BY E-MAIL

21 June 2024
Attention: Chair of the Ad Hoc Committee
Mr. Ramy M. Youssef

Dear Mr. Youssef

We are grateful for the opportunity to submit our comments on the zero draft Terms of Reference (ToR) for the United Nations Framework Convention on International Tax Cooperation (Framework Convention). The Framework Convention is essential to ensure that international tax rules support the progress of Sustainable Development Goals (SDGs).

Our feedback aims to contribute constructively to the refinement of the ToR, with explicit recognition of the following fundamental shifts in the international tax system and the risks and opportunities that arise:

1. The Challenge of Multilateral Power

Through collective action catalysed by the Base Erosion and Profit Shifting (BEPS) negotiations, standard and law-setting power has shifted to the multilateral level. The two-pillar solution has set the precedence for multilateral bodies to set standards and even model laws that constrain domestic tax systems. Going forward, we can expect this trend to continue as global coordinated action is required to address global agenda items such as climate action.

2. Risks and Opportunities

This sets the path for the type of global cooperation needed to address global challenges and create global public goods. However, without explicit recognition of power dynamics and interests of different countries, the outcome of such global systems can result in inequitable outcomes.

3. The Imperative for Global Action

Tackling tax avoidance and improving the coherence of international tax rules are urgent priorities to enable domestic resource mobilisation. However, as observed during the BEPS two-pillar negotiation process, the ultimate allocation of taxing rights between jurisdictions is often a contentious determinant of agreement. Without explicit agreement on whether there is an acceptance of the erosion of taxing rights even when justified by "fair taxation", the process can be ineffective.

The General Assembly's Resolution 78/230 and the Human Rights Council's[1] discussions highlight the need for a fairer and more inclusive global tax architecture to support SDGs and human rights.

Yet the global report card for SDG Goals and targets of the Paris Agreement continue to fall short of the required progress. The 2023/2024 Human Development report describes us as in a "gridlock". One of the causes identified include "geopolitical quagmires abound, driven by shifting power dynamics among states and by national gazes yanked inward by inequalities, insecurity and polarization."

[1] Sixth Intersessional Meeting of the Human Rights Council on human rights and the 2030 Agenda (18 January 2024)

Before proceeding, it is crucial to address whether there is agreement on whether there is **a need for a change in how taxation rights are allocated.** Advocates for substantive change would point to the way the international tax system is structurally designed to favour developed countries due to their greater influence in setting of tax rules. In turn, this results in inequitable distribution of global tax revenues and consequently barriers to sustainable development in developing countries.

Depending on the prevailing perspective, the Framework Convention can then take one of the following approaches:

Approach 1 – Status Quo: Assuming that the answer is that there is no need for a change in the way that taxation rights are allocated with the status quo largely preserved, then the role of the Framework Convention as a tool to advocate for equitable outcomes will be limited.

This approach is likely to result in broader participation at the cost of a loss of opportunity for substantive change. Nonetheless, the Framework Convention will still be a critical instrument to raise issues and ensure that where required, the consensus approach is modified to be more inclusive.

Approach 2 – Reallocation Approach: This preferred and ambitious approach requires a willingness to participate in change, for purposes of enabling equity and avoidance of globally detrimental outcomes in the long term.

Explicit in this commitment should be a willingness to accept that the allocation of taxation rights based on objectives of equity may result in the erosion of individual jurisdiction's taxation rights.

The Framework Convention can be more ambitious with principles that are based upon concepts of equity and human rights.

In either case, the Framework Convention is an important first step to both capitalise on the opportunity for global cooperation as well as address the risk of inequitable allocation of global tax resources. With the explicit agreement of objectives, an inclusive global governance instrument that is empowered to manage the new multilateral dynamics can be achieved.

Based on the above approach, the following section will provide some comments on specific sections of the Zero Draft.

1. Objectives

a. We refer to item 7b of the Zero Draft which indicates that the Framework Convention should achieve the following:

> "Establish a system of governance for international tax cooperation capable of responding to existing and future tax and tax-related challenges on an ongoing basis, while **respecting the tax sovereignty** of each Member State" (emphasis added)

In light of the global shift towards international tax being based on global consensus and limits on domestic tax systems, the boundaries of "tax sovereignty" have shifted. Therefore, instead of being premised on the objective of "respecting tax sovereignty", it would be clearer to agree on where limits on the domestic tax system arising from global consensus require specific or preferential consideration

For instance, where the multilaterally agreed consensus results in impediments to fundamental human development goals or results in significant inequity, such limits on domestic tax systems can be met with specific compensation measures.

b. We refer to item 7c of the Zero Draft which indicates that the Framework Convention should achieve the following:

> "Establish an inclusive, fair, transparent, efficient, equitable, and effective international tax system for **sustainable development**, with a view to enhancing the legitimacy, certainty, resilience, and fairness of international tax rules, while addressing tax related illicit financial flows and other challenges to strengthening domestic resource mobilization." (emphasis added)

Under **Approach 2**, a stronger emphasis on human rights principles is warranted. This can be achieved through the definition of "sustainable development" to be aligned with the Sustainable Development Goals (which explicitly integrates human rights) as set out in the 2030 Agenda for Sustainable Development.

2. **Specific priority areas to be addressed in early protocols**

The shift towards multilateralism in international tax law setting requires a change in approach when addressing international tax reform. Model laws, such as the GloBE rules set based upon multilateral collective levels can have unexpectedly broad implications with significant underlying complexities. In addition to grappling with complexity, the speed at which global events take place means reform cannot always be deferred until there is certainty of outcomes.

As such, priority areas undertaken by the Framework Convention should be clearly formulated, that is, with transparent and agreed definition of scope, boundaries, objectives and underlying complexities. Importantly, where time does not permit full analysis of complexities, there should be a mechanism in place at the multilateral level for feedback and modification of rules.

Applying this approach to early protocols, we propose two priority areas for consideration.

Firstly, the Framework Convention has a collaborative role to play in the **taxation of digitalised and globalised economy**. One of the common concerns with this is the potential for duplication with OECD. We agree that duplication should be avoided. However, the scope of GloBE Rules in terms of potential impact on development opportunities and multilateral dispute resolution leaves room for collaboration without duplication.

In particular, the complex interplay at the domestic level of a limited tax incentive toolkit on sustainable development goals remains uncertain. Currently, the GloBE rules have been set based on consensus. However, there are no mechanisms to allow for collective agreement for reform to the rules. Reactions to concerns or questions are now based upon ad-hoc Administrative Guidance published by the OECD Secretariat. This is a commendable initiative for the initial implementation period, but not a long-term solution, especially with the likely proliferation of issues over time.

Where handled holistically with the framework for financing sustainable development as agreed in the Addis Ababa Action Agenda, the Framework Convention is well placed to receive timely feedback on the impact of the GloBE rules on developing countries. It is also able to propose mechanisms that may be necessary at the collective level to address these issues. Such a mechanism has the potential to mitigate delays for developing countries to raise serious concerns where structural issues exist requiring differentiated treatment.

We would also like to express support for the Framework Convention to spearhead **tax measures on environmental and climate change**, in particular instruments such as the Climate Treaty for Global Taxation of Carbon.[2] As climate instruments are directly linked to sustainable development, universal and real inclusivity is a pre-condition for progress.

* * * * * *

We appreciate the opportunity to share our feedback and suggestions on the Zero Draft and thank you for your time to consider our comments. We look forward to continued engagement as you progress in this important endeavour.

Yours sincerely

Annalise Foong
Director

[2] Falcão, Tatiana (2024) A Climate Treaty for the Global Taxation of Carbon, ICTD Working Paper 187, Brighton: Institute of Development Studies, DOI: 10.19088/ICTD.2024.022

FLEXTAX CONSULTING PTE LTD
21 Woodlands Close #08-44 S737854
UEN 201814718W ⬧ www.flextax.com.sg