Enforcing the Arm's Length Principle in the Knowledge-based Economy: *There are no Winners, but all are Losers*

A Aplicação do Princípio do Arm's Length *na Era da Economia de Conhecimento: não há Vencedores, mas Todos são Perdedores*

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"Genuine freedom comes from constructing human institutions that protect the rights of each and everyone of us."[1]

Abstract
This paper examines the influence of the neo-liberal economic setting on taxation, and contends the enforcement of the arm's length principle (ALP) as a measure to share taxing rights among jurisdictions in the era of the knowledge-based economy, grounded on a Polanyian critique of market liberalism. It outlines Polanyi's main criticisms of laissez-faire economics and reviews the contemporary challenges faced by tax administrations. There is an analysis of the responses given to those problems by a number of experts, but the article makes the case for a coordinated action to uphold Corporate Income Tax. For a conclusion, the article rejects the Base Erosion and Profit Shifting project's proposal to enforce the ALP as a measure to allocate the tax base derived from the exploitation of intangibles. Without ignoring the mainstream critique regarding its feasibility, this paper looks at its desirability, claiming that its outcome will deliver a final blow to the hope for stronger social cohesion.
Keywords: BEPS, Polanyi, international taxation, globalization, knowledge-based economy, arm's length principle, transfer pricing.

Resumo
O artigo analisa os efeitos da política neoliberal sobre o sistema tributário e critica o princípio do *arm's length* como uma medida adequada para repartir os direitos de tributação na era da economia de conhecimento. O

[1] Fred Block and Margaret Somers. *The power of market fundamentalism*: Karl Polanyi's critique. Harvard University Press, 2014.

primeiro capítulo explora as principais críticas feitas por Karl Polanyi à política de livre mercado e cita os atuais desafios enfrentados por Administrações Tributárias. A segunda parte revisa as soluções oferecidas por estudiosos do tema e conclui pela necessidade de uma ação coordenada para a manutenção da tributação sobre a renda das pessoas jurídicas. Em conclusão, rejeita-se proposta formulada pela Organização para Cooperação e Desenvolvimento Econômico (OCDE) para que se adotem medidas que garantam a aplicação do princípio do *arm's length* como principal parâmetro de repartição da base tributária derivada da exploração de bens intangíveis por multinacionais. Sem ignorar as críticas relacionadas à viabilidade de sua aplicação, este estudo foca nos efeitos sociais de sua adoção, questionando se eles são desejáveis ou se entregarão uma sociedade ainda mais desigual e desagregada.

Palavras-chave: BEPS, Polanyi, tributação internacional, globalização, economia de conhecimento, princípio do *arm's length*, preços de transferência.

1. Introduction

International tax law has its roots in the nineteenth century, a period remarkable for the consolidation of the liberal state, the creation of the international gold standard and the rise of self-developed markets. The laissez-faire theory professed that the removal of trade barriers would enhance economic growth and improve people's living standards. Hence, double tax treaties (DTT) were designed to prevent two different jurisdictions from imposing taxes on the same base, this being a barrier to international trade. These institutions produced the first great movement towards globalization and "an unheard-of material welfare"[2]. However, this trend was abruptly interrupted by two world wars and the 1929 market crash. In the aftermath, the world was divided, the liberal state crumbled, the gold standard abolished and markets were constrained.

During the Cold War, the west feared the advance of the Soviet States and sheer investments were made in social welfare. Keynesian economics prevailed and levels of state expenditure were high. The average tax rate for Corporate Income Tax (CIT) among members of the Organization for Economic Cooperation and Development (OECD) was above 50%. Cross border investments were restrained by fixed exchange rates and there was a widespread use of capital controls. Such measures provided a favourable environment for establishing domestic policies that substantially improved social welfare. On the downside, the adoption of fixed exchange rates significantly contributed to the pressure on the US dollar that triggered the 1973 crisis and, eventually, led to the abandonment of the Breton-Woods regime[3]. As a consequence, over the following decades, Amer-

[2] Karl Polanyi. *The great transformation*: the political and economic origins of our time. 2nd edition. Beacon Press, 2002.

[3] Fred Block. A Neo-Polanyian theory of economic crises. *74 American Journal of Economics and Sociology* 361, 2015.

ican and British markets suffered substantial losses. By the end of the 1970s, their economies were struggling with rising unemployment, spiraling inflation and sizeable public deficits[4].

Within this context of economic stagnation, the nineteenth-century liberal movement was born anew. The collapse of the URSS reinforced the neoliberal campaign, adopted by Thatcher and Reagan, to inhibit state intervention in order to promote economic growth. Friedman and Hayek were cherished[5]. At that time, it seemed that the belief in unfettered markets had triumphed. Gradually, exchange controls were lowered, making financial capital more mobile than ever. Most countries reduced tax rates on corporate income and capital gains. In the UK, corporate tax rate fell from 52% in 1982–83 to 20% in 2015-16. Moreover, capital gains tax rates were lowered below the level imposed on income, which opened loopholes and meant that income from labour was taxed more heavily than that derived from investments[6].

Coincidently or not, real improvements in technology shortened distances, making global communication almost instantaneous. An irresistible and irreversible movement towards globalization took place in the last decades of the twentieth century[7]. Its positives are many and self-evident, which makes it irrelevant to be explored in this work. The problem is that the history of the past few decades has proven that the positives are not all across the board and that the liberal theory is not as consistent as its proponents have sustained. The world saw a second financial crisis in 2008, which is yet to be healed. In 2009, global trade contracted by 10.7%, which means 50% more than the 1975's decline[8]. Economies are again stagnant. Over the last three decades, inequality has increased in most OECD countries and became a deep concern[9]. Political parties from the extreme left and right have grown stronger and the United Kingdom has recently voted to leave the European Union. This is not to say that globalization should – or could – be reversed, but it might indicate that these challenges need to be addressed, if lessons taught by history are not to be forgotten.

This paper examines the influence of the neo-liberal economic setting on taxation, and contends the enforcement of the arm's length principle (ALP) as a measure to share taxing rights among jurisdictions in the era of the knowledge-based economy, grounded on a Polanyian critique of market liberalism. Part II outlines Polanyi's main criticisms of laissez-faire economics and, then, reviews contemporary challenges regarding taxation. Part III explores the respons-

4 OECD. *Fundamental reform of corporate income tax* (OECD 2007) 20.;OECD. *OECD economic surveys*: United Kingdom 1976, v. 1976 (OECD 1976) 5.

5 Milton Friedman and Friedrich Hayek, distinguished philosophers and economists who eagerly promoted classical liberalism.

6 John Tiley. *Revenue Law*. 2nd ed. London, 1978.

7 Michael Hardt and Antonio Negri. *Empire*. Harvard University Press, 2000.

8 Block (n 3).

9 Bert Brys and others. Tax design for inclusive economic growth. *OECD Taxation Working Papers*. OECD, 2016, <http://www.oecd-ilibrary.org/content/workingpaper/5jlv74ggk0g7-en>. Accessed 21 July 2016.

es given by a number of experts to those challenges, but makes the case for coordinated action to uphold CIT. Part IV rejects the Base Erosion and Profit Shifting (BEPS) project's proposal to enforce the ALP as a measure to allocate the tax base derived from the exploitation of intangibles. Without ignoring the mainstream critique regarding its feasibility, this paper looks at its desirability, claiming that its outcome will deliver a final blow to the hope for stronger social cohesion.

2. Globalization, the Changing Nature of Economy and Challenges Posed on Taxation

2.1. Polanyi's critique of unfettered markets

In *The Great Transformation* (GT), Karl Polanyi provides a thoughtful and well-balanced critique of laissez-faire economics[10]. The core of his theory lies in the concept of embeddedness. According to him, the economic system is just one aspect of a broader social context and, historically, societies had submitted the economy to politics, religion and social rules: "never before our own time were markets more than accessories of economic life". He condemns the attempt to subvert this logic, placing society under "an economic system controlled, regulated and directed by a price mechanism"[11]. To be sure, he makes clear that such a project is a "stark utopia". To fully realize it, labour and nature would have to be treated as pure commodities, subject to the same self-adjusting mechanism of supply and demand, and that is untenable for two main reasons.

Firstly, it is simply immoral to treat human beings and natural resources as market-priced objects:

> "For the alleged commodity 'labour power' cannot be shoved about, used indiscriminately, or even left unused, without affecting also the human individual who happens to be the bearer of this peculiar commodity. In disposing of a man's labour power the system would, incidentally, dispose of the physical, psychological, and moral entity 'man' attached to that tag. Robbed of the protective covering of cultural institutions, human beings would perish from the effects of social exposure; they would die as the victims of acute social dislocation through vice, perversion, crime and starvation. Nature will be reduced to its elements, neighbourhoods and landscapes defiled, rivers polluted, military safety jeopardized, the power to produce food and raw materials destroyed."[12]

Secondly, markets do not thrive without state regulation to manage, apart from labour and nature, the supply of money - which he calls the third fictitious commodity. Polanyi strongly rejects the idea that market economy can be released from political power: "[n]o society is possible in which power and compulsion are absent, nor a world in which force has no function"[13]. In the end, the political option for allowing power to rest on markets is not a desirable one. In fact, when-

[10] Polanyi (n 2).
[11] Ibid 71.
[12] Ibid 76.
[13] Ibid 266.

ever policies are implemented to shift the state to a greater reliance on market self-regulation, the society becomes disorganized and ordinary people and natural resources are forced to bear the costs of the cyclical demands. The natural response is a counter-movement, which are actions taken to protect society from these pressures ("laissez-faire was planned, planning was not")[14]. Those actions can be progressive or regressive, politically organized or disruptive. Moreover, it is often the case that economic forces will urge the state to protect the system from them.

Polanyi illustrates his thinking by citing the role of the international gold standard in the run up to the WWI. The gold standard was an ingenious mechanism, which laid the necessary foundation to structure the then emerging global market. According to the standard, every country had to set the value of its currency according to a fixed portion of gold, committing itself to buy and sell gold accordingly. This allowed prices to fluctuate without exogenous interference. A deficit on exports would lead a given currency to be in greater supply, thus, stimulating its exchange for gold, which would naturally be shipped abroad. In this case, the domestic supply of money would be reduced through deflation up to the point of an external balance. In turn, the reduction on prices and wages would make exports more competitive. However, society could not bear the costs of the adjustments needed when an unexpected outflow of gold occurred. Thus, tariffs on imports were the recourse adopted to offset the impact of free global trade and to protect internal prices, which made the trade flows less sensitive to external prices. The second recourse was the late rush to establish formal colonies, which helped to buffer internal problems by sacrificing overseas resources and populations, but also intensified political, military and economic rivalries.

2.2. Challenges posed for taxation

Possibly one of the most important effects of the liberal policies adopted in the 1980s was the emergence of powerful multinational enterprises (MNEs), accompanied by a corresponding decline in the ascendancy of the modern European state model[15]. Technological advances and lower controls made the most valuable factors of production highly mobile and the possibility of explore them in a global scale led to a shift from the country-specific business model to the global-operating one. As a consequence, the last decades have seen an exponential growth in the number of intra-group transactions. A lack of effective regulation opened opportunities for those companies to manipulate domestic and international tax rules in order to reduce their overall tax burden. This was acknowledged by the Institute for Fiscal Studies in the Mirrlees Review:

[14] Ibid 147.

[15] A similar pattern was observed in the eve of the 20th century Reuven S Avi-Yonah, Corporations, society and the state: a defense of the corporate tax. *Michigan Law, Public Law Research Paper* No. 40; *Michigan Law and Economics Research Paper* No. 04-006, 2004.

> "Perhaps the most important developments affecting business taxation since the Meade Report in 1978 have been the growth of multinational businesses and cross-border ownership of companies.
> These developments have placed increasing strain on international elements of company tax systems. Multinational firms can relocate both real activities and taxable profits to countries that offer more favourable corporate tax regimes. This increase in the international mobility of the corporate tax base has resulted in a proliferation of complex anti-avoidance legislation, particularly in high-tax countries, and put downward pressure on corporate tax rates."[16]

In fact, Judge Learned Hand words have never sounded so relevant[17]. Despite the risk of reputational damage, firms increasingly engage in tax-planning or income sheltering by exploiting structural rules within an ineffective international tax system. For instance, MNEs take advantage of inconsistencies in the concept of tax residence, which allows some groups to scape tax altogether by not being tax domiciled anywhere. Likewise, the different tax treatment given to debt and equity in virtually all jurisdictions has created the least sophisticated, but nonetheless popular, structure, in which highly leveraged affiliates, based in high-tax countries, are indebted to other branch of the group, located in a low-tax jurisdiction. In short, the lack of appropriate regulation has not only made economic relations more autonomous from political control, but simultaneously reduced states' power as they are increasingly unable to levy taxes on MNEs and their wealthy shareholders.

Concerns that cross-border transactions challenge domestic tax systems and create opportunities for either double or non-double taxation are not new. The League of Nations addressed this issue back in the 1920s, establishing international tax principles that form the basis for the current DTT models. The OECD and the United Nations (UN) have long sought to tackle the problem among their members. In parallel, many countries have responded by enacting anti-avoidance measures. Such measures have been adopted in different degrees by states, in accordance with their own interests. It is unsurprising, then, that the increasingly diffuse regulation has multiplied opportunities for sophisticated business architectures to legally exploit differences between the deals offered by differing domestic tax systems.

However, the commodification of knowledge has brought an unparalleled concern for taxation. It radically limited taxation in at least two ways. Firstly, intangibles are usually believed to be unique, which makes their evaluation rather

16 Stuart Adam, Timothy Besley and Richard Blundell. *Tax by design*: the mirrlees review. OUP Oxford, 2011, p. 406–407.

17 "Anyone may arrange his affairs so that his taxes shall be as low as possible; [...] There is not even a patriotic duty to increase one's taxes. Over and over again the Courts have said that there is nothing sinister in so arranging affairs as to keep taxes as low as possible. Everyone does it, rich and poor alike and all do right, for nobody owes any public duty to pay more than the law demands." *In Gregory v Helvering, Commissioner of Internal Revenue* (US Court of Appeals).

troublesome for tax administrations. Secondly, as a highly mobile asset, the ownership of intangibles can easily be transferred to other affiliates located in different jurisdictions. This has not only contributed to tax arbitrage and tax competition, but also made it difficult to find in which link of a chain profits are generated. In short, they challenged the international standards encapsulated in the OECD Transfer-Pricing Guidelines.

The fact that intangibles are valuable and mobile incentivizes companies to artificially locate their ownership where it happens to be more convenient (or low taxed). Their uniqueness makes it easy to manipulate transfer-pricing rules designed to deal with double taxation. Briefly, the payments of royalties to firms in low-tax countries where knowledge-based assets are located makes it possible to substantially reduce profits in others operations. It is arguably difficult to evaluate the rightness of these payments and even if profits are being adequately shared among countries involved in the global chain. Such arrangements came to public awareness in 2012, when MNEs such as Starbucks and Google were publicly enquired about their tax arrangements[18].

In parallel, tax inversions, the phenomena through which companies transfer their assets or their domicile to low-tax countries, have tormented certain countries such as the US, but have been very profitable to others, such as Ireland. For instance, in 2015, the Irish reported an economic growth of 26.3%, which was officially due to the fact that companies had transferred their intellectual properties to enjoy a CIT rate of 12.5%:

> "The official explanation was that the surge in gross domestic product was caused by 'inversions', in which companies move their assets or their domicile to Ireland to avail of its super-low 12.5 per cent corporate tax rate; companies moving intellectual property to Ireland for the same reason; and corporate restructurings. In other words, it has only a tenuous relation to activity in the real economy and tangible things such as the creation of jobs."[19]

The practice created the so-called "race-to-the-bottom". Open-economies followed the liberal reasoning that prescribes a reduction in CIT rates to attract foreign investments. That benefited a number of economies, which were able to attract companies or their valuable assets, but created a negative externality on those countries which underwent an outflow of investments. As a consequence, countries with higher rates came under pressure to reduce their rates, even where there was no more room for broadening the tax base[20]. The case was evident in the UK, when the then Chancellor of the Exchequer suggested slashing CIT to

[18] Vanessa Houlder and Hannah Kuchler. Multinationals face pressure on tax. *Financial Times* (3 December 2012), <http://www.ft.com/cms/s/0/f4c82afa-3ae5-11e2-b3f0-00144feabdc0.html#axzz4FmwkrORz>. Accessed 29 July 2016.

[19] Vincent Boland. Irish tell a tale of 26.3% growth spurt. *Financial times* (12 July 2016), <http://www.ft.com/cms/s/0/8a1ebc9c-4846-11e6-8d68-72e9211e86ab.html#axzz4FJfN6kcg>. Accessed 24 July 2016.

[20] OECD. *Fundamental reform of corporate income tax* (n. 4) 153.

less than 15 percent in an attempt to attract and secure investments, given the UK's vote to leave the European Union[21].

However, the traditional view that lower taxation makes more capital available for investment is contented by Joseph Stiglitz who argues that slashing taxes paid by the top richest will only help to move money from the bottom to the top. In doing so, it will contribute to weaken the aggregate demand and the economy, for those at the top generally spend less than those at the bottom[22]. Despite this, it is expected that, in a globalized world, high tax rates on mobile assets income will continue to induce tax inversions, despite all countries' efforts to resist the trend. Therefore, low-tax countries will attract investments, taking advantage of the positive externality generated by high-tax countries. Rates are likely to be set below the optimal level, which will lead to expenditure cuts. Yet reduction in state expenditure will affect taxpayers as a whole, opportunities to reduce the tax burden are only available to those who can move their assets abroad[23].

The reduction in countries' capacity to spend on welfare is a likely ingredient for growth in inequality. Unsurprisingly, the need to cut tax rates brings the need to cut expenditure because the reverse of "what the government gives it must first take away" is also true[24]. The 2016 UK budget provides a clear example of this. Cuts on expenses for disabled citizens were announced along with a decrease in the corporate tax rate (which was a promise of the Conservative campaign). The announcement provoked howls of outrage and heated the Conservative party crisis, leading Iain Smith, the Work and Pensions Secretary, to resign under the warning that "his party was balancing the books on the backs of Britain's most vulnerable people"[25]. No one can be certain that this episode did not contributed to a distrust in the Prime Minister's Remain Campaign.

Reduction in the burden of taxation for companies and asset holders turns out to be even more dramatic when we consider that taxation is so far the best way worked out to achieve redistribution and to "address rising income inequality, wealth concentration, and the dangers to basic liberties that those economic patterns present"[26]. In *The Price of Inequality*, Stiglitz commented on the issue, explaining "the vicious circle by which more economic inequality gets translated

21 George Parker and Political Editor. George Osborne puts corporation tax cut at heart of Brexit recovery plan. *Financial times* (3 July 2016), <http://www.ft.com/cms/s/0/d5aedda0-412e-11e6-9b-66-0712b3873ae1.html#axzz4EIpieRWK>. Accessed 13 July 2016.

22 Joseph E. Stiglitz. *The great divide*: unequal societies and what we can do about them. WWNorton & Company, 2016.

23 Ian Roxan. Limits to globalisation: some implications for taxation, tax policy, and the developing world. *LSE Law, Society and Economy Working Paper Series*, 2012.

24 Simon James and Christopher Nobes. *Economics of Taxation 2015/16* (13th revised edition. Fiscal Publications, 2013) 7.

25 Cancel latest tax cuts for the wealthy to protect disability benefits, Jeremy Corbyn Says | UK Politics | News | the independent, <http://www.independent.co.uk/news/uk/politics/cancel-corporation-and-capital-gains-tax-cuts-to-protect-disability-benefits-jeremy-corbyn-says-a6943856.html>. Accessed 9 July 2016.

26 Linda Sugin. Theories of distributive justice and limitations on taxation: what Rawls demands from tax systems. *72 Fordham Law Review* 1.991, 2004.

into political inequality, especially in America's political system, which gives such unbridled power to money"[27]. In The Great Divide, he gives an account of the role played by liberal policies in the 2008 financial crisis and on the rising levels of inequality around the world, highlighting the part played by the tax cuts for upper-income people and corporations:

> "The tax cuts played a pivotal role in shaping the background conditions of the current crisis. Because they did very little to stimulate the economy, real stimulation was left to the Fed, which took up the task with unprecedented low-interest rates and liquidity [...]."[28]

This means that the liberal economic view that taxation should not concern itself with addressing inequality is flawed. In fact, as Polanyi has rightly asserted, the liberal promise of a world without politics is utopic. Economic forces generate political forces which are then influential on governmental decisions. If taxation does not address redistribution, it is unlikely that an imbalanced society will do so. To illustrate, the lack of capacity to tax mobile capital has forced a shift of this burden onto less mobile capital, such as labour and consumption. A study released by the OECD in 2015 revealed that individuals are bearing increases in indirect and social security taxes to replace the corporate share[29]. However, those earning labour income are usually less well off than owners of capital and intangibles. Thus, taxation is undermined on two fronts: –in tackling inequality and in raising revenue.

Globalization and lax control have put a strain on the international tax system. If there is any agreement left, it is that the regulation in force has not been able to deal with the current economic environment. Even laissez-faire apologists, who are not moved by reductions in countries' capacities to spend, recognize that opportunities for tax arbitrage are not evenly distributed and, thus, can create markets distortions. The challenges are quite significant and no longer restricted to the expert's committees. They had long reached the newspapers headlines, causing popular outrage.

3. Responses

3.1. Abolishing corporate income tax

The current difficulties in taxing MNEs have strengthened the argument of a number of tax experts in favour of the abolishing of CIT. Among the arguments, it is said that neither the legal personality nor the benefit principle can justify taxation on companies' profits. Indeed, they cannot solely account for taxation, but they might be among the rationales that justify levies on both artificial and real entities. The case for progressivity on personal income is denied by the

[27] Joseph Stiglitz. The price of inequality. *30 New Perspectives Quarterly* 52, 2013.
[28] Stiglitz (n 22).
[29] OECD. *Revenue Statistics 2015* (OECD 2015), <http://www.oecd-ilibrary.org/taxation/revenue-statistics-2015_rev_stats-2015-en-fr>. Accessed 14 July 2016; Joachim Englisch and Anzhela Yevgenyeva. The upgraded strategy against harmful tax practices under the BEPS action plan. *5 British Tax Review* 620, 2013.

fact that many shareholders are "institutional investors such as pension funds or charitable organizations"[30]. Moreover, it is advocated that CIT is distortionary and violates the principle of horizontal equity, since two individuals can make identical investments and receive different after-tax return. In turn, this can influence their decision to incorporate or not, leading to a "shifting of capital away from corporate equities"[31]. The case for the last argument is weakened by the fact that 80% of US economic activity is developed through corporations[32].

A stronger case is made by disputing where the effective incidence of CIT falls. In an open economy setting, it has commonly been assumed that much of the burden of CIT is shifted onto workers and consumers in the form of lower wages or higher prices. Thus, workers would be better off if their wages or consumption were taxed directly. This argument is mostly that taxing corporations does not reduce shareholders' profits, but shifts the burden to the amount employees will earn and consumers will pay. Although rather compelling, this reasoning is somewhat weakened by the fact that companies are spending high amounts on tax planning. Obviously, competitiveness can explain the rush to build creative tax structures. Once the first MNE invested in tax planning, the others followed suit in order to maintain competitive value for workers and consumers. However, the most likely explanation is that the burden of taxation falls somewhere in between. In any case, taxing companies remains politically appealing at an international level. As CIT is supposedly levied on a source basis, regardless of their ownership, taxing MNEs ultimately means taxing foreigners. Thus, abolishing this levy would lead to the abolition (even if only formally) of source taxation.

3.2. "No reasons for cartelistic cooperation"[33]

Apart from those who defend the abolition of CIT, there are a number of authors who believe that competition among nations is a healthy tool to maintain state power under control. In this context, tax competition is widely view as an uncooperative but interdependent process of setting tax rates between sovereign jurisdictions, in a bid to attract or secure investment[34]. Contending the view of the natural goodness of the democratic decision-making process, the public choice school of thought would see politicians acting in the same self-interested way as individuals. Therefore, they will always abuse their power to tax in order to promote clientelism and populism. In this reasoning, international tax competition is a desired effect of globalization, which protects "economically potent minorities" from being overburdened by politicians' appetite for power:

[30] Anthony Polito. A proposal for an integrated income tax. *Harvard Journal of Law & Public Policy* 1.016.
[31] Polito (n 30). p. 1.016.
[32] Avi-Yonah (n 15).
[33] In Yariv Brauner and Pasquale Pistone (eds.). *BRICS and the emergence of international tax coordination*. IBFD, 2011.
[34] Englisch and Yevgenyeva (n 29).

> "[P]oliticians' and, possibly, the bureaucrats' appetite for power and influence may lead to an overproduction of public goods and to an oversized public sector, beyond the level that could be justified by social welfare considerations. Similar results have been estimated as likely outcomes in democratic societies if median voter preferences determine the supply of public goods and the level and mix of taxes. Even to the extent that desirable public goods and transfer payments are financed by tax revenues, this has been assumed to often be done inefficiently due to waste and corruption. Finally, deadweight losses due to the behavioural effects of taxation are often ignored or underestimated in politics, especially since they are frequently not fully appreciated by ordinary voters either. Against this background, international tax competition has been regarded by some as a much-needed instrument to 'tame the Leviathan' by imposing budgetary restraints on excessive or wasteful spending."[35]

A worthier aspect to consider is that of the sovereignty of jurisdictions. There are countries with specific structural disadvantages that rely on low tax rates to offset their disadvantages. Taxes are only one among other several factors taken into account by investors when deciding where to invest. To take away one of these instruments from sovereign nations would certainly mean to reward other countries who have relied on low standards of regulation for labour or environment, just to say a few. Tsilly Dagan, challenging the views agreed under BEPS, argues that cooperation is not necessarily good and its consequences are not always desirable. For her, a "cartelistic cooperation" may be to the benefit of OECD countries, but not necessarily to developing or emergent economies:

> "Some of the prevailing arguments in international taxation sound indisputable. [...] The underlying theme of these prevailing arguments is the often-praised value of cooperation in the international tax game. Cooperation is used in support of the conventional wisdom on all three levels at which international tax evolves. On the unilateral level, countries are encouraged to follow "neutral" policies as a cooperative strategy towards global neutrality; on the bilateral level, countries are encouraged to cooperate in order to eliminate double taxation; on the multilateral level they are encouraged to cooperate in order to harmonize their taxes in an effort to save the welfare state.
>
> But cooperation is not necessarily desirable. It is far from clear that multilateral cooperation can evolve and that, if it can evolve, it can be sustained. It is also not clear that multilateral cooperation would be normatively desirable even if it could evolve. Nevertheless, cooperative strategies sound indisputable. Thus they serve as useful rhetorical tools that support a certain contingent policy choice, but obscure other, potentially important, considerations and alternatives.

[35] Ibid.

> Most importantly, supporters of cooperation in international tax downplay the heterogeneity of the international community. In international tax, every policy chosen potentially affects different people, groups, and nations in different ways. Identifying the winners and losers of cooperative policies is thus necessary in order to evaluate such polices. Cooperation cannot be and is not the ultimate goal in international tax policy."[36]

Current economic theory is thus divided as to what extent cooperation and competition should be enhanced. The support offered to the positives of competition is offset by evidence in literature that international competition might cause restriction on a state's capacity to pursue adequate social welfare policies through its tax system. Even for developing or emerging economies, coordination and cooperation might be necessary if sustained growth is to be pursued. Offering tax holidays might be a successful short-sighted policy. However, regarding long term prospects, firms will require developed human capital and adequate infra-structure. Moreover, speculative investments can quickly ebb away, leaving labour unprotected, if the state has low capacity to spend on social welfare. No doubt sovereignty should be respected, which means that there should be little hope to impose other's decisions for good. If measures decided at an international level turn out to be overwhelmingly unfavorable to a share of stakeholders, that will likely respond by behaving uncooperatively in the near future.

3.3. The case for upholding CIT

Despite the significant number of academics that have argued for the repeal of CIT, those views are far from undisputed. All arguments stem from a sense that there are no alternatives beyond the enforcement of the self-regulated markets. In general, the arguments for the abolishment of CIT fail to notice the importance of a state's control over private interests. On the other side, the arguments for the maintenance of the *status quo* somewhat neglect the benefits of the welfare state.

a) Administrative rationales

As underlined in the Mirrlees Review, CIT eases the work of tax administrations as it is much easier to collect taxes from a few number of companies than from millions of shareholders[37]. Firstly, if corporations were not taxed, it would be more troublesome to tax profits which are reinvested without being distributed among shareholders. Secondly, taxing corporations preserves personal income tax either in the form of labour or of return on investments. If corporate profits were not levied, it would be easier to shelter personal income under the corporate veil. Workers could incorporate to offer their labour force, preserving the income generated by their service undistributed within the company. Thirdly, companies are saving boxes. If companies were not taxed, there would be an incentive to

[36] Brauner and Pistone (n 33).
[37] Adam, Besley and Blundell (n 16).

maintain income derived from this investment (capital gains and dividends) undistributed until needed. In this way, income tax would be effectively a consumption tax.

However, all of these administrative reasons are somewhat weakened by the fact that there are high administrative costs in keeping CIT, and particularly in the case of MNEs. In fact, there are a couple of instruments designed to avoid taxation of companies, while enforcing the levy on shareholders.

In the first place, there are methods which target companies and exempt shareholders. For instance, the integration method can cope with the need to ease the work of tax administrations, by imposing taxes at the corporate level and exempting dividends. Taxes are imposed on corporate profits and dividends are tax-free. Another solution is the Australian model which was already been adopted, but then repealed, in the UK. According to this "imputation system", taxpayers held credits for the taxes paid on dividends against their personal income. The negative side of this option is that it creates a discrimination against foreigners which deters outward investments and is incompatible with the European Union rules.

Alternatively, there have been some suggestions to tax shareholders directly, exempting the corporate level. For closed companies, the US offers the examples of S corporations or of the Limited Liability Companies, where shareholders are directly levied on the corporate income as it is earned[38]. For publicly traded companies, the option would be the market to market taxation, where taxpayers are levied on the basis of the appreciation of their shares. This is actually the Haig-Simons option, which meets with a considerable political resistance, given the volatility of markets.

All in all, administrative reasons do appear to explain the reluctance to abandon CIT, better than that there are no alternatives. The issue is that abolishing CIT would require considerable reform to the whole tax system. That would mean firms incurring significant administrative and compliance costs and, most importantly, there would be high political costs. It is likely that tax reform will make a share of taxpayers well off, while making others worse-off. Moreover, for well-established tax systems, such as those found in developed economies and common-law jurisdictions, there is the feeling that a major reform would mean shooting oneself in the foot.

b) Economic rationales

CIT revenues are not responsible for a major share of the total revenue in countries surveyed by the OECD, for instance. For 2011, the OECD reported numbers varying from 1.2% to 11% of the total of tax revenues, in countries such as Germany and Norway, respectively. Even not covering a major proportion, when considering the total of revenue raised, the absolute numbers are quite significant.

[38] Avi-Yonah (n 15).

Other economics aspects can play a more important role in the case for the maintenance of taxes on corporate profits. As mentioned above, the UK Mirrlees review found a pattern between the cuts on CIT accompanied by increases in social security and value-added taxes. Both play a regressive role. Social security taxes are generally levied on wage earners who tend to be less well-off than asset holders. As for consumption levies, a 2014 report released by the OECD shows that, for the 20 countries covered, VAT systems were regressive when measured as a percentage of income, although they were proportional or slightly progressive when measured as a proportion of expenditure[39].

The case for taxation as a means of redistribution is generally approached in two ways. For the first, neoclassical economics advocates that taxation should not bother itself with redistribution but with avoiding distortionary effects on markets. Redistribution should be achieved by expenditure, this being the field of politics. For instance, this is supported by John Rawls. Although acknowledging the need to look at the particularities of a given jurisdiction, he argued in favour of a proportional expenditure tax, grounding his theory in the logic that one should be levied on how much one takes from the common store of goods rather than from how much one contributes[40]. For him, the "transfer branch" would be responsible for guaranteeing the social minimum[41].

A second approach urges that taxation should target redistribution as its own goal. The following moral rationales justify this alternative. Firstly, market outcomes are highly dependent on the amount of assets one owns. Secondly, the logic of supply-and-demand tends to downplay valuable contributions made by some professions while over-valuing others. In any case, an economic reason justifies this approach. As Stiglitz has pointed out, high levels of inequality can weaken aggregate demand, impairing economic growth. On the top of that, the case for the rawlsian approach is ruled out by the Sokoloff and Zolt's findings. In a research focused on the development of the American continent, they found evidence that "inequality across societies contributed to the different political decisions made regarding tax and expenditure policies"[42]. For instance, Brazil, a highly unequal country, sets its marginal personal income tax rate at 27,5% while raising a total revenue of 35% of GDP, which suggests political options for regressive taxes[43].

c) Political rationales

As advocated by Avi-Yonah, taxation remains as an important regulatory tool and a important element in managing the balance between corporations,

[39] OECD and KIPF. *The distributional effects of consumption taxes in OECD countries* (Organisation for Economic Co-operation and Development 2014), <http://www.oecd-ilibrary.org/content/book/9789264224520-en>. Accessed 25 July 2016.

[40] This is not to forget that Rawls defended the tax on gift and inheritances as a way to tackle inequality.

[41] John Rawls. *A theory of justice.* Original ed. Belknap Press, 2005, p. 272 ss.

[42] Kenneth Sokoloff and Eric Zolt. Inequality and taxation: evidence from the Americas on how inequality may influence tax institutions. *59 Tax Law Review* 167, 206, 2006.

[43] Revenue statistics in Latin America (OECD) 2310-9211, <http://www.oecd-ilibrary.org/content/serial/2310922x>. Accessed 29 July 2016.

society and the state. People recognized back in the early twentieth century that taxation was needed to cut any excessive power in the hands of corporate management[44]. The rise of powerful corporations threatens the current model of state-sovereignty, because MNEs operate across jurisdiction and are able to play with the different rules of different jurisdictions, escaping regulation altogether. Taxation represents the most important way to curb this power by "limiting the rate of corporate wealth accumulation" and by functioning as a tool to create incentives and disincentives to certain economic activities[45].

Moreover, as Oakeshott reminds us, modern European states are remarkable for being endowed with sovereign authority and great actual power (what he names *potentia*)[46]. This power has been acquired by the ability to control people and things in a very distinct way from that seen in earlier times, but some MNEs are increasingly escaping this submission. Illustrative of this trend are the contention between the FBI and Apple over encryption technologies or Brazilian courts imposing a ban on WhatsApp three times. Moreover, also in Brazil, a Facebook executive was arrested over allegations of contempt of court, leading its CEO, Mark Zuckerberg, to launch an online campaign, which gained significant support, to pass a bill which could prevent the blockage of internet services, saying that the ban "is very scary in a democracy"[47]. Thus, the fact that these MNEs are able to thrive under no country authority is meaningful.

Finally, the BEPS Project has its roots in political accountability. During the current global recession, naming, blaming and shaming MNEs found widespread political appeal. Addressing the public outrage is crucial to the integrity of the system. It is widely accepted that attitudes towards taxation depend very much on the views that the taxpayers have of their system. Studies have found that when taxation is no longer considered fair, it ceases to be perceived a form of mutual obligation and becomes a burden, which tends to undermine its legitimacy, increasing evasion and administrative costs. In his research, Livingston highlights how remarkable it is that successful jurisdictions usually rely heavily on the voluntary compliance of their taxpayers[48].

Overall, this chapter has reviewed the current literature against CIT, but has made the case for the maintenance of this levy, particularly for economic and political reasons. Furthermore, it advocates that international cooperation can build an environment where democratic decisions can flourish; whereas the mar-

44 Avi-Yonah (n 15). 38.

45 Ibid 41.

46 Michael Oakeshott. Lectures on the history of political thought, 2006, Chapter 23.

47 Financial times. Apple and FBI in plea for encryption legislation (Wwwftcom, 232016), <http://www.ft.com/intl/cms/s/0/994168ce-df3b-11e5-b072-006d8d362ba3.html?siteedition=uk#axzz48o4Ve8va>. Accessed 16 May 2016; Facebook executive arrested in Brazil over WhatsApp data clash (Wwwftcom, 132016), <http://www.ft.com/cms/s/0/3f057e7e-dfd4-11e5-b7fd-0dfe89910bd6.html#axzz48o4Ve8va>. Accessed 16 May 2016.

48 Michael A. Livingston. Law, culture, and anthropology: on the hopes and limits of comparative tax. *18 Canadian Journal of Law & Jurisprudence* 119, 2005, p. 119-134.

ket mentality will submit countries to a dispute for investments, leaving room for resentments and disputes.

4. Multilateralism and International Cooperation

4.1. The BEPS alternative

For a combination of the abovementioned reasons, the OECD and the G20 countries have recognized the need to address MNE's base erosion and profit shifting. In 2013, the they decided to launch the BEPS Project, which aims to design new international standards that can guarantee the maintenance of corporate income taxation, ensuring that profits are taxed where activity occurs[49]. The initiative acknowledges that "multilateralism is of even greater importance in the current climate, and remains our best asset to resolve the global economy's difficulties"[50]. In a nutshell, the Project aims to bring back control over the flow of assets, either by not recognizing artificial arrangements or by enhancing coherence and transparency through coordination and cooperation among jurisdictions.

The actions of BEPS are threefold. Firstly, the project is concerned with establishing international coherence regarding tax rules, which will curtail opportunities for tax arbitrage. Secondly, it aims to restore the effects of the international agreed standards, through substantive measures. These encompass (a) updates to the OECD transfer pricing guidelines, under the slogan "aligning profits with value creation", (b) modification to the rules regarding the setting up of a permanent establishment, (c) the elimination of opportunities for treaty shopping and (d) action against harmful tax practices. Thirdly, the OECD is working on transparency as a means to enhance cooperation among jurisdictions, in the battle against double non taxation[51].

The OECD has opted for the reinforcement of the current normative standards, but through a set of renovated rules, which supposedly have the potential to deal with an era "characterized by an increasing importance of intellectual property as a value-driver [...]"[52]. Putting aside concerns regarding its feasibility, this approach endangers real cooperation and social cohesion. Although it was conceded that changes to the normative standards were demanded by a number of countries, the option was ruled out, under the argument that "[w]hile actions to address BEPS will restore both source and residence taxation [...], these actions are not directly aimed at changing the existing international standards[53].

49 OECD. *Addressing base erosion and profit shifting*. OECD, 2013.

50 OECD. *Action plan on base erosion and profit shifting*. OECD, 2013, 11.

51 It has to be noted, as it was commented by Brauner, that actions on transparency does not mean publicizing information to the public, media or academia but "[i]n general, transparency in the OECD context means provision of better information, more cost-effectively, to governments in order to assist them to enforce their tax rules and combat double-non taxation (of the BEPS variety in this case)." Yariv Brauner. Transfer pricing in BEPS: first round – business interests win (but, not in knock-out). *43 Intertax* 72, 2015.

52 Ibid. p. 5.

53 OECD. *Action plan on base erosion and profit shifting* (n 50) 11.

The work undertaken by the OECD is certainly an attempt to constrain unfettered markets. Through the actions proposed, the OECD makes an effort to devise a set of rules that can restrain MNEs' opportunities to profit without paying their share of taxes in accordance with the agreed international tax principles. As highlighted in the Action Plan, the current situation harms governments, individuals and small businesses[54]. Governments are struggling to balance less revenue, higher costs of compliance and pressure from constituents; individuals have had their social security contributions increased; and, finally, local businesses have been harmed by unfair competition, as they do not have the same opportunities available to MNEs. The concern is opposed to the one that led, back in the nineteenth century, countries to develop the current international tax standards.

DTTs succeeded in avoiding double taxation, but lack of cooperation proved positively harmful. Now countries are struggling with the threats of double non-taxation, as well as low-taxation associated with artificial practices. Thus, can BEPS be what Polanyi described as a countermovement? The project is a fair recognition that the lack of effective regulation caused social harm. Popular outrage against the share paid, or unpaid, by high-profitable corporations shows how intolerable free-market outcomes can be. Polanyi's 1944 work remains important. Neo-liberal theorists insist on looking only at the bright side of global unfettered markets, but revenue losses caused by tax competition and lack of regulation are just the tip of the iceberg.

When one analyses the context in which the BEPS project was developed, it is possible to identify connections with the concept presented in GT. In his masterpiece, Polanyi criticizes the liberal the attempt to segregate market economy from political control. For him, this will inevitably harm the "fictitious commodities" (labour, nature, money), disrupting social cohesion and leading society towards a precipice. However, in response to this pressure, society will likely restrain markets: although many would wrongly view Polanyi as accusing market-liberals of having segregated the economic from the social sphere, the truth is that he actually maintains the impossibility of such a project. Polanyi says that society will always resist any attempt to do such a thing. According to his reasoning, the embeddedness of economy in society is unavoidable. Thus, whenever markets grow unbearably strong, there is a resistance and an attempt to keep markets again under control, to re-embed market-economy in the social context, either by disruptive movements or by organized political action.

Therefore, the OECD and the G20 acknowledge that globalization has created an environment in which MNEs are able to explore economic activity without being regulated by any jurisdiction. This has undermined the benefits taxation bring to society. The lack of cooperation (and the enhancement of competition) have opened opportunities for tax arbitrage and the erosion of the tax base.

[54] Ibid 8.

In response to this, the BEPS project encompasses the idea that in a globalized economy governments need more cooperation and less competition. The present situation hurts individuals, governments and the market itself (creating competitive disadvantages to domestic companies). The BEPS countermovement seeks the enforcement of multilateral rules that could effectively control and tax the flow of assets, guaranteeing countries power over MNEs.

4.2. Enforcing the ALP for intangibles

Alas, as Polanyi pointed out, not all counter-movements are progressive.

To begin with, OECD ruled out any attempt to negotiate changes in its bilateral tax treaty model, although conceding that this was demanded by a number of countries. However, the rules agreed in the wake of the twentieth century, regarding particularly the taxation of capital turned out to be highly disadvantageous to capital importers[55]. It is remarkable the outrage expressed by the Belgian Expert who said that the agreement would "reduce debtor nations to economic servitude"[56]. To illustrate, Article 5 of the OECD model sets withholding tax rates at zero on royalties and at 10 and 15 percent on, respectively, interest and dividends. The rate on dividends is reduced to 5%, if the beneficiary is a corporation holding 10% of the company shares. Now, if it did not reduced countries to economic servitude, this imbalance is a likely explanation for the lack of cooperation demonstrated by capital importers while institutionalizing practices such as treaty shopping[57].

The second – and more important – problem resides in the BEPS action designed to update the Transfer-Pricing Guidelines regarding intangibles[58]. The BEPS project opted for the enforcement of the ALP. Under the ALP, a transaction which takes place within a group is analysed as if it were conducted between unrelated parties. Tax administrations estimate a price to reflect that which would have been negotiated in the market in a comparable transaction, were independent entities to have been involved. In short, transfer-pricing rules are a system of tax norms which deals with the allocation of the tax base between jurisdictions involved in cross-border transactions, although this fact is somewhat missed by the current discussions at OECD. They determine the conditions, including the price, of the transactions within related parties. In doing so, they allocate the tax base in different countries.

Much criticism has been directed against the ALP. Many argue that the lack of comparables, which is a problem innate to the uniqueness of these assets, makes

[55] Reuven S. Avi-Yonah. Double tax treaties: an introduction. *Social Science Research Network* 2007, *SSRN Scholarly Paper* ID 1048441, <http://papers.ssrn.com/abstract=1048441>. Accessed 15 July 2016.

[56] Michael J. Graetz and Michael M. O'Hear. The "original intent" of U. S. international taxation. *46 Duke Law Journal* 1.021, 1.087, 1997.

[57] *India v Azadi Bachao Andolan* [2003] 6 ITL Rep 233 (Supreme Court (India)).

[58] OECD. *Aligning transfer pricing outcomes with value creation, actions 8-10-2015 Final Reports*. OECD, 2015.

the ALP unworkable[59]. Although acknowledging these arguments, this paper is concerned with, first, the argument deployed to uphold this measure and, second, the results it is likely to produce. First, use of the ALP assumes the enduring myth of a market's neutrality and freedom from political interference to be true. Second, as if the final stages of the commodification of knowledge had not been a big enough hit to poor countries, the use of the ALP to share taxing rights involving intangibles will definitely legitimize, under the flag of neutrality, the submission of human beings and nature to an immoral market logic of supply and demand. Countries importing knowledge will receive low shares for offering cheap workforces and natural resources.

a) The Myth of ALP neutrality

ALP is vaunted for its supposed neutrality. Considering that jurisdictions will allocate income as if the parties transacting were not part of the same group, it is argued that there are not unfair measures favouring any jurisdiction. Following this reasoning, transfer-pricing rules are successful in curbing price manipulation which could lead to spillovers or to the erosion of the higher tax jurisdiction base. It is also claimed that both uncontrolled and controlled transactions would be treated on equal terms for tax purposes, enhancing fairness between national-based companies. In sum, its justification encapsulates the myth of market neutrality that frees decisions from politics.

However, this account does not explain how poor countries are suddenly to compete with developed economies in the production of knowledge-assets. It is not necessary to go too far to recognize that countries' investments are a product of available opportunities. The current situation will be influential on what they are to produce, and it should not be forgotten that most of these countries are the same ones that lost the dispute over the sharing on the taxation of capital. What they are able to produce to the market is indeed a function of their current assets, including their human capital.

Moreover, there is no neutrality in the trend towards the commodification of knowledge. The knowledge-based economy is not a product of "human nature to barter and exchange", as the liberal creed often restates. As May and Sell make sure, "the history of intellectual property was not (and is still not) a neutral, functionally driven set of improvements towards an 'optimal' legal settlement that is naturally just"[60]. Commodification of knowledge was a political option: an option that has changed the economy and left winners and losers. It is a fine example of "reregulation", a practice that takes place by dismantling the regulation that protects labour, the environment or consumers, while claiming state intervention to protect business interests, usually under the argument of self-righteousness. Yet,

59 Yariv Brauner. Value in the eye of the beholder: the valuation of intangibles for transfer pricing puporses. *28 Virginia Tax Review* 79, 2008.

60 Christopher May and Susan K. Sell. *Intellectual property rights*: a critical history. Lynne Rienners, 2006, 204.

as Ha-Joon has spotted, "Switzerland became one of the world's technological leaders in the nineteenth century without a patent law"[61].

Finally, it is really ingenuous to argue that countries are free to adopt measures that can protect their labour force or their natural resources from market pressures, thus, influencing on the share of taxes due to them. In the current environment, jurisdictions are always under the pressure to become more competitive. Therefore, as much as levying reasonable levels of CIT, enhancing measures such as decent minimum wages, levies on employers or environmental protection has been a recipe to rank very low for competitiveness by the World Economic Forum.

b) A gloomy outcome

In the current business model, particularly represented by the global value chains, MNEs are usually reliant upon one or more intangibles. However, the intangible itself is dependent on other factors of production to realize its value. To be sure, the car-booking app Uber is still nothing without its drivers. Even Google or Facebook cannot realize their value without a massive net of users. In the large majority of cases, it is not possible to segregate the value of the knowledge from what it actually produces. However, the OECD's decision to give special weight to research, development and controlling functions institutionalizes the enlargement of MNEs' head offices and patent boxes, whilst reducing the tax base of those jurisdictions employing several unskilled workers.

Commodification of labour is at the centre of Polanyi's critique of market liberalism. Although claiming that markets are essential to organize the economy, he highlights the perils to social cohesion that submitting humans to a market logic can signify. More than being immoral, it is naïve to believe that workers can passively bear the costs of low demand and thrive after substantial losses. It is expected that, eventually, a lack of governmental response to those problems will lead to disruptive movements. For Polanyi, it is the lack of social cohesion that produces brutalities. Rejecting social naturalism, he denies the self-interest liberal view and sees only one innate human characteristic: relational sociality. Through this reasoning, he defends social interdependence as the foundation of humanity and, thus, demands recognition that wealth is ultimately collectively produced. By ignoring this caveat, the OECD decision to enforce the ALP regarding transactions involving intangibles tends to exponentially increases the abysm between rich and poor nations.

If globalization has not already been a big enough hit to low skilled labour, sharing taxing rights according to the same logic tends just to perpetuate under-education, for it will reduce the revenue available to invest in human capital or infra-structure. At times of high unemployment rates and zero-hour contracts, labour will be cheap and disposable. As Polanyi asserted, while markets are necessary for organizing economic activity, they also represent a threat to society,

[61] Ha-Joon Chang. *Kicking away the ladder? Economic development in historical perspective*. Anthem, 2002, 10.

because market logic does not value human beings as citizens, but as commodities[62]. "At arm's length", it is very likely that the most profitable affiliates of a group will be the small knowledge-boxes developing and protecting intangibles. On the other side, countries offering cheap workforce and natural resources will receive less revenue and suffer greater impacts from the activity developed.

Even if one believes in the ALP's feasibility and neutrality, there still remains concerns regarding its outcomes. If it is "simply wrong to treat nature and humans beings as objects whose price will be determined by the markets", sharing taxing rights, according to the same logic, will help to perpetuate the *status quo*[63]. Having low revenues, how can those countries educate their workforce? How can governments buffer the effects of low demand when a workforce is made redundant or alleviate the environmental impact of factories? Even considering that CIT derived from MNEs are not the unique source of revenue, it is hard to deny that the enforcing the ALP in the knowledge-based economy is prejudicial for developing economies, which is particular worrying as CIT is far more important in these countries[64]. In short, in the knowledge-based economy, adopting the ALP is highly regressive: it will raise revenue from the less well-off to distribute it in countries hosting the knowledge-boxes.

Moreover, privileging the ALP in the case of intangibles, when no one can really segregate their value from the commodities and services they allow, is even more unprincipled. While superior technology is usually based in developed economies, they inevitably need developing economies' resources and markets to monetize their value. Sharing the global value chain's outcome according to the ALP will mean giving too much taxing rights to few jurisdictions, while not providing even the costs to many others, where the assembly-line factory will be located. Ultimately, this may result in very few highly skilled researchers being valued considerably more than very many low skilled blue-collar workers, working in poor conditions. This at time when many view the gap between blue-collar and executive earnings with dismay. Perhaps, we are going back to a time where human beings are seen as means only to realize the ambition and greed of those at the top.

The alternative – a formula-based approach which could measure MNEs' profits worldwide – would be a more adequate policy and one that, at least, would implicitly recognize that "wealth is ultimately collectively produced". That would not necessarily mean giving the same weight to every factor of production, but should certainly include a safety minimum for every jurisdiction involved. Surely, finding such a measure would be a product of politics, inasmuch as the option for a market outcome is. The knowledge-based economy has been enhanced by law, which is ultimately a consequence of political power. To summarize, as Sustein

62 Block and Somers (n 1) 219.

63 Polanyi (n 2) xxv.

64 IMF. Revenue mobilization in developing countries, 2011, <https://www.imf.org/external/np/pp/eng/2011/030811.pdf>.

states: "markets are mere instruments to be evaluated by their effects", and they can "produce inefficiency and (worse) a great deal of injustice"[65].

5. Conclusion

Soaring levels of inequality, high unemployment rates and growing political parties from both the extreme right and left are here to prove that the outcomes of trade liberalization have not been as positive as predicted in the late 1980s. The theory that cuts to CIT and capital gains are a recipe for an economic boom is yet to be verified. The facts are that lower controls over the flow of assets and the lack of coordination between countries were the perfect ingredients for MNEs to hide their profits in loopholes or to shift them to appealing tax jurisdictions. Eventually, governments, individuals and markets are damaged. To address these issues, the lessons from Polanyi remain important. Self-regulated markets are a "stark utopia". To begin with, it is not a matter of deregulation but of reregulation. Claims for "wage flexibility" come along with others, such as for the "strong enforcement of intellectual property rights".

However compelling the case for the abolition of CIT may be, there are more reasons to believe that its maintenance through international cooperation is the best alternative. The rise of powerful corporations threatens the authority of countries and disregard the importance of them in controlling inordinate private interests. As for economic reasoning, the patterns of reduction of CIT and increases on social security and consumption levies have contributed to the trend towards more inequality. If taxation does not address redistribution, it is unlikely that an imbalanced society will do so. The BEPS project acknowledges the need to uphold CIT and represents an attempt of the biggest economies to devise a legal mechanism able to reinforce their rights tax corporations and curb their power. In short, it can be seen as a typical countermovement to constrain markets and enforce regulation.

Alas, the OECD BEPS deliverables does not create a sustainable set of rules. The existing international standards on the allocation of taxing rights over financial capital are to be retained. In parallel, in the era of the knowledge-based economy, the enforcement of a market mechanism to share the rights to tax profits derived from intangibles tends to speed up a process that is taking society to the Polanyian "precipice". As before in history, the myth of market neutrality is used to deny a political option, one that increases inequality around the world. As if globalization were not harsh enough on unskilled labour, sharing taxing rights according to their market value in comparison to intangibles' will only perpetuate their *status quo*, denying the vulnerable access to social protection. On a global scale, applying the ALP for intangibles is highly regressive, undermining any redistributive effect of taxation.

As Stiglitz rightly put it, the richness of Polanyi's work does not lie in his attack against free-markets utopianism, for this myth is virtually dead. Rather, the

[65] Apud Eric MacGilvray. *The invention of market freedom*. Cambridge University Press, 2011, 196.

value is found in his emphasis on the relationship between the economy and society and how economic systems, or reforms, can affect how individuals relate to one another. High levels of inequality and pervasive poverty has had disastrous effect on social cohesion and contributed to high and rising levels of violence around the world[66]. Even though it has recognized the need for regulation, the BEPS Project is still falling behind in its understanding of these relationships. However, there is no way to enhance long-term cooperation without acknowledging that the current society is globally interconnected and that its wealth is collectively produced[67].

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66 Foreword Polanyi (n 2) x.

67 Polanyi (n 2).

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