CONCEPT NOTE

Tax policy options for funding the post-COVID recovery in the Global South

23 July 2020

A. Background

The COVID-19 pandemic has negatively affected tax revenue collection globally, with the Global South especially hard-hit. The decline in economic activity has meant reduced corporate profits, declining consumption and increasing unemployment. This in turn implies declining revenue from corporate income taxes, goods and services taxes and personal income taxes. Resource-rich countries are especially being affected by the drop in global commodity prices and decline in international trade.

Governments are implementing tax measures such as deadline extensions, payment deferrals and accelerated tax refunds to lessen the burden on taxpayers and keep the cash-flows of businesses running. However, this is at the expense of lower public revenue, at least in the short-term. This worsens an ongoing trend – developing countries were in any case suffering from declining revenues from a global slowdown in addition to bearing the burden of an international tax system that has historically been against developing country interests. Developing countries have for years called for reforming an international tax system that was built on top of the tax practices within the imperial trading blocs of the 1920s and resulted in significant drain of resources from the Global South.

Cumulatively, these mechanisms would drastically lower domestic resource mobilization in developing countries. This will negatively affect their ability to respond to the COVID-19 crisis and thus constrains their expenditure on healthcare and providing support to households. This also impacts being able to address the gendered dimensions of the crisis with unpaid domestic and care work once again stepping up to increase the already huge subsidy to the global economy. Already, ominous signs of austerity measures are emerging as countries are being forced to slash budgets and place restrictions on government expenditure and fiscal deficits debt. In some cases, tax administrations themselves are being downsized.

It is therefore important to explore what are the concrete tax policy measures developing countries can take to raise revenue at this critical time. For the crisis has also produced winners; the digitalized economy, dominated by a few multinationals based out of the global North, is seeing increased sales and subscribers as demand for their services such as video conferencing grows. The wealth of billionaires has also seen an increase during this period. Hence, redistributive fiscal measures are both possible and necessary.

The Global South has been innovating its own tax policy solutions, suited to its context, both at the domestic and international level. Developing countries have been implementing laws that tax income from digital services and provide nexus to digitalized companies without physical presence but who nevertheless make profits from jurisdictions. At the international level, developing countries are pushing for changes at both the UN Committee of Experts on International Cooperation in Tax Matters (UN Tax Committee) and the OECD/G20 Inclusive Framework with regard to international tax standards on the digitalized economy that will in effect redistribute taxing rights between source and residence jurisdictions.

There has been progress on nexus rules and the concept of Significant Economic Presence has been largely accepted globally, i.e that nexus can be established for digital companies who lack physical presence in a jurisdiction. However, on profit attribution there still remain a diversity of opinions. The G24 group of developing countries had advocated the fractional apportionment method of profit attribution using a four factor formula of Sales, Assets, Employees and Users. This was rather questionably removed from further consideration in the OECD's Unified Approach to Pillar One, but nevertheless has been introduced in the UN Tax Committee as an independent proposal and is being subject to further consideration.

The profit attribution method in the OECD's Unified Approach to Pillar One is a highly complicated mix of modified transfer pricing rules with an additional formulary component. There remains scepticism about its viability and administrability and negotiations are compounded by public disagreements between some of the major economies of the OECD. Developed and developing countries both have proceeded with taking national measures on taxing the digitalized economy and have earned threats of retaliatory measures. These domestic efforts have gained fresh impetus and importance with the revenue requirements posed by the COVID crisis.

In the context of an EU blacklisting process that has seen developing countries being blacklisted for not implementing OECD norms they were not part of negotiating and the threat of retaliatory measures for moving ahead with unilateral measures to tax the digitalized economy, the long held G77 and China call for a principled, inclusive and transparent intergovernmental tax negotiation process at the UN has never been more urgent.

This webinar, organized by the South Centre and the Global Alliance for Tax Justice, will feature prominent voices of the Global South on these ongoing dynamics as well as the national and international tax policy options for funding the post-COVID-19 recovery. The speakers are a diverse mix representing tax administrations, academia and civil society from Asia, Africa and Latin America.

B. Key Issues

The webinar will cover the following topics:

1) Challenges of Domestic Resource Mobilisation (DRM) in the Global South amid COVID-19

2) Redistributing taxing rights to developing countries – the Two Pillar Approach and the way forward from the impasse

3) Alternative international frameworks from the South for taxing the digitalized economy

4) National measures for taxing the digitalised economy

5) Financing the recovery from COVID-19 – domestic options for developing countries

6) South- South cooperation facing the COVID-19 induced socio-economic crisis

C. Time:

The webinar will be jointly organized by the South Centre and the Global Alliance for Tax Justice on **23 July 2020** from **15:00 to 16:45 CET**.