China’s Rising (and the US’ Declining) Influence on Global Tax Governance? Some Observations

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Outline

• Some facts
• Indications of influence in global tax governance
  – Institutional participation and multilateralism
  – International tax norm-setting
• Some observations
Some Facts – Share of global exports (1878-2020)

<table>
<thead>
<tr>
<th></th>
<th>China</th>
<th>USA</th>
</tr>
</thead>
<tbody>
<tr>
<td>1980-90</td>
<td>&lt;5%</td>
<td>About 35%</td>
</tr>
<tr>
<td>1990-2000</td>
<td>Over 10%</td>
<td>About 35%</td>
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<tr>
<td>2000-10</td>
<td>About 27%</td>
<td>About 10%</td>
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<tr>
<td>2010-20</td>
<td>About 45%</td>
<td>About 12%</td>
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Some Facts - Contribution to Global GDP growth

Note: ANZ is Australia and New Zealand
Source: EIU

https://www.bain.com/insights/china-deglobalization-and-the-multinational-article/#
Some Facts - Top 10 countries with highest revenue top 500 companies

<table>
<thead>
<tr>
<th>Rank</th>
<th>Country</th>
<th>Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>China</td>
<td>135</td>
</tr>
<tr>
<td>2</td>
<td>United States</td>
<td>122</td>
</tr>
<tr>
<td>3</td>
<td>Japan</td>
<td>53</td>
</tr>
<tr>
<td>4</td>
<td>France</td>
<td>28</td>
</tr>
<tr>
<td>5</td>
<td>Germany</td>
<td>27</td>
</tr>
<tr>
<td>6</td>
<td>United Kingdom</td>
<td>22</td>
</tr>
<tr>
<td>7</td>
<td>South Korea</td>
<td>15</td>
</tr>
<tr>
<td>8</td>
<td>Switzerland</td>
<td>13</td>
</tr>
<tr>
<td>9</td>
<td>Canada</td>
<td>12</td>
</tr>
<tr>
<td>10</td>
<td>Netherlands</td>
<td>11</td>
</tr>
</tbody>
</table>

Compare: China-based MNEs

- 2008: 10 of top 500
- 1995: 2 of top 500
- 1980: 0

Source:
https://fortune.com/global500/2008/search/?hqCountry=China
Some Facts – *International Tax*

- Tax revenue = bloodline of states
- Income tax = national (taxing = spending > fiscal sovereignty)
- International tax = conflicts of national laws
More Facts: *Chinese Enterprise Income Tax*

- **1978-81**: JVIT/FEIT
- **1983**: First tax treaty (Japan)
- **1991**: FIE and FE Income Tax
- **2008**: EIT
Some Facts – *International Tax*

- MNEs = “global” income
- Multiple countries’ tax laws
Some Facts – *International Tax*

International “consensus” or norms

1) “Nexus” for tax jurisdiction
   - Residence of corporation
   - Source of income

2) “Arm’s length principle”
   - “market” price expected for intra-MNE group transactions
More Facts – *International Tax*

- No international “TAX” organization
- No public international law on income tax
- Network (4,000 or so) bilateral tax agreements
- What institutions have been “in charge” of developing international tax consensus?
- What is China’s role?
### International Institutions & China - UN

- **League of Nations**
  - 1920-46
  - China as a member (USA was not)
  - 1923 Report on Double Taxation
  - 1928 Model tax convention by “Technical experts”
    - China represented

- **United Nations**
  - 1945 - present
  - China founding member
  - PRC became a member of SC (1971)
  - UN Tax Committee (a member from China since early 1980s; sometimes as vice-chair)
  - *UN Model Convention*
  - *UN Manual on Transfer Pricing* (China Practice section)
International Institutions & China - OECD

OECD

• “de facto” tax organization
• 2004: China became “observer” in CFA’s work
• OECD Model Convention

https://www.oecd.org/newsroom/chinasouthafricanparticipateinworkofoecdscommitteeonfiscalaffairs.htm
19. We will continue our support for international tax cooperation to achieve a globally fair and modern international tax system and to foster growth, including advancing on-going cooperation on base erosion and profits shifting (BEPS), exchange of tax information, tax capacity-building of developing countries and tax policies to promote growth and tax certainty. We welcome the establishment of the G20/OECD Inclusive Framework on BEPS, and its first meeting in Kyoto.
International Institutions & China – BEPS IF

- **G20/OECD BEPS Inclusive Framework**
  - OECD → Technical expertise
  - G20 → Political clout
    - accounts for around 90% of [gross world product](#)
    - 75 – 80% of [international trade](#),
    - 2/3 of the [global population](#)
    - roughly 1/2 the [world's land area](#)

- **BEPS 1.0 project**
  - China active participant

- **BEPS 2.0**
  - China as Deputy Chair of Steering Group (as of Jan.2022)
International tax norms
The **Global Tax Deal**

On October 8, 2021, 136 countries of the OECD/G20 Inclusive Framework agreed to a 2-pillar solution to address tax challenges arising from the digitalization of the economy

- **Pillar 1:**
  - creating new taxing rights in market jurisdictions
  - MNE groups with over 10 billion euros in revenue

- **Pillar 2:**
  - creating a floor for a 15% effective corporate tax rate
  - MNE groups with 750 million euros in revenue
“Historical”? 

- First time in history
- Agreed to create a **new “global” tax law** (multilateral tax convention) for Pillar 1
- Agreed to adopt universal **“model” rules** into national tax law (Pillar 1 and Pillar 2)
- Agreed to create a **new class of taxpayers** (i.e. large global firms) and tax them based on “accounting income”
Why did it happen?

1. Tax = bloodline of state
2. Existing international tax system:
   - Outdated rules (100 years old, designed for a physical economy)
   - “unfair”
   - Loss of tax revenue
     ( “large corporations pay little tax” )
3. Political pressure
   - Citizens and local businesses
   - Deficit and revenue shortfalls
China’s Role in Designing the Pillars?

BEPS Action 1

2-pillar solution (Global tax deal)
China’s role in implementing the pillars?
The devil is in the detail

• Pillar 1:
  – “agreement” on “nexus” and “source”/location of sale RULES?
  – “agreement” on tax dispute prevention/resolution?

• Pillar 2
  – US?
  – EU?
  – Developing countries?
Sum up: China & International Tax Norms

Norm-taker

Norm-shaker

Norm-maker?
Some Observations: US Influence

1. Contributor of ideas and principles
   - Basis for allocating taxing rights
     - 1923 Report (Prof. Seligman)
     - 1928 draft model Tax Convention (T.S. Adams)
   - Arm’s length principle (M. Carroll)
   - Worldwide-based taxation and foreign tax credit
Some Observations: US Influence

2. Originator of tax rules
   - Transfer pricing
   - Controlled foreign corporations (CFC)
   - Treaty-abuse (LOB)
   - Anti-abuse rules (e.g., GILTI and BEAT which are basis for Pillar 2)
Some Observations: US Influence

3. Unilateralism, but “Constructive”

- Out of US self interest
- US corporations’ clout and US tax rules (e.g., foreign tax credit rule)
- Principles- and rules-based; transparent
Some Observations: US Influence

4. Other countries’ transplantation
   - Out of their own self interest (e.g., Canada)
   - Countries with similar political/economic systems
   - Countries attracting investment by US corporations
Some Observations: US Influence Declining?

a) Institutionally?
   - yes, BEPS IF
   - EU
   - G20

b) Scientifically?
   - Ideas underlying Pillar 1 and Pillar 2

c) Realistically?
   – Fate of Pillar 1 and Pillar 2?
Some Observations: US and China’s Tax Interests Converge?

a) Digital economy
   - Dominance of digital firms
   - Large markets

b) Headquarter jurisdiction of large MNEs

c) Use of corporate tax incentives

d) Two-way investments
Some Observations:
US and China’s Approach to Global Tax Governance: Diverge

unilateralism

multilateralism
Wrap-up

• Preliminary observations
• Tax is “accessory” to economic, political and international relations
• Paper:
  https://digitalcommons.osgoode.yorku.ca/scholarly_works/2863/

Thank you!