain. The resolution marks a bold departure from the status quo. It proposes the establishment of an inclusive intergovernmental committee tasked with drafting a framework convention on international taxation. This move directly challenges the existing OECD-led model and seeks to correct historical imbalances in the allocation of taxing rights. The resolution's passage, albeit met with opposition from several developed countries (mostly European countries), garnered global support, reflecting a paradigm shift towards more inclusive global tax governance.

As discussions continue on the establishment of a globally inclusive and intergovernmental process on formation of tax norms, rules, governance, and cooperation, it is crucial to rectify the historical imbalances that have marginalised Africa in international tax matters. A radical reimagining of the global tax system is necessary. This requires a shift towards a more inclusive and equitable framework that empowers developing nations to participate on an equal footing and ensures their tax policy choices are respected. The African Union's and African Groups efforts in the fight against IFFs and for tax justice have paved the way for a new era of engagement in international tax matters. They represent a decisive move towards the establishment of a globally inclusive and equitable tax system that respects the needs and realities of all nations, not just the economically powerful ones.

[4] https://www.ataftax.org/

3 The Existing International Tax Architecture: Challenges and Opportunities

3.1 Challenges

African countries are often underrepresented in international forums that shape global tax governance policies. This has led to policies that are not in line with the interests of African countries and has even harmed their economies (Oelofsen 2022). The political influence of the global north is also a persistent challenge for African countries. The dominance of developed countries in international organisations and forums has meant that their interests often take priority over those of African countries. This has been particularly evident in the area of tax governance, where policies have often been shaped to protect the interests of developed countries and their multinational corporations through trade and investment (Johannesen et al. 2020; Latif 2020).

Many of these challenges have been addressed by the AU HLP on IFFs and the FACTI Panel. One of the critical challenges that these panels have identified is the lack of transparency in international financial transactions. This opacity enables illicit financial flows and hinders efforts towards international tax cooperation. The skewed balance of power in the global tax architecture is another challenge pointed out by both panels. As it stands today, this architecture largely favours high-income, developed nations, especially those within the OECD, often leading to the marginalisation of lower-income and developing countries. Furthermore, the current international legal and policy frameworks fall short in their attempts to prevent illicit financial flows. These frameworks often do not adequately address aggressive tax planning strategies and weak regulation of multinational corporations. There is also the issue of capacity constraints. Low-income countries often do not possess the technical capacity, resources, and infrastructure necessary to combat illicit financial flows and to implement complex tax systems effectively. Despite these challenges, there are numerous opportunities for significant advancements.

Both panels underscored the necessity of a more inclusive, equitable, and transparent global tax system. This system would allow all nations to participate in the decision-making process, ensuring that the needs of developing nations are acknowledged and respected. Revamping international legal and policy frameworks offers another opportunity to prevent tax evasion and aggressive tax planning more effectively. Additionally, international cooperation could significantly contribute to capacity building in developing countries. This cooperation would support these countries in implementing effective tax systems and combating illicit financial flows. The implementation of more robust standards for transparency and accountability in international financial transactions could substantially reduce opportunities for illicit financial flows. This could be achieved through efforts such as automatic exchange of tax information, ensuring transparency in beneficial ownership, and instituting country-by-country reporting by multinational corporations.

The potential benefits of digitalisation have also been recognised. Digital tools and technologies could greatly improve tax administration and compliance. They could also be utilised in detecting and preventing illicit financial flows. One of the opportunities underscored by the FACTI panel is the proposal of a global minimum corporate tax rate. This could help curb tax competition and profit shifting. Another possibility suggested by both panels is the expansion of the mandate of the UN Tax Committee. A broader range of international tax issues could be included in this mandate, thereby providing a more inclusive platform for global tax cooperation. By addressing these challenges and harnessing these opportunities, the AU HLP on IFFs and the FACTI panel emphasise the potential to significantly reduce illicit financial flows, enhance tax cooperation, and mobilise domestic resources for sustainable development.

The outcomes and recommendations of the First African Fiscal Policy Forum, jointly organised by the Coalition for Dialogue on Africa (CoDA) and the South Centre, also present a comprehensive overview of Africa's challenges and opportunities in international tax cooperation (CODA/South Centre 2021). The overarching theme of the forum is the need for a more inclusive and transformative international tax cooperation framework that would allow Africa and other developing regions to have a greater say in setting global tax norms and reduce IFFs. This First African Fiscal Policy Forum recognised that the international tax system is characterised by inequalities that exacerbate IFFs, tax evasion, and tax avoidance. These inequalities have left Africa and other developing countries at a disadvantage, leading to substantial revenue losses. At the same time, international aid has stagnated, and foreign direct investment has declined, further emphasising the need for domestic resource mobilisation. The forum's acknowledgement that the ongoing OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS) has not been beneficial to African and other developing countries is significant. The digitalisation of the economy has introduced new challenges in taxing Multinational Enterprises (MNEs), and the measures proposed in the two-pillar solution[5] offer minimal benefits to developing countries. This reality calls for a rethinking of the current international tax cooperation framework, pushing for a more inclusive and transformative approach.

This First African Fiscal Policy Forum emphasises the need for increased representation and participation of African countries in international processes to address taxation issues and IFFs. The forum also identifies the two-pillar solution as a source of concern, as it offers limited benefits to developing countries, especially in the context of their existing corporate tax rates. The forum calls for the need for African countries to find alternative ways to increase tax revenue from activities taking place in their jurisdictions. The forum also highlights the need for a

[5] The OECD's BEPS project consists of two pillars. Pillar 1 aims to tax multinational enterprises (MNEs) based on where they generate profits, especially targeting digital companies without a physical presence. Pillar 2 establishes a global minimum tax to prevent profit shifting to low-tax jurisdictions, ensuring MNEs pay a minimum level of tax regardless of location. These measures represent a major shift in international tax rules to ensure fairer taxation of multinationals.

well-coordinated and coherent approach for Africa in global processes to curb IFFs and ensures that the processes are inclusive and address the peculiarities of African countries. South-South cooperation is identified as a critical strategy in this regard. The recommendation to bring tax negotiations to the United Nations where voices of developing countries would be stronger underscores the forum's push for an inclusive and transformative international tax cooperation framework. Establishing an intergovernmental body on tax matters at the UN would provide an avenue where negotiations take place on an equal footing.

While the AU HLP on IFFs, the FACTI panel, and the First African Fiscal Policy Forum have identified potential avenues for reform, including the implementation of a global minimum corporate tax rate, enhanced transparency measures, and an expanded mandate for the UN Tax Committee, they have found the current OECD proposals to be somewhat lacking. Their concerns signal a disconnect between the international tax cooperation frameworks advanced by the OECD and the unique needs and circumstances of developing nations. The existing asymmetries in international tax norm and rulemaking, chiefly guided by the OECD, represent a recurring pattern where the interests of wealthier nations and multinational corporations often take precedence over those of less economically developed countries. In the context of global taxation, an asymmetry arises when certain conditions or practices inadvertently create a lack of balance or equality between parties. This often manifests in the distribution of power, status, or opportunities, which tend to disproportionately favour one group over another. Applying this concept to the two-pillar framework designed by the OECD, we can see such asymmetries in play, particularly when analysing their impact on developing economies, including African nations. The discussion that follows next puts this into perspective.

3.1.1 Reallocation of Taxing Rights

Pillar 1 focuses on reallocating taxing rights to markets where multinational enterprises (MNEs) conduct significant business activities, while Pillar 2 proposes a global minimum tax for MNEs to curb tax competition and profit shifting. While these pillars appear to address global tax issues, the approach disregards the socio-economic context of African countries in setting tax parameters. For instance, Pillar 2 sets the global minimum corporate income tax rate at 15%. While this rate aims to eliminate the under-taxation of MNEs, it overlooks the fact that the average corporate tax rate across African countries is around 27%, significantly higher than the suggested minimum (ATAF 2021). The unilateral decision to set the global minimum rate at 15% puts African countries at a disadvantage as it potentially limits their taxing rights and could lead to significant revenue losses (McCarthy 2022). It fails to consider that African countries rely heavily on corporate income tax, which, on average, contributes about 18.6% of their total tax revenues, compared to 9.3% in OECD countries (OECD 2020a, b).

3.1.2 Digital Taxation

The current digital tax proposals under Pillar One primarily target highly digitalised businesses and large multinational enterprises (MNEs) with substantial global turnovers. However, this narrow focus may not adequately capture the digital activities and revenue generated by smaller businesses in African economies (Latif 2020). In contrast, UN Article 12B presents a broader framework that encompasses a wider range of digital businesses, including those with lower revenue thresholds. Implementing the Pillar One proposals, as they stand, could introduce administrative complexities for African tax administrations. The calculations and criteria involved in determining taxable digital presence and profit allocation may be more intricate, requiring a higher level of administrative capacity. This can pose challenges for African countries with limited resources and technical expertise in tax administration.

Data collection and availability pose another challenge. Accurately assessing the digital activities and revenue generated by businesses relies on access to comprehensive and reliable data. African tax administrations may face difficulties in obtaining accurate data from digital companies operating in their jurisdictions, particularly if these companies are not fully cooperative or transparent. UN Article 12B, with its alternative framework, places less reliance on the availability of data from multinational enterprises, potentially making it more feasible for African countries to implement. Furthermore, the influence and representation of African countries in shaping the Pillar One proposals have been limited. The formulation of these proposals has primarily been driven by the OECD and its member countries, raising concerns about the representation of African nations and their specific challenges. In contrast, UN Article 12B offers an alternative platform within the United Nations framework, providing African countries with a stronger voice and representation in shaping international tax rules. Given these challenges, exploring alternative approaches such as UN Article 12B becomes significant for African countries. These alternatives may better align with the realities, capacities, and priorities of African economies, fostering a more inclusive and equitable international tax framework for taxing digital businesses.

3.1.3 High Threshold

Further asymmetries are seen in the context of Pillar 1. Its application primarily affects large multinationals with a global turnover of more than EUR 20 billion and a profitability above 10% (OECD 2022). This high threshold neglects a multitude of multinational companies operating within Africa, leaving an expansive portion of the continent's tax base untouched by the new proposals. The framework primarily targets large and highly profitable multinational corporations. However, many developing nations, including those in Africa, host a significant number of smaller multinational corporations that fall below the set threshold for the application of

these rules (Dina 2021). Consequently, the framework fails to adequately address the economic realities of these countries, which is where the first asymmetry arises.

3.1.4 Residual Profits

Additionally, the framework involves the reallocation of only a fragment of residual profits, rather than routine profits (Grondona 2019). This arrangement is particularly disadvantageous for market jurisdictions, including many African nations, which are likely to see lower residual profit margins from multinational enterprises. The segmentation rules that exempt the extractive and regulated financial services industries from Pillar 1's scope are another point of contention, as many African economies heavily rely on these sectors. This exclusion poses a significant challenge for many African nations, given the economic relevance of these industries in the region. Thus, another asymmetry becomes apparent in the sectoral composition.

3.1.5 Global Minimum Tax

A 15% global minimum tax rate is substantially lower than the current corporate tax rates of 25–35% commonly seen across African countries. While such a low global minimum tax rate has been proposed to gain consensus among as many countries as possible, it could also have significant implications for African countries. Firstly, setting the global minimum tax rate at 15% could erode the tax base of African countries if multinational corporations adjust their tax strategies to take advantage of the lower rate. This could potentially result in substantial losses of corporate tax revenues. Secondly, if the global minimum tax is set below the corporate tax rates of African countries, it could diminish their ability to attract foreign direct investment (FDI). Corporations might lean towards investing in countries where they can pay the global minimum, rather than the higher domestic corporate tax rate. Thirdly, it could affect African countries' fiscal sovereignty. Setting tax rates is a significant aspect of a nation's economic policy, enabling it to balance between attracting FDI and generating revenue for public goods and services. A global minimum tax rate that is substantially lower than the existing corporate tax rates might limit African nations' ability to manage their tax policies effectively.

The AU HLP on IFFs and the African Union Commission (AUC) Strategy for Tax share a vision for Africa—a continent with robust tax collection, minimal tax evasion and illicit financial flows, and strong fiscal sovereignty. However, the proposition of a 15% global minimum tax rate, substantially lower than the prevailing corporate tax rates across the African continent, threatens to undermine this vision. In this complex and challenging landscape, AU HLP on IFFs and the AUC Strategy for Tax can play significant roles, using the proposal for a UN intergovernmental tax body as a lever to address these pressing concerns.

Firstly, they can champion the call for a higher global minimum tax rate that aligns more closely with the tax rates of African nations. Armed with data and research, they can lay bare the potential detrimental impacts of a lower rate on African economies, advocating for justice in global taxation. Secondly, they can ensure that every nation, including those from Africa, is represented in the decision-making process within the proposed UN intergovernmental tax body. Inclusion in this arena is paramount in ensuring that African voices are not just heard, but also shape global tax policies. Thirdly, they can extend their reach to African nations, providing technical assistance to help them build robust tax systems and policies. Such initiatives could empower these nations to optimise tax collection, minimise tax evasion, and effectively implement the global minimum tax. Fourthly, by using the intergovernmental tax body as a platform for dialogue and cooperation, they can foster an environment of transparency, ensuring fair tax competition and reducing IFFs.

3.1.6 Administrative and Implementation Challenges

Further, the rules associated with Pillar 2 are decidedly complex, demanding substantial administrative capacity and resources for effective implementation. This might pose a significant challenge for many African tax administrations that may not possess the necessary resources to enforce these rules, thereby reducing their effectiveness. Pillar 2 also introduces potential conflicts with existing tax rules in many African countries, such as issues of interoperability with current tax treaty obligations and domestic laws. The need for extensive revisions to accommodate these new rules could prove burdensome for these countries. The subject to tax rule (STTR) introduced under Pillar 2 of international tax reform can potentially aid tax treaty negotiations by providing clarity and guidance on the treatment of income subject to the global minimum tax (OECD 2020a, b). The STTR sets a threshold for the taxation of certain income at a minimum rate, ensuring that profits are subject to a minimum level of taxation.

In the context of tax treaty negotiations, the STTR can help address issues related to the allocation of taxing rights and the prevention of double taxation. By establishing a minimum tax rate, it provides a standardised approach that countries can refer to during treaty negotiations. The rule can serve as a reference point for determining the treatment of income in cross-border transactions, helping to resolve conflicts and provide a more level playing field in tax treaty discussions. Additionally, the STTR may also encourage countries to revise their existing tax treaties or negotiate new ones to incorporate provisions related to the global minimum tax. This can facilitate the negotiation process by offering a common framework and objective for countries to work towards, thus aiding in reaching agreements that are aligned with the new international tax norms.

However, it is important to note that the STTR is just one component of the broader tax treaty negotiations and may not address all the complexities and challenges involved. Tax treaty negotiations involve various factors, including the

specific interests and objectives of each country. The STTR can provide a basis for discussions, but ultimately, the negotiations will depend on the willingness of countries to reach mutually beneficial agreements that consider their individual circumstances and priorities. Herein lies the potential of asymmetries creeping in. For example, developed nations often have more resources and expertise, giving them a stronger position in shaping the outcomes of the negotiations, alongside political interference. This can result in asymmetrical agreements that may not fully consider the interests and concerns of developing countries.

While the STTR holds considerable promise for aiding developing nations by curbing base-eroding outflows, its practical execution poses intricate challenges. Unlike the Income Inclusion Rule (IIR) and the Under-Taxed Payments Rule (UTPR), which have been incorporated within modifications to the OECD Model Tax Convention, the implementation of STTR requires altering bilateral treaties between states. Importantly, destination jurisdictions that levy a nominal tax below 9% on related payments will be obligated to incorporate STTR provisions into their bilateral treaties with developing nations that are the sources of these payments, *but only when asked to do so* under the OECD BEPS (OECD 2021). This mandate, as delineated by the OECD in 2021, however, only extends to parties that are part of the OECD agreement. This conditional arrangement potentially hampers the effectiveness of STTR. Some of the key intermediary tax havens—states known for their role as channels for capital flows towards low-tax destination havens—may opt not to participate in the OECD deal. Their lack of commitment to this accord could substantially undermine the ability of the STTR to achieve its primary objective. Consequently, the successful implementation of STTR not only depends on policy redesign, but also hinges significantly on the collective commitment of all jurisdictions to equitably align global tax practices.

Further, many African nations lack the necessary expertise and resources to effectively participate in the discussions. The complexities of international tax rules and the implementation of the subject to tax rule can make it difficult for these countries to fully comprehend and contribute to the negotiation process. Developing countries, including African nations, may face a disproportionate burden in terms of compliance costs and administrative challenges. This can create a compliance gap between developing and developed countries, potentially widening the disparity between them. These asymmetries underscore the need for a more inclusive and equitable approach to tax treaty negotiations. It is crucial to consider the specific circumstances and capacity constraints of developing countries, including those in Africa, to ensure that international tax reforms, such as the subject to tax rule, do not further disadvantage them. Addressing these asymmetries is essential to achieving a fair and balanced global tax governance framework.

Also, the process of reaching a consensus within the OECD's Inclusive Framework, particularly under the pressures of an expedited timeline, contributes to the asymmetry in global tax governance by disproportionately affecting developing nations. The essence of this asymmetry lies in the differences in capacity between developed and developing countries to comprehend, negotiate, and implement such complex reforms within a tight timeframe. The OECD's two-pillar approach is a

complex reform of international taxation norms, which requires detailed understanding and careful consideration of implications, particularly for countries with diverse and unique economic contexts like many in Africa. The expedited timeline for these reforms may not afford these nations the requisite time to fully digest the proposals, assess their potential impact, and constructively contribute to the discussions.

Furthermore, countries need sufficient time and resources to develop potential alternatives that would better align with their unique economic realities. An accelerated timeline might undermine this process, pressuring countries to agree to provisions that may not serve their best interests. Given that developed countries typically have greater resources, including expert human capital in tax law and international relations, they are likely better equipped to handle such expedited processes. On the other hand, developing countries, many of which are already resource-strained, may struggle to keep pace. This scenario exacerbates the existing power imbalance between developed and developing countries in global tax governance. It accentuates the asymmetry by potentially side-lining the voices of less-resourced nations, thereby reinforcing the necessity for more inclusivity and fairness in shaping global tax reforms.

The pillars' potential conflicts with existing domestic laws and tax treaties can lead to legislative and implementation challenges. For countries with limited administrative capacity, these conflicts add another layer of complexity, further widening the gap between developed and developing nations. In essence, while the OECD's two-pillar framework aims to curb global tax avoidance, the way it is designed and implemented may inadvertently disadvantage developing nations. This results in clear asymmetries in global tax governance, reinforcing the urgent need for a more equitable approach.

Even with the implementation phase of the OECD's two-pillar framework already underway, concerns surrounding the expedited process remain pertinent for several reasons. Firstly, the repercussions of such profound tax reforms may not be immediate and could require several years to fully manifest. As such, nations need ample time and resources to assess these effects on their economies and formulate appropriate responses. This need is more acute for resource-strained nations that could find the rapid timeline of these reforms overwhelming. Secondly, the global tax landscape is perpetually evolving. The burgeoning digital economy and the emergence of new business models demand the continuous refinement and modification of tax policies. This necessitates nations to remain engaged with the reforms, understand their implications, and devise alternatives if required. The haste associated with the reforms' initial timeline may set an undesired precedent for future policy amendments, potentially placing developing countries at a sustained disadvantage.

Thirdly, the complex nature of these reforms could pose challenges for developing countries in preparing for the implementation phase. Addressing these challenges necessitates substantial capacity-building efforts. The swiftness of the reform process may not provide adequate time for such capacity enhancement, possibly affecting these countries' ability to effectively implement and reap the benefits of

the reforms. Lastly, the principle of tax policy sovereignty stands threatened by the accelerated timeline of the OECD's reforms. Countries should have the freedom to devise tax policies that best align with their unique economic conditions. An expedited reform process could pressure countries into accepting provisions that may not resonate with their needs or preferences, thereby undermining their tax policy sovereignty.

3.1.7 Arm's Length Principle

The arm's length principle (ALP) has been a significant point of contention. This principle, which guides transfer pricing rules, mandates that transactions between related entities should be priced as if they were between unrelated parties. However, this often falls short in reflecting the economic realities of complex multinational operations, as these entities can manipulate transfer pricing to minimise their tax liabilities. African countries, with their limited resources and technical capacities, often find it difficult to enforce ALP, leaving them susceptible to profit shifting by multinationals. One of the alternatives to ALP that has been proposed is the system of formulary apportionment, including the concept of unitary taxation. Under this system, the profits of a multinational enterprise are considered as a whole, rather than attributed to individual entities within the group. These profits are then apportioned to different countries based on a formula that typically takes into account factors such as the proportion of sales, assets, and employees that the company has in each country. The advantage of this approach is that it better reflects the reality of how multinationals operate as integrated businesses, and it can help to reduce profit shifting and tax avoidance.

However, the OECD has not accepted this approach as a replacement for the ALP. Instead, the OECD's Base Erosion and Profit Shifting (BEPS) project has focused on modifications to the ALP and related rules in order to address some of their deficiencies. For example, Action 1 of the BEPS project, dealing with the tax challenges of the digital economy, recognises that the digitalisation of the economy and the rise of multinational digital businesses pose significant challenges to the existing international tax rules, including the ALP. In response, the OECD has proposed a two-pillar solution. The first pillar (Pillar One) includes elements that deviate from the traditional ALP by allocating some profits of multinationals to market jurisdictions, regardless of physical presence. However, this is a limited and specific measure and does not represent a full shift away from the ALP. The second pillar (Pillar Two) of the OECD's solution is a proposed global minimum tax, which would work to ensure that multinational corporations pay a minimum level of tax, irrespective of where they are headquartered or the jurisdictions, they operate in. While this does not replace the ALP, it complements it by providing a backstop that curbs the incentives for profit shifting and aggressive tax planning.

While the proposals under Pillar One and Pillar Two of the OECD's Base Erosion and Profit Shifting (BEPS) project represent progress in international tax cooperation, they may not fully address the specific concerns and challenges of African

countries. For example, Pillar Two, which introduces a global minimum tax, aims to prevent multinational corporations from shifting profits to low-tax jurisdictions. In theory, this could limit the erosion of the tax base in African countries and provide a more stable environment for corporate taxation. However, the effectiveness of Pillar Two for African countries is also contingent on its design. A major concern is the level at which the minimum tax rate is set. If it is set too low, it may not do much to deter profit shifting. Additionally, the 'income inclusion rule' and the 'under-taxed payment rule', which are part of the global minimum tax, may not be easy for African tax administrations to implement due to their complexity and the requirement for sophisticated tax administration capacity. The risk of disputes and double taxation could also increase if countries do not adopt the rules uniformly or interpret them differently.

In light of these challenges, African policymakers, as well as groups like the AU HLP on IFFs, FACTI Panel, the First African Fiscal Policy Forum, and the UN Tax Committee have advocated for more inclusive and equitable solutions in international tax cooperation. They have stressed the need for greater representation of African countries in international tax norm-setting, and for the consideration of alternatives to the arm's length principle, among other things. However, these concerns have not been adequately addressed in the final design and implementation of the BEPS project.

3.1.8 Automatic Exchange of Information

The automatic exchange of information (AEOI) represents another challenge. The AEOI is designed to enhance transparency in tax matters, but its effective implementation demands substantial administrative and technological capabilities that many developing countries lack. This capacity deficit hinders these countries from fully participating in and benefiting from the AEOI, thus undermining the intended level playing field in international tax cooperation (Global Forum on Transparency and Exchange of Information for Tax Purposes 2021).

The AEOI is a global standard designed to enhance transparency and combat tax evasion. It requires countries to automatically exchange non-resident financial account information with the account holders' countries of residence. This is a core requirement acknowledged under the AU HLP on IFF (AU/ECA Conference of Ministers of Finance, Planning and Economic Development 2015). However, the implementation of AEOI is a resource-intensive process. It demands a sophisticated administrative and technical infrastructure capable of collecting, storing, and transmitting vast amounts of sensitive financial data securely. For many African countries lacking such resources, the full participation in AEOI remains an uphill task. Moreover, issues around reciprocity can pose a significant challenge, as information may flow primarily from developing to developed countries, without a similar flow in the opposite direction (UN FACTI Panel 2021).

The AU HLP on IFF's proposed to base the application of AEOI on the principle of 'common but differentiated responsibilities' (AU/ECA Conference of Ministers

of Finance, Planning and Economic Development 2015). This principle recognises that countries have different levels of capacities and responsibilities in addressing global challenges. It acknowledges the need to take into account the varying circumstances and capabilities of countries when implementing international agreements or initiatives. On the contrary, the OECD's current approach to AEOI is based on a more uniform standard of automatic exchange of financial account information among participating jurisdictions. The OECD's Common Reporting Standard (CRS) establishes a global standard for AEOI, promoting the automatic and systematic exchange of financial information between countries to combat tax evasion and promote transparency. Many African countries face significant capacity constraints in terms of resources, infrastructure, and technical expertise. Implementing the CRS requires establishing comprehensive systems for collecting, storing, and exchanging large amounts of financial data. African tax administrations often lack the necessary infrastructure and expertise to handle the complexities associated with CRS implementation effectively.

The effectiveness of the CRS depends on the accuracy and reliability of the reported financial information. African countries may face challenges in ensuring the quality of the data received from financial institutions within their jurisdictions. Issues such as limited resources for data verification and the potential for inaccurate or incomplete reporting can undermine the integrity of the exchanged information. While many African countries have committed to implementing the CRS, the global participation is not yet universal. Some jurisdictions, including certain tax havens and non-cooperative jurisdictions, have not joined the CRS initiative or have not fully committed to reciprocity in sharing information. This limited participation can create gaps in the effectiveness of the CRS and potentially allow individuals and entities to continue evading taxes by exploiting jurisdictions that do not fully participate in the exchange of information. In this regard, ATAF has emphasised the importance of adopting a phased or staggered implementation of AEOI, allowing countries to start with a more manual and request-based approach to information exchange, and gradually transitioning to the automatic model as their capacities develop.

Meanwhile the report on 'Tax Transparency in Africa 2021' under the Africa Initiative indicates significant progress in tax transparency and the exchange of information (EOI) standards among African Union members. It highlights the expanding bilateral EOI relationships and the increased number of EOI requests by African countries, showcasing a growing capacity in combating tax evasion and illicit financial flows under EOI. These advancements underscore the commitment of African nations to enhance their tax administration infrastructures, thereby progressively bridging the capacity gap noted in the implementation of AEOI (OECD 2021).

3.1.9 Country-by-Country Reporting (CbCR)

CbCR is a transparency mechanism introduced under the OECD's BEPS Action Plan to curb tax evasion by multinational enterprises. Despite its intended purpose, CbCR presents several challenges for African countries. The high thresholds for reporting often exclude many multinationals operating in these countries, leaving significant economic activities unreported. Moreover, the restrictions on the use of the information disclosed under CbCR can hamper effective tax administration in developing countries. CbCR is another transparency mechanism introduced to help tax administrations gain a more comprehensive understanding of multinational corporations' activities. However, its implementation presents several challenges for developing countries. Firstly, the reporting threshold for CbCR under the OECD's framework is an annual consolidated group revenue of 750 million Euros, which can exclude many multinationals that have significant operations in developing countries. Secondly, the information in CbCR is often not sufficiently detailed for effective risk assessment, especially in complex sectors. Lastly, there are restrictions on how the information disclosed under CbCR can be used, which could potentially hamper effective tax administration in developing countries.

3.1.10 Beneficial Ownership Transparency (BOT)

BOT is another area with its unique challenges. BOT is critical for curbing illicit financial flows and tax evasion, but its enforcement requires a robust regulatory environment and sophisticated technical infrastructure, which many African countries may lack. Issues such as lack of legal and regulatory frameworks for BOT, difficulties in identifying the actual beneficial owners, and challenges in verifying the accuracy of the reported information further complicate its implementation. BOT is a critical tool in combating illicit financial flows, tax evasion, and other financial crimes. However, creating and maintaining a BOT registry requires a robust legal and regulatory framework, a well-functioning administrative system, and a commitment to ensuring the accuracy and timeliness of the data. These requirements pose significant challenges for many developing countries. Without proper implementation and enforcement mechanisms, BOT efforts may result in a database filled with outdated or inaccurate information, undermining its effectiveness. These challenges, which underscore the asymmetries in the current international tax system, further illustrate the necessity for an inclusive and equitable global tax framework that caters to the unique needs and circumstances of developing countries. This again emphasises the need for a more representative body for international tax cooperation, one which accounts for the perspectives and priorities of all nations, not just the most economically powerful.

3.2 Opportunities

Countering these asymmetries requires inclusive and equitable tax governance. One way to achieve inclusive and equitable tax governance is by implementing the recommendations by the AU HLP on IFFs which requires stronger cooperation, focusing on strengthening independent institutions, facilitating information sharing, and increasing oversight of financial institutions. These measures aim to bolster domestic resource mobilisation and curb IFFs, improving fiscal self-reliance and reducing dependency on foreign aid. In line with this, the UN Resolution 77/244 advocates for inclusive and effective tax cooperation at the international level, which inherently involves mitigating the asymmetries that currently exist in the global tax governance. The same themes of inclusivity, effectiveness, and equity echo through the UN resolution.

The Africa Agenda 2023 (African Union Commission 2015) identifies the need for Africa to recognise and consider its unique circumstances and constraints insofar as domestic resource mobilisation is concerned. African nations, understanding the critical need for this, have started taking steps. Kenya, for instance, has been proactively involved in negotiations at the OECD level to ensure its interests are represented. It has also implemented digital service taxes to ensure tech multinationals contribute their fair share, showing it can adapt to the rapidly changing economic landscape (Government of Kenya 2020). Nigeria has been engaging robustly in capacity-building and technical assistance programmes to strengthen its tax administration and has initiated measures to expand its tax base and improve tax collection efficiency (IMF 2023). The Nigerian government has also expressed commitment to engage in and contribute to global tax policy dialogues, indicating a willingness to actively participate in shaping global tax reforms. Such initiatives from African nations are an encouraging sign of their determination to counter these asymmetries and ensure their interests are well-represented in global tax governance. However, to truly level the playing field, the international community must work towards providing these nations the necessary support and capacity-building opportunities to actively participate in and benefit from global tax reforms.

Given the challenges and limitations of the current OECD process, it is crucial to explore alternative institutional frameworks and recommendations to achieve meaningful progress in international corporate tax reform. The UN Tax Committee, while limited in its advisory capacity, has demonstrated its potential in proposing alternative models. To advance the policy debate on corporate tax, it is imperative to prioritise Africa's active participation and ensure that its unique needs and realities are considered. African countries should actively engage in decision-making processes and advocate for policies that align with their development goals. Therefore, in terms of institutional recommendations, there is a need to strengthen and empower at present the UN Tax Committee to play a more influential role in international tax policymaking. This would require expanding its mandate and ensuring representation from influential finance ministries to bridge the gap between technical expertise and policy implementation. Moreover, the international community should

encourage the exploration and adoption of alternative measures by individual countries and regions. Unilateral measures, such as countering permanent establishment (PE) avoidance, strengthening withholding taxes, and considering alternative minimum taxes (AMTs), can provide a catalyst for change. Coordinated action among countries can mitigate the risks associated with political, economic, and legal pressure.

The Eurodad report on the civil society proposal for a UN convention on tax is highly relevant to the discussions surrounding international tax cooperation and the challenges faced by African countries (Ryding 2022). The report emphasises the need for a transformative and inclusive approach to address the asymmetries and shortcomings in the current international tax system. The content discussed earlier, including the challenges faced by African countries in international tax cooperation, the push for an inclusive and transformative framework, and the call for increased representation and participation of African nations, aligns closely with the proposals outlined in the Eurodad report. The report advocates for the establishment of a UN tax convention as a way to shift the power dynamics in international tax matters and create a more democratic and equitable global tax system. It recognises the inequalities that have marginalised African countries and highlights the importance of bringing tax negotiations to the United Nations, where the voices of African countries and other developing nations would have stronger representation and influence.

The proposal for a UN tax convention is rooted in the principle of sovereign equality and common but differentiated responsibilities. It seeks to address the challenges faced by African countries, such as limited participation, unequal bargaining power, and the need for tailored solutions that consider the unique circumstances and capacities of developing nations. The Eurodad report supports the idea that a UN tax convention would provide a more inclusive and relevant platform for discussions on tax norms, rules, governance, and cooperation. It recognises the need for coordination among member states to ensure a coherent and coordinated approach to international tax matters.

The global pursuit of robust international tax cooperation has been a pivotal discussion point across numerous high-level summits and agreements, illustrated by the Doha Declaration (2008), and the Addis Ababa Action Agenda (2015). An analysis of these agreements unveils a comprehensive discourse on fiscal reform, tax system modernisation, and the containment of tax evasion, domestically and internationally. As we deconstruct these documents further, we also observe a call for making tax systems more ‘pro-poor’, alluding to tax regimes that do not disproportionately impact the economically disadvantaged. A salient point from the aforementioned documents is the urgent appeal for bolstered international cooperation in navigating complex international tax matters. These encompass intricate issues of double taxation, the eradication of tax evasion, and the elevation of transparency within tax systems. The appeal for an international tax cooperation framework or an instrument resonates with these agreements, effectively setting the stage for a more globalised approach to tax policy.

The 2030 Agenda for Sustainable Development also lays the foundation for tax cooperation. A commitment to the significant reduction of illicit financial flows (Goal 16.4) and the strengthening of domestic resource mobilisation (Goal 17.1) underscores the inherent link between effective tax cooperation and sustainable development (UNGA 2015). A judiciously crafted international tax cooperation framework would play a critical role in diminishing illicit financial flows and augmenting domestic resource mobilisation, particularly in the context of developing nations. Simultaneously, Goal 10 of the Sustainable Development Goals calls for a reduction in inequalities. Herein, an effective international tax system becomes instrumental. By ensuring a fair distribution of tax burdens, such a system can have far-reaching impacts on intra- and inter-country income and wealth disparities. The development of an international tax cooperation framework through a United Nations intergovernmental process, possibly embodied by the proposed UN Convention on Tax, aligns seamlessly with the principles laid down in these pivotal international agreements. A framework of this nature holds immense potential to address a broad spectrum of tax-related and financial issues, thereby contributing significantly to global efforts towards sustainable development.

Taking all this into consideration, the passing of UN Resolution 77/244, titled 'Promoting Inclusive and Effective Tax Cooperation at the United Nations', has sparked a debate regarding the possibilities for a UN framework convention for international tax cooperation. This resolution highlights the need to enhance global tax cooperation, particularly in addressing tax evasion, profit shifting, and IFFs. The United Nations provides a platform for inclusive participation, allowing all member states, including low- and middle-income countries, to have a voice in shaping international tax policies. This inclusivity addresses the criticism that the current international tax system is dominated by a few powerful nations. A UN framework convention on tax would take into account the diverse needs and realities of countries worldwide, ensuring that international tax rules are not skewed in favour of developed economies. It would promote a more balanced and equitable approach to tax cooperation. Developing countries, through the UN, could potentially influence the global tax agenda and advocate for measures that align with their specific development priorities. This could help address existing imbalances and ensure a fairer distribution of taxing rights.

The progress made at various international platforms has played a crucial role in advancing the agenda for a globally inclusive, intergovernmental process at the UN in the realm of tax cooperation. Several key initiatives and declarations have contributed to raising awareness, fostering dialogue, and shaping the discourse around international tax governance. Firstly, the AU HLP on IFF has been instrumental in highlighting the detrimental effects of illicit financial flows and the need for global cooperation to address them. The panel's recommendations, particularly its emphasis on transparency measures such as automatic information exchange, beneficial ownership transparency, and country-by-country reporting, have gained continental recognition and support. The panel's work underscores the significance of tackling tax-related issues as part of broader efforts to achieve sustainable development,

including SDG 16.4, which aims to significantly reduce illicit financial flows by 2030.

The African Conference of Ministers of Finance, convened by the United Nations Economic Commission for Africa (ECA), has also played a vital role in shaping Africa's stance on tax cooperation. The declaration 990.LIV adopted by the ministers of finance emphasises the importance of mobilising domestic resources, strengthening tax administrations, and combatting illicit financial flows in Africa. This declaration reflects the commitment of African countries to address the challenges they face in the realm of taxation and underscores the need for a coordinated and inclusive approach. Building on these initiatives, the African Group within the UN General Assembly has been actively engaged in advancing the agenda for a UN intergovernmental process on tax cooperation. The African Group's draft resolution and the subsequent adoption of resolution 77/244 demonstrate Africa's determination to challenge the dominance of the OECD and advocate for a more inclusive and equitable global tax governance framework. The resolution calls for the development of an international tax cooperation instrument through a UN intergovernmental process, marking a significant milestone in Africa's push for a stronger voice in global tax policy discussions.

These collective efforts reflect Africa's recognition of the importance of addressing tax-related challenges and ensuring that global tax governance serves the interests of African countries and contributes to sustainable development through trade and investment on the continent. They highlight the continent's commitment to mobilising domestic resources, combating IFFs, and creating an enabling environment for inclusive economic growth. Furthermore, these initiatives have fostered regional collaboration and knowledge-sharing among African countries. The AU and ATAF have played pivotal roles in coordinating efforts, building technical capacity, and presenting unified positions on tax matters. This regional cooperation has amplified Africa's voice and enhanced its ability to actively participate in international tax negotiations. While Africa's coordinated efforts and participation in the existing tax governance structures have yielded some successes, they also reveal the urgent need for a more inclusive, effective, and fairer international tax system. This brings us to a crucial point of contention: the debate surrounding the establishment of a new global tax body.

4 Conclusion

The 2023 UNSG report (A/78/235) represented a pivotal juncture in the reconfiguration of global tax governance, potentially ushering in a U.N.-centric approach that could rectify entrenched fiscal disparities. Elevating the U.N.'s mandate in shaping global tax directives paves the way for a more pronounced African voice in these deliberations, ensuring that international tax policies resonate with Africa's developmental goals. Such a recalibration holds profound implications for trade, tax, and investment within the continent. In terms of taxation, it offers African nations a

stronger voice in shaping tax norms that cater to their developmental objectives, which could enhance revenue from key sectors like natural resources and digital services. For investment, a UN-centric tax framework could signal a more stable and transparent environment, increasing Africa's appeal to foreign investors and reducing the risk of fiscal exploitation. Collectively, these changes could significantly bolster Africa's economic self-reliance and sustainable growth.

The three options set out in the UNSG report relate to varied levels of regulatory integration and commitment. Option 1 introduces a comprehensive treaty that establishes binding regulations, addressing a spectrum of tax challenges, including those that intersect with trade and investment. Ensuring transparency in information reporting and exchange can streamline trade processes, foster investor confidence, and minimise tax evasion—aspects vital for Africa's economic advancement.

Option 2, with its constitutive convention, offers an elegant blend of structured governance and adaptability. By allowing member states to adopt specific regulatory protocols based on their unique priorities, it accommodates the diverse economic landscapes within Africa. Such flexibility can stimulate trade by enabling nations to harmonise tax policies with their trade strategies. Furthermore, a consistent and transparent governance structure can attract investments by offering clarity and predictability to international investors.

Option 3, while nonbinding, emphasises coordinated multilateral action, acknowledging the heterogeneity of tax landscapes. Such coordination can bolster trade by creating an environment of trust and mutual understanding, encouraging nations to open up their markets and reduce trade barriers. Moreover, the tailored solutions this option promotes can create favourable investment climates, catering to the specific needs of individual African nations.

Of these, Option 2 stands out for its potential to empower Africa in the realms of trade, tax, and investment. A binding yet adaptable framework allows African nations to rectify historical imbalances while actively moulding international tax policies. Such a framework can harmonise tax regulations across the continent, simplifying trade processes and fostering a conducive environment for both intra-African and international trade facilitated under the African Continental Free Trade Area (AfCFTA). Furthermore, by providing a stable and transparent governance structure, it can attract foreign investments, as investors often seek predictability and clarity in tax regimes. Collectively, these advantages position Africa to not only address historical injustices but also to fortify its stance in global economic affairs, fostering a trade, tax, and investment ecosystem that is aligned with its growth aspirations.

The recent adoption of UN resolution A/C.2/78/L.18/Rev.1 advances the second option, which entails creating a binding yet adaptable framework to address the specific tax challenges faced by African nations. This framework is essential not just for addressing the tax-related issues that have been discussed in this chapter, but also for broader economic implications. In terms of trade, a consistent and harmonised tax framework across Africa would simplify the complexities currently faced in cross-border commerce. By aligning tax policies, the resolution will facilitate smoother transactions under AfCFTA, potentially increasing intra-African trade and

making the continent a more integrated and competitive market. For investment, a stable and predictable tax environment is a key determinant for attracting foreign direct investment. The resolution's proposed framework would provide the transparency and stability that investors seek, reducing the risk associated with unpredictability in tax regimes. Clear tax policies and reliable administration are fundamental to fostering a favourable investment climate, thus enabling African countries to attract and retain capital that is crucial for development and economic diversification.

The resolution's focus on advancing a unified approach reflects a strategic ambition to enhance Africa's position not just in the realm of taxation, but also in the global trade and investment landscape. This unified approach is not merely about reforming tax systems, but also about leveraging tax policy as a tool for economic empowerment, fostering conditions that are conducive to sustainable growth and development.

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Decision-Making in a Proposed African Union Tax Governance Structure

Afton Titus

1 Introduction

The international tax landscape is changing rapidly as important tax policy decisions are being made at incredible speeds. In the light of this, I argue that African countries should use this time to seize the opportunity to make some key international tax policy decisions together as a continental body.

I have argued elsewhere that working groups of African countries be created within the African Union ('AU') according to the current regional economic community groupings ('RECs') (Titus forthcoming). Such working groups are to develop regional tax policy approaches to international tax stimuli before presenting such approaches to the AU. The AU working together with the African Tax Administration Forum ('ATAF') is then to ensure continental coherence in policies and identify instances where the approaches would conflict across RECs. In the event of technical tax-related conflicts, ATAF working together with the identified RECs would resolve such conflicts and amend policies where needed. In the event of conflicts arising from the intersection of tax policies with other areas, such as politics or trade, such intersectional conflicts could be resolved through the finding of a common continental position. This could be achieved through the AU's organs working with the RECs to address the non-tax-related concerns that would prohibit the formation of a common continental position. Intuitively, it seems as though many political or trade issues could be simplified if all African countries worked together to defend their common position. In this regard, the AU may be used to defend such a continental position at international tax fora like the OECD's Global Forum on Transparency and Exchange of Information for Tax Purposes or the international tax forum that may be created at the United Nations, or the RECs may

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choose to do so themselves working together in groups of RECs. In so doing, this paper provides an African perspective on the changing global tax governance landscape, especially in the wake of the United Nations resolution to work towards building an inclusive and effective global tax cooperation (United Nations General Assembly 2023).

This proposal ties in directly with the recent Memorandum of Understanding concluded between ATAF and the AU Commission, in which they pledge to strengthen Africa's tax coordination efforts (ATAF 2023). Moreover, the proposed structure would allow ATAF to continue to play a supportive role to African countries in a manner similar to the desire expressed by many AU countries, ATAF, the African Development Bank, UNECA, and others at the Fourth High-Level Tax Policy Dialogue organised by ATAF and the AU Commission in 2020 (ATAF 2020d).

In making this proposal, I flesh out what issues would give rise to technical conflicts and which would give rise to intersectional conflicts that would prohibit the creation of a common continental position. I aim to do this by considering the OECD's Pillar One proposal, which would likely give rise to an intersectional conflict. I will also consider the possibility of implementing a digital service tax ('DST') in African countries which may give rise to technical conflicts across the RECs in Africa. Further to this, the Southern African Development Community ('SADC') and the East African Community ('EAC') will be used as a sample of RECs subject to analysis in this way. Both RECs have at least one member who has implemented a DST as a direct tax. Moreover, ATAF has done some notable work in this area by publishing its DST model (the 'ATAF Model') (ATAF 2020b).

I argue that the governance structure, as applied in this chapter, could assist African countries in developing a common continental position on whether to adopt Pillar One. Moreover, the governance structure could also assist African countries in ensuring that, should they decide to adopt a DST, such taxes are coherent across Africa insofar as they do not conflict with or work against each other.

The taxation of the digital economy has been selected as being relevant for the implementation of this governance structure because the taxation of the digital economy is a priority in Africa. In terms of numbers, Statista indicates that the number of Internet users in Africa has increased from 163 million in 2013 to 540 million in 2022 (Statista n.d.-a). Moreover, there are 384 million users of social media in Africa, with Facebook being the leading media platform in terms of market share (Statista n.d.-b). Given these estimations, it is increasingly frustrating for African countries to rely on a flawed international income tax regime to tax effectively, or even minimally, the widespread use of digital services.

And so was born the idea of a DST, which is a relatively new development. While most African countries make use of indirect taxes to tax giant digital companies, a few African countries have decided to take the direct tax route when introducing a DST.

The overriding purpose of such tax is to directly address the inadequacy of the current international income tax regime to correctly identify where on the planet

profits have been generated and then match that to the country that should have the right to tax such profits (Cui 2019b). In doing so, countries seek to transform the evidence of user-created value within their jurisdictions into taxes collected. If done successfully, this would result in not only an increase in government revenues but also an increase in public confidence in the tax system (Mpofu 2022).

I make the assertion that given the primacy and growth of e-commerce and the appetite for digital services in Africa, Africa may well be on the precipice of seeing an increase in the implementation of DSTs across the continent. In such a setting, it would be prudent to consider how this development would impact the political agreement some African Inclusive Framework ('IF') members have made regarding the OECD's Pillar One proposal. The OECD has presented Pillar One and DSTs as mutually exclusive options.

In this setting, the study of DSTs in the context of global tax governance is particularly relevant given the link between international tax and global trade. Kenya recently announced that it would repeal its DST in order to facilitate a trade deal with the USA (Muiruri 2023). This is despite the fact that it would then create inconsistency within the EAC, following the recent EAC Revenue Commissioners resolution to adopt DSTs across the EAC Partner States (Gahene 2023). It has been reported that Kenya has decided on this route in order to facilitate the conclusion of a free trade area agreement between it and the United States (Banga and Beyleveld 2024).

In this context, this paper proceeds as follows: First, the options available to countries when considering how to tax the digital economy, namely, Pillar One or a DST, are set out. In focusing this discussion on African countries, Part 3 discusses the contributions ATAF has made to assist African countries in this process. Part 4 proposes how both technical and intersectional conflicts may be resolved in terms of my proposed governance structure so as to assist African countries to make their policy decisions freely. This is followed by Part 5 which considers how the EAC, as a REC, should make its policy decisions before moving to Part 5, where SADC's decision-making is analysed. The paper's conclusions are set out in Part 6.

2 Taxing the Digital Economy: The Options

The challenges arising from the taxation of the digital economy have been an issue considered by the OECD for a long time. Since the release of the Base Erosion and Profit Shifting ('BEPS') Action Plan 1 in 2015 (OECD 2015), the OECD has been hard at work to properly bring the profits of highly technology-centred businesses within the international tax rules. The latest development in this saga is the OECD's Pillar One proposal which, together with Pillar Two, is meant to reform the international tax rules to tax the digital economy effectively.

Conceptually, Pillar One is meant to provide new rules to introduce more fairness into the international tax system when establishing the right to tax and how much of this to allocate to countries (OECD 2020a), while Pillar Two is meant to ensure that the profits of some of the world's largest MNEs are subject to tax somewhere in the world through the implementation of a global minimum corporate income tax (OECD 2020b). The OECD has succeeded in gaining significant momentum for the progression of Pillar Two (OECD 2023). However, the Pillar One proposal is still in the design phase.

In terms of its design, Pillar One's new nexus and profit allocation rules to distribute more profits to market jurisdictions are embodied in 'Amount A' while 'Amount B' is meant to provide simplified transfer pricing rules regarding the application of the arm's length principle for baseline marketing and distribution activities (OECD 2020a).

For African countries, the main and contentious issue is the calculation and application of Amount A because most African countries would be the 'market' jurisdiction seeking to tax the profits of the MNEs that operate within their jurisdictions. Similar to the rationale and effect of the permanent establishment rules, African countries, as the market jurisdictions, would only have the right to tax the profits of the world's biggest MNEs if certain thresholds are met. Once those thresholds are met, the MNEs are known as 'Covered Groups'. First, the thresholds are as they apply to the MNEs themselves. The MNEs must have revenues that exceed EURO 20 billion and have profitability that exceeds 10% for two of the past 4 years and on average over the last 5 years, or the MNE has been a Covered Group in one of the past 2 years (OECD 2022). Following this, an African country would have the right to tax if the MNE makes at least €1 million in that jurisdiction according to the sourcing rules, or €250,000 if the African country's GDP is less than €40 million (Ibid). Now that the African country's right to tax is established, 25% of the MNE's revenues that are in excess of 10% of the MNE's total profits is apportioned to the African country based on the proportion of the total MNE profits that are earned in such African country (Ibid).

Should African countries agree to implement Pillar One, they would do so while also agreeing to never adopt a DST—and, if they have one, to repeal it (Ibid). African countries would be making a difficult decision to give up so much of their tax sovereignty in complying with Pillar One, even if the provisions of Pillar One itself were flawless. However, the fact that Pillar One has been, and continues to be, subject to harsh criticism makes this request unreasonable.

Some have commended the OECD for proposing a politically acceptable mechanism by which to tax the digital economy (Elliffe 2022). However, for others, the proposal clearly operates, Dourado (2020) writes, 'as defensive rules against market states'. Aside from the criticisms of Pillar One regarding its lack of focus (Brauner 2020) and that it (along with Pillar Two) is primarily politically driven and pragmatic without embodying any corresponding principles (Ibid; Martín Jimenez 2020), for African countries, the most concerning is the criticism of Amount A and the small amounts of revenue that would be allocated to market countries (Dourado 2020; Astuti 2020).

Developing countries will lose out in the application of Amount A (Li 2021; Mahu Martínez 2021). This is not surprising given the narrowing scope of Amount A over the years. Initially, commentators estimated that Pillar One would have between 620 and 2300 companies subject to it worldwide (Goulder 2021). This estimation has become considerably narrower, with Devereux and Simmler (2021) estimating that only 78 of the world's biggest companies would be subject to Amount A. This number is further reduced by Barake and Le Pouhaër (2023), who in their study reduce this number to 69 by excluding 9 Chinese companies who operate almost exclusively in China.

Moreover, Barake and Le Pouhaër (2023) find that developed countries would collect 77% of the net revenues arising from Pillar One and developing countries the other 23%, although China would collect the majority of this. In fact, the net revenues that the least developed countries would collect are almost null (Ibid). Further, in real terms, Barake and Le Pouhaër (2023) estimate that developing and the least developed countries stand to collect 0.15% of their total tax revenues through Amount A.

There appears to be little motivation for developing countries to agree to implement Pillar One as it is currently designed. In the light of this, the implementation of a DST appears far more promising.

DSTs are attractive insofar as they directly address the issues of where profits arising from digital services should be allocated and how they should be taxed (Cui 2019b). Moreover, DSTs represent a singular opportunity for African countries to increase their tax revenues and expand the tax base at a time when this is critically needed (Magwape 2022). Moreover, if the DST is designed as a tax on location saving, it would fall outside the scope of the income tax treaty framework and would accordingly be relatively easy for African countries to implement (Cui 2019b). A DST would also come with drawbacks. Some have argued that the tax may have the effect of deterring technological development (Mpofu 2022). Also, it is possible that the additional cost of the tax would be passed on to the consumer (Ndjajiwo 2020). As with any new tax, the DST would have its own administrative costs and would place a heavy reliance on obtaining relevant information from foreign revenue authorities (Mpofu 2022). Finally, it has been cautioned that the proliferation of DSTs would likely result in trade wars (Ibid).

It would therefore be prudent for each country to do its own feasibility studies to determine the revenues that a DST would likely generate, the costs involved in administering the tax, and then to compare this to the revenues and costs that would be associated with Pillar One. Barake and Le Pouhaër (2023) performed a limited comparison in this regard, where they compared the revenues from Pillar One against the revenues from a DST in a small sample of countries. Their comparison indicates that while Pillar One and a DST would bring in relatively the same amount of revenues for developed countries, some developing countries would be worse off under Pillar One (Barake and Le Pouhaër 2023). Under the circumstances, it would be necessary for African countries to do their own studies before deciding whether to implement Pillar One instead of a DST.

3 The Role of the African Tax Administration Forum

In beginning such feasibility studies, a useful starting point for African RECs would be the sterling work ATAF has already done in this area.

3.1 ATAF and Pillar One

ATAF has actively engaged with the OECD on Pillar One since 2019 (ATAF 2019b). Moreover, ATAF has largely been in support of the stated objectives of Pillar One; namely, to revise the allocation of taxing rights with the aim of affording market countries more taxing rights and, more generally, to simplify the rules of cross-border taxation (ATAF 2019a).

In this respect, ATAF has had limited success in advocating for African countries. It was successful in introducing an elective binding dispute resolution mechanism for African countries that have no or low levels of mutual agreement procedure (MAP) disputes and meet the criteria for a deferral of their BEPS Action 14 peer review (ATAF 2021). It was also successful in having the extractive industries excluded from Pillar One, although this is through the application of complex rules to determine the eligibility of such extractive firms for this (ATAF 2022). Moreover, it was successful in introducing a lower nexus threshold of €250,000 for countries with a GDP lower than €40 billion (ATAF 2019b).

Such limited success with respect to Pillar One negotiations is in stark contrast with the success ATAF has had more broadly in advocating for the international recognition of Africa's common tax policy position (Lesage et al. 2024). For instance, ATAF's Cross Border Technical Tax Committee successfully had an African-based example included in the OECD's Transfer Pricing Guidelines, the first time this has ever happened (ATAF 2018; Lesage et al. 2024). Moreover, ATAF successfully included a provision in OECD's guidelines on the attribution of profits of a permanent establishment that recognises that African countries use an alternative method in calculating this than the Approved OECD Approach (Christensen et al. 2020; Lesage et al. 2024). Finally, of the six African countries who form part of the United Nations Tax Committee, five of them are ATAF members (Lesage et al. 2024).

In its Pillar One negotiations, however, ATAF has struggled somewhat. For example, it was not able to stop the introduction of a safe harbour rule in respect of marketing and distribution profits (Marketing and Distribution profits Safe Harbour (MDSH)) (ATAF 2019c), although the introduction of a *de minimis* threshold does ensure that many African countries would be excluded from the application of the MDSH (ATAF 2022). In this regard, ATAF notes that the use of the return on depreciation and payroll ('RoDP') for the MDSH is problematic because RoDP is not a recognised profit level indicator in the OECD Transfer Pricing Guideline (Ibid). ATAF adds that there is no economic or policy basis for converting the group 10%

return on revenue ('ROR') into a group RoDP, especially considering that there is no economic link between profit measurements based on RoR and on RoDP (Ibid). Most importantly, ATAF cautions that the use of the RoDP in this way would have a particularly adverse and unfair effect on low-income countries (Ibid). Because low-income countries may have significantly lower payroll costs than high-income countries, this may lead to higher RoDP in such low-income countries (Ibid). Another provision that could have even more adverse implications for African countries is the elimination of the double taxation rule. In terms of this, should an African country be identified as a Specified Jurisdiction, that is, a country within which the MNE earns its income, the African country would have to allow the MNE's residence country to tax the MNE's income by providing a credit or exemption for the MNE's income earned in its jurisdiction. According to ATAF, the effect of this rule is even more insidious than the MDSH (Ibid).

ATAF was also not successful in its bid to have 35% of Amount A allocated to market countries. With each technical note, ATAF has traced how Amount A has progressively become smaller and smaller until the amount that may be allocated to market countries (assuming that there is an amount to allocate) is a mere 25% of the formulaic calculation of a small portion of a part of the MNEs profits. In this way, it is possible to trace the change in tone in ATAF's technical notes from the optimism in the first note about the OECD's recognition that market countries should be afforded more taxing rights to the dejected opposition of the OECD's use of the RoDP for the MDSH.

Through its never-tiring efforts to engage with the OECD on the composition of Pillar One, ATAF has done all that it could to minimise the negative impact of Pillar One on the policies of African countries. For this, ATAF's work is admirable.

3.2 ATAF and Digital Service Taxes

In 2020, ATAF proposed its model legislation for the enactment of a DST (ATAF 2020b). According to ATAF, African countries may feel the need to enact a DST, given the inadequacy of the current international tax rules to provide African countries with the right to tax highly digitalised businesses that have no or very little physical presence in their country (Ibid). Moreover, assuming that DSTs are not structured as income taxes—in contrast to Nigeria's significant economic presence provision, for instance (ATAF 2024)—African countries could enact DSTs unilaterally without impacting their double taxation agreements or the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS (ATAF 2020a). This is particularly important considering the pressing urgency of this issue (Ibid).

In the spirit of such urgency, the ATAF Model is divided into two parts: Part I sets out the substantive rules of the DST, and Part II sets out the tax administrative provisions supporting the implementation of such a tax. In total, the model encompasses 15 provisions, with ten of these setting out the substantive rules. Given space

constraints, this paper shall only focus on the substantive provisions of the ATAF model.

Section 1 of the model recommends the levying of a flat tax between 1% and 3% on the gross digital service revenue earned from the provision of digital services. 'Digital service revenue' is defined in Section 2 as the 'total amount of revenue derived directly or indirectly from or attributable to [the African country] by a company or multinational enterprise (MNE) group in a chargeable period in connection with the provision of digital services'. The commentary to the model notes that Section 2 envisages that digital service revenue materialises through either the direct or indirect payment made from an African country or through such revenue being attributed to such a country, for instance, as a result of user participation (Ibid).

Section 3(1) continues by broadly defining the term 'digital services' as a 'service which is delivered over the internet or an electronic network including through online platforms' while Section 3(2) expands on this by setting out a non-exhaustive list of specific types of digital services such as data services and online advertising services, for instance. Section 4 builds on this by setting out which of these services would result in digital service revenue being attributed to the African country and which would be directly or indirectly derived from such country. Digital service revenue would be derived where such revenue is linked to a user (Ibid). This would include the digital service revenue derived from online marketplaces or intermediate platform services; the facilitation of rental or the use of real property; the facilitation of the vehicle hire services; and the provision of digital content services, online gaming services, and cloud computing services (Ibid). Section 5 defines a 'user' as ' any person that uses, views or otherwise engages with an online platform' before listing specific user-identifying transactions'. Section 7 builds on this by detailing how such users should be located. These identifying methods range from the standard techniques of using the registered address, physical delivery address, or billing address of the user; and the location of the bank account of the payor to the more technologically-demanding exercise of finding the geolocation of the device accessing the service (Ibid).

On the other hand, digital service revenue would be attributed to the African country with the provision of online advertising services; data services; and any other digital service not specifically listed (Ibid). Section 6 usefully provides formulas for the calculation of such revenue with reference to the number of global and country-wide users providing a ratio by which to attribute a portion of the service-provider's global revenue to the African country.

Section 8 goes on to propose a *de minimis* threshold to ensure that the implementation of a DST does not have a chilling effect on the growth of the digital economy (Ibid). ATAF suggests the adoption of two thresholds: one related to the service-providers worldwide turnover and one related to the digital service revenue generated within the African country (Ibid). Moreover, in the calculation of the service-provider's worldwide turnover, section 9 provides an exclusion for intra-group transactions for the provision of digital services. This is in order to provide a reliable means by which to gauge the size of MNE groups through the use of group

consolidated financial statements (Ibid). Finally, section 10 addresses the instance where an African country may choose to draft its DST as an income tax (Ibid). In such event, section 10 allows for the set-off of the DST paid against the service-provider's corporate income tax.

ATAF has done well to provide a high degree of certainty by inserting fairly detailed definitions, although all of the lists in the model are not exhaustive. Moreover, it has done well to be clear about the delineation of the tax base and the calculation of the digital service revenue to be subject to the tax.

My view is that ATAF has done a sterling job in setting out this proposed legislation. Having said that, I would, however, have liked for ATAF to have taken a principled stance on whether it considers the DST to be an income tax or something in the nature of excise taxes and then modelled legislation appropriately. It is noteworthy that ATAF's earlier released policy brief argues that the DST should not be seen as an income tax (ATAF 2020a). Such clarity has not carried through as strongly into the model legislation. Yet this clarity is needed as it would likely allow for the more consistent implementation of a DST across the continent, one that specifically speaks to its purpose of reallocating taxing rights over digital services based on where the profits are generated. Moreover, framing the DST in this way would also allow for its easier implementation as it could be legislated without having to consider the implications of the income tax treaty network across Africa (Cui 2019b; ATAF 2024).

This avenue would of course raise the possibility of the United States threatening retaliatory measures against those African countries who choose to enact DSTs, or offering them trade benefits in exchange for the repeal of their DSTs as was the case with Kenya. In the light of this and as argued in the following part, the governance structure proposed in this paper would assist African countries facing such a situation. The proposed governance structure would position the AU to fulfil its mandate to protect the common position of African countries—in this case, against the United States.

4 The African Union, ATAF, and Building Continental Coherence

Once the RECs have made their policy decisions as detailed below, it is important that these do not conflict across the RECs, and secondly, while not strictly necessary, it would be ideal if the tax policies could evolve to strengthen each other as the RECs learn best practices from each other. This could occur as the RECs work together more closely and more regularly through the proposed structure.

However, the policies could result in a technical conflict or an intersectional conflict—that is, a conflict arising from the intersection of the tax policies with another area, like trade for instance. ATAF, working together with each REC, is best placed to address issues of technical conflicts while the AU is best placed to deal

with intersectional conflicts as the RECs present their positions to the AU and thereby mandating the AU to protect their positions.

In terms of technical conflicts, as a member of all the RECs, ATAF would be in a position to quickly see any conflict across the REC's tax policies. As such, ATAF could work with the RECs to address such issues. In this way, I am of the view that ATAF would provide the best assistance regarding continental coordination decisions, such as the REC's adoption of DSTs.

Possible conflicts that may arise from such decision-making may relate to defining the tax base, deciding who should pay the tax, and the rate of the tax. Because of its knowledge of all the REC's policies, ATAF would have a bird's eye view of the operation of such DSTs across the continent. My view is that by using its model legislation as a guide across all RECs, ATAF could ensure a fair amount of technical harmonisation—if not outright uniformity—across the continent.

In terms of the formation of a continental common position, this may become more complex. I see ATAF's role here as to provide the RECs with as much technical information as is relevant for their context. For instance, when deciding whether the RECs should take a position on whether to adopt the OECD's Pillar One proposal, each REC would need information on what the likely impact of Pillar One would be on each of their members, similar to the way in which Barake and Le Pouhaër conduct their study. Moreover, such impact studies should include information such as how much it would cost their members individually and regionally to adopt Pillar One in terms of the demand on their capacity and the amount of additional income it is expected that Pillar One would produce. It would also be useful to compare such numbers against the cost and possible income of implementing a DST. Armed with this information, it would then be possible for each REC to take a position on whether it should implement Pillar One.

Once all RECs have made a decision, the issue would then progress to the AU. At this stage, the purpose would be to see whether all REC's positions are already common (without any further intervention) or whether there are now conflicting positions.

In the event of conflicting decisions, I am of the view that this would probably occur because of political or trade reasons. Such political inconsistency may arise should the 9 IF members decide to recant their initial consent to the OECD's Pillar One proposal following the impact studies already in circulation and those that would be produced in the future following ATAF's involvement with the RECs on this. Given the consistently reported future dismal performance of Pillar One for African countries, it is difficult to see how a REC could agree to Pillar One based purely on its technical prospects.

The AU would be best placed to facilitate this common position-taking. This is because coordinating and harmonising the policies of RECs towards establishing a common continental position falls squarely within the objectives of the AU in terms of article 3 of the Constitutive Act of the African Union (the 'Constitutive Act'). Moreover, the Constitutive Act provides that one of the functions of the Assembly is to determine the common policies of the AU (Ibid, article 9(1)(a)).

I am of the view that within the AU Assembly, African countries would be able to find a common continental position on the OECD's Pillar One proposal without fear of political fallout, trade wars, or fears of restricting technological development. This is because if the entire continent were to decide that adopting Pillar One would not be to their benefit (as is Nigeria's position and also had been Kenya's), it would be easier for African countries to hold their position in negotiations with other countries who may retaliate. In fact, the AU Assembly would be able to assist with this directly since one of its functions is to promote and defend African common positions on issues of interest to the continent (Ibid, art 3(d)). It should be easier for the AU to hold the common position to reject the OECD's proposal and to defend the implementation of DSTs across Africa if what is at stake for the rest of the world, is access to the African continental market. The call for developing countries to use their numbers to collectively withhold their cooperation in order to shape tax policies is not new (Law 2014).

Moreover, I believe that there is no better time to take up this position. This is because the nature of the digital economy may well be changing the power dynamics in international relations in favour of developing countries. Cui argues that developing countries have a much stronger source claim to the profits generated by digital services than they have ever had for any other type of profit, given the low-cost nature of digital services (Cui 2020). If the profits cannot be attributed to the supply side of profit generation—because the costs are low—then the bulk of the profits must be attributed to the markets (Ibid). Also, the digital companies of the world need access to as many markets as possible for their business model to thrive. This makes these companies—and their countries of residence—vulnerable to threats to refuse them market access, especially if this is done in concert with other countries. There are, of course, only so many markets in the world.

I do acknowledge, however, that this would be the best-case scenario, and given how protective African countries are of their sovereignty—even of the AU—it is unlikely that they would allow the AU to act in this way. It may also be that it is not politically possible to form a common continental position. I would then suggest that the RECs all adopt the position to reject the OECD's proposal. I would further suggest that the RECs negotiate in groups to address the response their common position would elicit. I would also recommend that the AU Executive Council, together with the Specialised Technical Committees, provides reports and recommendations to the RECs as to how best to navigate the trade aspect and other areas that would become negotiation points. Such information should make it easier for the RECs to defend their common position, especially if they are doing so in groups—the larger, the better. Moreover, ATAF could also assist the RECs should they require technical assistance in the event of other taxes becoming the point of discussion with non-African countries.

I argue that my proposed structure has the best chance of allowing the AU to carry out its functions as set out in its Constitutive Act. Moreover, my proposed structure would allow the AU to meet one of its important objectives; namely, to establish the necessary conditions that would enable the continent to 'play its

rightful role in the global economy and in international negotiations', as espoused in article 3(i) of the Constitutive Act.

Against the backdrop, how the RECs may make the decisions that the AU is to defend will now be considered.

5 Decision-Making and the East African Community

For the EAC, the issue is whether it should support Pillar One and, if not, whether it should adopt a DST regionally.

Only two of the EAC Partner States are members of the OECD's IF. In the IF negotiations, while the Democratic Republic of Congo ('DRC') consented to the OECD's Proposal, Kenya was one of the countries that refused to agree. The reasons for Kenya's stance are clear. According to the OECD, only a 'modest gain' in corporate tax revenues may follow the implementation of Pillar One (OECD 2020a). Others have commented that the calculations of Amount A may result in only a tiny amount being allocated to market countries in the end (Astuti 2020; Li 2021). As most of the EAC Partner States would be 'market' countries, this is an important point to consider. Barake and Le Pouhaër's (2023) study puts numbers to the possible impact of Pillar One for those who belong to the IF. According to the study, the impact on the EAC would be as follows (Table 1):

Although Table 1 only includes the impact on two of the seven EAC members, the numbers are not comforting. As the table indicates, the DRC would see only a 0.07% increase and Kenya a 0.05% increase in the total taxes collected by them. This is a very slim margin by which to cover the costs of administering Pillar One. Pillar One is meant to act as an overlay over the existing international tax rules. This would likely have the effect of further straining the already constrained capacity of the revenue authorities in the region, while there is very little hope that the taxes collected from Pillar One would replenish the resources used in its administration.

Of particular relevance for the EAC is to consider the scope of Pillar One versus that of DSTs. Pillar One would only cover 11 in-scope companies, while Kenya's DST covered 89 companies (Goulder 2022). There could be no rational, logical tax-based reason to accept this sort of trade-off. A further complication is that in February 2023, at the 50th East Africa Revenue Authorities General Meeting, a resolution was adopted that the EAC revenue authorities would all adopt a DST

Table 1 Pillar One impact on EAC members

Country[a]	% Taxes collected
Democratic Republic of Congo	0.07%
Kenya	0.05%
Average	0.06%

[a]Source: Mona Barake, Elvin Le Pouhaër, Tax Revenue from Pillar One Amount A: Country-by-Country Estimates, 2023, Appendix A, Table A.1

(Muiruri 2023). Given this development, an undertaking to adopt the OECD's Pillar One would not align with this recent regional resolution.

Under these circumstances, it would not be in the best interest, or further the agreed objectives, of the EAC to adopt Pillar One. Having said that, the DRC has agreed to the OECD's proposal. This is an issue of intersectional conflict which would have to be addressed by the AU, as further discussed in Part 6 below.

Should the EAC decide not to adopt Pillar One because it has too little to gain from the proposal, the next issue to consider is whether the EAC should adopt DSTs in the region. In terms of the data provided by UNCTAD in Table 2, the EAC region has seen an increase in the import of digital services to the region from 2008 to 2021 (UNCTAD n.d.).

According to UNCTAD and as reflected in Table 2, Kenya has seen an almost 200% increase in the import of digital services, while Uganda has seen over a 500% increase from 2008 to 2021. In the light of these numbers, it makes sense that the EAC Revenue Commissioners adopted the resolution they did in February 2023—a DST is necessary for the region. It would now be useful to consider the existing DST legislation in the region.

The most recent direct DST was legislated by Tanzania in 2022 (Tanzania: Income Tax Act, Chapter 332, 11 of 2004, s90A(1)). The Tanzanian tax is levied on non-residents only and is triggered by the payment for the rendering of services through a digital marketplace (Ibid). A 'digital marketplace' is 'a platform enabling direct interaction between buyers and sellers of electronic services' (Ibid, section 3). The rate is 2% of the gross payment made for such services (Ibid, section 90A(1)). This tax has been modelled closely on the Kenyan direct DST.

Kenya's DST was introduced in 2021 and was triggered by income accruing to a non-resident from a business carried out over the Internet or an electronic network, including through a digital marketplace (Kenya: Income Tax Act, Chapter 470, s12E(1)). A 'digital marketplace' was defined as 'an online or electronic platform which enables users to sell or provide services, goods or other property to other users' (Ibid, section 3(3)(ba)). The rate was 1.5% of the gross consideration received or the amount paid for the service (Ibid, Third Schedule, item B(12)). Initially, the tax applied to residents and non-resident digital service providers and was amended in 2022 to only apply to non-residents who do not have permanent establishment in Kenya. It was announced in March 2023 that Kenya would be repealing its digital service tax with effect from July 2023 (Mukere 2023).

The regulations in Kenya and Tanzania share similar rules regarding source. Both jurisdictions look to establish this by locating the user of the service (Kenya: Income Tax (Digital Service Tax) Regulations, 2020, section 5; Tanzania: Income Tax (Non-Resident Electronic Services Provider) Regulations, 2022, section 5). This may be done through the use of proxies, namely the residence proxy, the payment proxy, and the access proxy (Ibid). The residence of the user is assumed through using the business, billing, or home address of the user as a proxy (Ibid). The payment proxy is established through the banking details and card information of the user (Ibid). The access proxy is established through the user's Internet

Table 2 Import of digital services to the EAC measure (US dollars at current prices in millions)

Economy[a]	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Burundi	16	14	26	27	37	32	45	34	28	34	31	36	36	45
Kenya	537	550	663	700	767	821	938	963	946	1062	1518	1479	1502	1587
Rwanda	–	–	18	15	13	18	15	36	40	60	57	72	52	64
South Sudan	_	_	_	_	–	–	72	146	216	188	163	31	83	88
Tanzania, United Republic of	183	277	257	259	283	247	319	305	278	324	446	319	341	451
Uganda	191	295	395	609	501	798	1147	918	699	606	770	793	1405	1173

[a]Source: UNCTAD International trade in digitally deliverable services, value, shares, and growth, annual

protocol address or the country code of the mobile phone used to access the digital service (Ibid).

There is also a similarity in the types of services that would fall within the scope of this tax. Both jurisdictions provide a non-exhaustive list of digital services, which includes electronic data management; downloadable digital content; streaming services; access to subscription-based media; search engine and automated helpdesk services; electronic booking services; and online distance training (Kenya: Income Tax (Digital Service Tax) Regulations, 2020, section 3; Tanzania: Income Tax (Non-Resident Electronic Services Provider) Regulations, 2022, section 3). From the description of the services, it is clear that the tax is meant to target the big digital service providers like Netflix, for instance.

It appears as though the EAC Partner States are using, or plan to use, the Kenyan DST legislation as a template from which to develop their own legislation. This may not be bad as Kenya's legislation has done well to provide a relatively comprehensive definition of the digital services to fall within the scope of the tax and how the source of the income subject to the tax should be determined. In terms of modelling legislation for the region and how the existing template may be improved, ATAF's draft legislation would be useful here. For instance, the ATAF model proposes a rate between 1% and 3%. While Kenya and Tanzania do fall within this range, the EAC Revenue Commissioners' resolution calls for a 5% tax. It may do well for the EAC to adhere to ATAF's recommendation unless all the other African RECs also impose a rate of 5%. Having said that, it may also behove the EAC to consider ATAF's warning not to have the DST deter digital innovation and access in the region. Should the EAC impose a DST of 5%, it may then be prudent for them to also adopt ATAF's proposed *de minimis* rules.

The EAC should also consider including ATAF's provisions on the calculation of the income that is to be subject to the DST. ATAF's depiction of income directly or indirectly derived from the region and income that is attributed to the region based on the type of digital service is useful in this regard. Further to this, the EAC should also adopt the rules and formulae for calculating such income as suggested by ATAF.

In sum, when deciding whether to adopt the OECD's Pillar One proposal, the EAC's likely response would be a 'no'. Regarding whether to adopt a DST, the EAC's answer here should be a 'yes'. Moreover, the EAC has already decided to do this despite Kenya's recent decision to repeal its DST. I recommend that the EAC build on Kenya's DST by adding certain aspects of the ATAF model legislation, as discussed.

6 Decision-Making and the Southern African Development Community

Similar to Part 5 above, it will now be considered whether SADC should adopt the OECD's Pillar One proposal and, if not, whether a DST should be adopted instead.

Of the 16 SADC members, 9 belong to the IF. Moreover, all 9 have consented to Pillar One. Despite this, not one has taken steps to adopt the principles of Pillar One

into their domestic legislation. Such reticence is understandable given the recent studies indicating the likely dismal impact Pillar One would have for developing countries. In terms of what this would mean for the SADC members individually, the Table 3 reproduces Barake and Le Pouhaër's (2023) findings:

In terms of Table 3, the most SADC members may possibly gain from the adoption of Pillar One is a 1.58% increase in their total taxes collected, while the worst that some may expect is a decrease of 2.17% in their total taxes collected. Barake and Le Pouhaër (2023) have classified Mauritius and the Seychelles as tax havens which, according to their calculations, would suffer the most adverse effects of the implementation of Pillar One (Ibid). Interestingly, South Africa has not been so classified, and yet it would suffer a more adverse impact than Mauritius. From a regional perspective, however, the impact of Pillar One would see an average decrease of 0.25% in the total taxes collected in the SADC region. Regardless of the political pressure that may come to bear on countries to follow the dictates of the OECD, numbers such as these cannot translate into a rational, logical reason for SADC to adopt the provisions of Pillar One into their domestic legislation. Given these circumstances, it would now become a political decision whether SADC should act on their initial consent to Pillar One. Such a discussion would be more suited for discussion within the AU, as discussed further in Part 6.

Assuming for the purposes of this discussion that the numbers would dissuade SADC from adopting Pillar One, the next issue is whether its members should adopt a regional DST.

The only country in SADC that has adopted a direct DST is Zimbabwe. In 2019, Zimbabwe introduced a 5% flat rate on the gross income of non-resident providers of satellite broadcasting services or those who provide or deliver goods and services as an electronic commerce operator through an electronic commerce platform (Zimbabwe: Income Tax Act, Chapter 23:06, s12A). An 'electronic commerce

Table 3 Pillar One impact on SADC members

Country[a]	% Taxes collected
Angola	0.12%
Botswana	0.03%
DRC	0.07%
Eswatini	−0.56%
Mauritius	−0.29%
Namibia	0.04%
Seychelles	−2.17%
South Africa	−1.03%
Zambia	1.58%
Average impact on Region	−0.25%

[a]Source: Mona Barake, Elvin Le Pouhaër, Tax Revenue from Pillar One Amount A: Country-by-Country Estimates, 2023, Appendix A, Table A.1

platform' is defined as 'a service which by the use of a telecommunications service or electronic means (and whether mediated by computers, mobile telephones or other devices) sells and delivers goods and services to customers' while 'satellite broadcasting service' is defined as 'a service which by means of a satellite (whether or not in combination with cable optical fibre or any other means of delivery) delivers television or radio programmes to persons having equipment appropriate for receiving that service' (Ibid, section 12(8)). Zimbabwe has a *de minimis* threshold, and the tax will only be levied on income above US$ 500,000 (Ibid, section 12A(2)).

Zimbabwe's tax is quite broad insofar as it could apply to any service provided online with little in the way of definitions to rein in the scope. Moreover, the tax is triggered by the single criteria of payment being received by a non-resident from a resident (Ibid, sections 12(6) and (7)). There are no further provisions in the Income Tax Act as to how to determine that the payment was made by a resident—would this be assumed based on the in-country banking details of the payor, or would this be determined based on the payor's address or through the identification of the payor as a resident of Zimbabwe? Zimbabwe's legislation in this respect is quite brief.

The next question is whether other SADC members should do the same. According to UNCTAD, the import of digital services within the SADC region has seen a rapid and sustained increase from 2008 to 2021 (UNCTAD n.d.).

As indicated in Table 4, one of the most dramatic increases in imported digital services is in the DRC, where only US$703 million was imported in 2008 compared to the US$ 1.7 billion imported in 2021. In fact, on average, the SADC region has seen a 128% increase in the import of digital services over this period. The numbers alone could therefore justify a decision to adopt a DST.

Should the decision be made on this basis, it would be advisable for SADC members to consider adopting ATAF's model legislation. ATAF's model is far more comprehensive than Zimbabwe's legislation and would do well to define the parameters of the tax as well as how it is to be calculated. SADC members may also wish to consider whether they will follow Zimbabwe's example regarding the rate. Zimbabwe's rate of 5% is higher than ATAF's suggested range; however, the 5% rate would align with the rate called for by the EAC's Revenue Commissioners. This would indicate the beginnings of a harmonised rate should two RECs choose to adopt the same rate with the base and calculations largely adhering to the ATAF model.

In sum, because the numbers do not support SADC following through on its consent to adopt Pillar One, non-tax considerations would factor into the final regional position on this point. The AU would be best placed to assist with this. In the event that Pillar One is not adopted, a DST would be needed. It is recommended that SADC follow ATAF's model legislation in this regard.

Table 4 Import of digital services to the SADC region measure (US dollars at current prices in millions)

Economy[a]	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Angola	11,348	9100	7992	10,489	10,324	11,294	11,927	9001	6116	6418	3807	2861	2187	2520
Botswana	236	286	390	420	248	326	503	463	405	553	571	609	727	749
Comoros	12	14	16	19	17	19	19	21	20	23	26	26	27	–
Congo, Dem. Rep. of the	703	685	818	901	861	784	813	753	970	582	1203	903	1142	1714
Eswatini	386	276	513	69	82	85	111	49	77	102	106	78	93	110
Lesotho	88	111	73	98	102	80	77	66	58	70	67	64	54	58
Madagascar	636	526	561	439	416	395	272	239	224	298	355	321	282	376
Malawi	40	49	48	63	68	91	97	95	79	97	132	147	149	93
Mauritius	757	659	898	1345	1360	1060	911	804	778	808	804	764	680	727
Mozambique	298	303	457	802	1270	1755	2324	1725	2300	2046	3546	1715	1730	1504
Namibia	202	227	344	288	259	373	419	347	303	258	238	278	223	317
Seychelles	88	84	83	91	185	270	279	289	265	273	380	386	307	186
South Africa	4328	4627	6156	6528	6121	6419	6163	6029	6530	6828	6680	6720	6210	7161
Tanzania, United Republic of	183	277	257	259	283	247	319	305	278	324	446	319	341	451
Zambia	94	76	110	180	231	549	399	251	252	281	311	291	220	213
Zimbabwe	49	304	479	514	506	552	556	487	518	447	352	327	326	411

[a]Source: UNCTAD International trade in digitally deliverable services, value, shares and growth, annual

7 Conclusion

Regionalism has long been vital to the development of Africa (Olu-Adeyrmi and Ayodele 2007). In fact, some of the oldest recorded regional cooperative efforts in trade and monetary integration emanate from Africa (Aniche 2020). As Africa has recently moved to adopt its most ambitious effort yet to create continental unity through the adoption of the African Continental Free Trade Area Agreement, some have pondered how to ensure greater integration without erasing the good work RECs have made across the continent.

The governance structure I propose would ensure that RECs are integrated into a broader governance structure that would also enable the AU to fully meet its own objectives. In order to illustrate the decision-making involved in this structure, this paper sets out how one of the biggest and most complex conundrums in international tax today—the effective taxation of the digital economy—could be addressed by the RECs assisted by the AU and ATAF.

In doing so, I argue that when deciding on issues that require coordination among African countries, such as in the case of DSTs, the RECs should work closely with ATAF. This would allow for ATAF to play a coordinating role across the continent as it would identify technical points of incoherence across RECs and work towards their elimination. Once the design aspects are complete, the RECs will present their tax policies to the AU. This would allow the AU to identify any issues of intersectional conflicts that would entail the REC's tax policies possibly conflicting with policies in other areas, such as trade for instance. In the event of such conflict, the AU organs, such as the specialised technical committees, may work with the RECs to make recommendations as to address and eliminate these conflicts.

In respect of issues that require a common continental position, for instance, when deciding whether Proposal One should be adopted, the first step would be for ATAF and the RECs to work together to put numbers to the impact that Proposal One may have on each individual African country and also on the region. Given the findings of recent studies, Pillar One is not expected to bring in much revenue for developing countries. It is therefore likely that for most African countries, the cost of implementing Pillar One would outweigh the revenues it would generate. If only the tax aspects of Pillar One were to be used when deciding whether to implement Pillar One, the answer across African RECs would probably be uniform—that is, the answer would be no. Such a common position would give rise to non-tax concerns, namely, the prospect of trade wars or threats to close off trade. I argue that such concerns would best be addressed through the AU as one of the AU's functions is to defend common continental positions in its bid to act in the best interest of Africa and her people. While I am aware that the AU has been criticised as not having the resources or political will to carry out its mandate, my view is that the OECD's fundamentally unfair proposal in Pillar One could be a unifying factor as has never before been seen in international relations. One of the only views that Pillar One has succeeded in solidifying across the globe is that Pillar One does not benefit developing countries.

In such unprecedented circumstances, I am of the view that DSTs could serve as the great equaliser across the developing and developed world (Cui 2019a). Developed countries may have invented the technologies, but developing countries are creating mechanisms by which their contributions to such technologies can be taxed effectively. If the structure I propose in this paper is used to its fullest potential, the taxation of the digital economy could be Africa's greatest opportunity to level the international tax playing field.

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