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RESPONSE TO OECD PUBLIC CONSULTATION DOCUMENT – ADDRESSING THE CHALLENGES OF THE DIGITALISATION OF THE ECONOMY

Att. Tax Policy and Statistics Division, Centre for Tax Policy and Administration

Please find below our comments on the OECD Public Consultation Document, 'Addressing the Challenges of the Digitalisation of the Economy'.

The undersigned are a group of political science academics working on issues of international taxation. Such a coalition has rarely involved itself in the OECD's technical consultations. This submission reflects two compelling factors. First, the global tax system and its governance stand at a critical junction. The current debate on solutions to the tax challenges of digitalisation has the potential to shape global tax policy and its outcomes for countries and citizens across the world for decades to come – and this has motivated us to prepare this submission. Second, our research offers important insights that can help the global tax policy community pursue sustainable reforms. Below, we offer some general comments before moving to specific responses to the consultation questions.

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General comments

We wish to highlight three key considerations for effective and sustainable action on the tax challenges of digitalisation.

1. **The objectives of the consultation and the taxation of the digital economy policy discussion more broadly are as much *political* as they are *technical*.** By 'political' we mean that the drivers of this consultation are rooted in the popular politics of taxation, and that the political implications of policy solutions are not incidental or secondary considerations. This includes the consequences for inter- and intra-national (re)distribution, for citizens' experiences of fiscal systems, for the viability of global tax governance, and for the wider economic transformations occurring as a result of digitalisation, where tax policy will help determine winners and losers. Historically, the relative isolation of international tax policy-making from popular politics helped produce a remarkably stable cross-border tax system.[1] However, isolation challenges responsiveness to political demands for change.[2] In today's context, international tax politics has become both more mainstream and highly politicized. The risks of not engaging proactively with diverse political stakeholder interests – including ordinary citizens, civil society, business groups (large and small), academia, etc. – are significant. For instance, one reason for the recent struggles of multilateral trade cooperation is that the trade agenda extended into areas where social and environmental concerns implicated new political actors. Yet, the multilateral regime continued to treat these issues through a narrow trade lens. Technical approaches to taxing the digital economy are unlikely to be sustainable unless their substance and the process by which they were produced are perceived as fair by a broad range of stakeholders.

2. **The recent expansion of the OECD's tax policy-making institutions to include non-OECD members brings important dilemmas.** While this expansion represents an important step towards global inclusiveness and accountability, it also calls into question the balance between inclusiveness and the coherence of the global tax system itself. Global economic shifts are raising the profile and influence of historically marginalised countries in global economic governance. In some cases, incrementalism has been enough to satisfy 'rising powers'; in others, dissatisfaction with the status quo has led to the pursuit of outside options or to stalemate over wholesale reforms.[3] The balance between building on the work undertaken over decades and responding to these new challenges is critical for achieving effective and coherent global action on the tax challenges of digitalisation. Institutional expansion at the OECD challenges the historical division of labour

[1] Genschel, P., & Rixen, T. (2015). Settling and unsettling the transnational legal order of international taxation. In T. C. Halliday & G. Shaffer (Eds.), Transnational Legal Orders. New York: Cambridge University Press; Picciotto, S. (1992). International Business Taxation: A Study in the Internationalization of Business Regulation. New York: Praeger.

[2] Sharman, J. C. (2006). Havens in a Storm: The Struggle for Global Tax Regulation. Ithaca: Cornell University Press; Seabrooke, L., & Wigan, D. (2016). Powering ideas through expertise: professionals in global tax battles. Journal of European Public Policy, 23(3), 357–374.

[3] Woods, N. (2010). Global Governance after the Financial Crisis: A New Multilateralism or the Last Gasp of the Great Powers? Global Policy, 1(1), 51–63; Wade, R. H. (2011). Emerging World Order? From Multipolarity to Multilateralism in the G20, the World Bank, and the IMF. Politics & Society, 39(3), 347–378; Clifton, J., & Díaz-Fuentes, D. (2011). From 'Club of the Rich' to 'Globalisation à la carte'? Evaluating Reform at the OECD. Global Policy, 2(3), 300–311.

between the OECD and other bodies for international tax cooperation (such as the United Nations), which allowed one group of like-minded countries to move quickly while the process of global consensus-building could take place at a necessarily slower pace. We believe that the success of institutional expansion is contingent on a serious reconsideration of policies and processes that were not historically designed to accommodate the interests of emerging and developing countries. To turn again to the example of international trade cooperation, developed countries' unwillingness to respond to developing countries' longstanding concerns about agricultural protectionism was a major contributor to the breakdown of the talks.[4]

3. **The move towards binding, global cooperation on taxation creates costs as well as benefits.** The reluctance of governments to enter into binding cooperation has shaped the global tax system for a century, at times hindering effective action and enabling harmful tax competition.[5] Commitments to strong cooperation on international taxation are a key prerequisite for governments' abilities to make and enforce fiscal policies in their own interests.[6] Moreover, given the significance of the tax challenges of digitalisation, and the increasing willingness of states to act unilaterally,[7] the risks of furthering cross-national mismatches and unintended externalities (in the form of double taxation or double non-taxation) in the international corporate tax system are high. Nonetheless, setting the bar too high creates a risk of short-term failure, as the OECD experienced in the past with the Multilateral Investment Agreement, or long-term instability as countries defect from binding agreements. In this context, the sustainability of any policy option depends on managing effective cooperation that prevents harmful tax competition while recognising that it is contingent on meeting the interests and expectations of all its members, and limiting incursions into the design of national tax systems when such a balance is not feasible. Moreover, it is important that each government is open and transparent with its domestic stakeholders about the likely costs and benefits of entering such cooperation.

[4] Clapp, J. (2006) WTO Agriculture negotiations: implications for the Global South, Third World Quarterly, 27(4), 563-577. See also Narlikar, A. (2010). New powers in the club: The challenges of global trade governance. International Affairs, 86(3), 717-728

[5] Rixen, T. (2008). The Political Economy of International Tax Governance. Palgrave Macmillan; Arel-Bundock, V. (2017), The Unintended Consequences of Bilateralism: Treaty Shopping and International Tax Policy. International Organization, 71(2), 349-371;. Genschel, P. and Seelkopf, L. (2016), Winners and Losers of Tax Competition, in Dietsch/Rixen (eds.), Global Tax Governance - What is Wrong With It and How to Fix It (Colchester: ECPR Press), 55-75; Sharman, J. C. (2006). Havens in a Storm: The Struggle for Global Tax Regulation (1 edition). Ithaca: Cornell University Press.

[6] E,g, Dietsch, P. (2015). Catching Capital: The Ethics of Tax Competition. Oxford, New York: Oxford University Press.

[7] Hearson, M., & Prichard, W. (2018). China's challenge to international tax rules and the implications for global economic governance. International Affairs, 94(6), 1287–1307; Lips, W. (2019), Great powers in global tax governance: a comparison of the US role in the CRS and BEPS. Globalizations, 16 (1), 104-19.

Specific comments

What is your general view on the proposals? In answering this question please consider the objectives, policy rationale, and economic and behavioural implications.

4. **Distributional considerations should be foregrounded.** Discussing the three suggestions on revised profit allocation and nexus rules, the consultation document usefully acknowledges that while they all have the objective of recognising value created in market jurisdictions, their implications for shifts of taxing rights are different. These differences, which we take to be highly significant, have implications for the considerations on effective action outlined above. Of the three proposals, the 'significant economic presence' idea, given its greater sectoral scope, seems to offer the potential to shift taxing rights covering most profit, although this would naturally be contingent on the final design of the mechanics.

5. **The emerging differences between taxation on the basis of source and residence vs. market/destination merit further consideration.** The Inclusive Framework is committed to considering solutions that reallocate the tax base. In today's economy, the distinction between source and residence taxation is indeed increasingly unhelpful; yet, there is a risk that a singular emphasis on 'market jurisdictions' may unduly disadvantage traditional source jurisdictions without sizeable markets and limited purchasing power. The interests of these jurisdictions – often less powerful and underrepresented at the OECD – should receive significant attention.

How would you suggest that the rules should best be co-ordinated?

6. **Coordination design is contingent on meeting stakeholder expectations**. A number of implementation measures are available to the Inclusive Framework, including standard-setting, peer review, blacklisting and sanctioning, which have proven effective to varying degrees.[8] These measures differ in their balancing of binding 'lock-in', national flexibility to pursue government policy choices (especially as regards raising effective capital taxation), and international redistribution. All of these critical considerations are interrelated and must be taken into account together in coordination design. For instance, the reopening of the distributional debate on allocation issues has become necessary because of the challenges faced by the current international tax system in enforcing effective capital taxation. Thus, on the one hand, should a workable and commonly agreeable solution that matches all members' distributional interests and national policy choices be found, strong and binding cooperation is preferable. If, however, and we see a real risk of this, the envisaged solution is unfavourable to emerging/developing countries (see previous paragraph), then strong and binding cooperation is undesirable.

[8] Hakelberg, L. (2016), Coercion in international tax cooperation: identifying the prerequisites for sanction threats by a great power. Review of International Political Economy, 23(3), 511-41; Eggenberger, K. (2018). When is blacklisting effective? Stigma, sanctions and legitimacy: the reputational and financial costs of being blacklisted. Review of International Political Economy, 25(4), 483-504.

What could be the best approaches to reduce complexity, ensure early tax certainty and to avoid or resolve multi-jurisdictional disputes?

7. **The consultation should seek to refocus public debate away from *ex post* criticism of the outcomes of tax rules once they are implemented, and towards *ex ante* debate over rules as they develop**. A core component of tax certainty is *political* stability - the certainty of a tax position given the likelihood of future political action affecting that position. Such action may be in the form of legislative initiatives that change tax results, changed administrative practice, or public pressure on companies to alter approaches to tax planning. The stability of any policy solution(s) on the tax challenge of digitalisation developed by the Inclusive Framework depends critically on engaging with the voices and objectives of a broad range of stakeholders, and on a reconsideration of entrenched interests. In this context, the limitations of the consultation to primarily consider ostensibly technical questions on 'aligning value creation' may hinder positive engagement with a broader range of stakeholders. Such consultation design erects barriers of language and expertise that limit diverse engagement, closing off stakeholder engagement.[9] In turn, this may negatively affect the likelihood that its policy outcomes will be broadly seen as fair.

8. **Deeper and broader stakeholder engagement.** In this context, we encourage the OECD and the Inclusive Framework to pursue more proactive engagement with non-traditional and diverse stakeholders in relation to the tax challenges of digitalisation. At the national level, this should mean an active approach to education and consultation with stakeholders around national negotiating positions, and parliamentary debate over the adoption of new rules that moves beyond the rubber-stamping that has thus far characterised the adoption of BEPS outcomes by most countries. At the multilateral level, this would go beyond the currently institutionalised TUAC and BIAC partnerships and the few substantive consultation letters received from non-expert interests, and would include sustained interactions on questions of the political implications of the tax challenges of digitalisation, including the inter- and intra-national distributional implications. Inspiration could, for instance, be drawn from other policy domains of the OECD where non-state actors have been successfully integrated through increased voice and access channels, implementation partnerships, institutionalised reviews, etc.[10] More generally, we suggest the Inclusive Framework could – at a minimum – set out its formal ambitions for the involvement and diversity of stakeholders in global tax policy-making, and specific initiatives to achieve these ambitions.

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[9] Büttner, T., & Thiemann, M. (2017). Breaking Regime Stability? The Politicization of Expertise in the OECD/G20 Process on BEPS and the Potential Transformation of International Taxation. Accounting, Economics, and Law: A Convivium, 7(1); Christensen, R. C. (2017). Professional Competition in Global Tax Reform: Transparency in Global Wealth Chains. SocArXiV: https://osf.io/preprints/socarxiv/gu63m/.

[10] Ougaard, M. (2011). Civil society and patterns of accountability in the OECD. In J. A. Scholte (Ed.), Building Global Democracy?: Civil Society and Accountable Global Governance. Cambridge: Cambridge University Press.