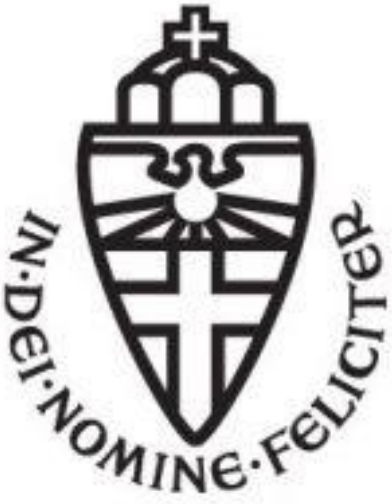
Tax Avoidance by Multinational Enterprises and the Current International Tax System: an Ethical Perspective



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You can't tax business. Business doesn't pay taxes. It collects taxes.

-Ronald Reagan, [1975] (Inside Ronald Reagan, 1975)

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1. Introduction

Although the words from former United States President Reagan were applicable in the 1970s, the relevance of these words was never so high as it is nowadays. As in 2018, Amazon made an $11.2 billion profit but didn't pay income tax for the second year in a row, instead, Amazon received a federal tax refund of $129 million due to tax credits and deductions (The Guardian, 2019b). However, Amazon is not the only big multinational enterprise (MNE) that engages in 'aggressive' tax avoidance. In the last decade, the 'big six'[1] US tech companies avoided $100 billion in tax obligations (The Guardian, 2019a). It is therefore not surprising that corporate taxation attracted considerable attention from media, a wide range of stakeholders and is at the centre of (academic) debate for the last couple of years (Scarpa & Signori, 2020). The ramifications of 'aggressive' tax avoidance are disruptive for the general welfare and bad for businesses, governments, and citizens, especially for those in poor countries and developing and emerging economies (Weinzierl, 2018; OECD, 2021). Considering the above, one would expect tax avoidance to be illegal, however, these 'aggressive' tax avoidance strategies are perfectly legal by law (Hansen et al, 1992). Due to globalization MNEs can exploit informational gaps in a global environment that are not exploitable for ordinary citizens and small and medium enterprises (SME). Therefore, another criterion, then just technical compliance to the letter of the law, is needed to assess the fairness of tax avoidance by MNEs. A normative assessment is needed to scrutinize this behaviour of MNEs and assess their compliance to the spirit of the law (Hansen et al, 1992).

Although tax avoidance is a legal practice, stakeholders involved face ethical and moral concerns that go beyond technically complying with the letter of the law. For instance, MNEs' managers tend to hire tax practitioners to minimize the company's taxes. These managers are often blamed for incentivizing tax avoidance, but simultaneously, they are obliged to act to the best of their capabilities to maximize the company's profit and satisfy shareholders (Weinzierl, 2018). Tax practitioners, therefore, have the moral obligation to fulfil the desires of the company by minimizing the taxes, even if it involves making use of loopholes. Therefore, assessing the compliance to the spirit of the law is more relevant than ever as nowadays the world is an interconnected marketplace with differing tax policies and informational gaps across countries that MNEs can exploit (Weinzierl, 2018).

[1] The big six tech companies in the United States are Amazon, Apple, Facebook, Google, Microsoft, and Netflix.

1. Introduction

This interconnected world is at an advanced stage of economic globalization and is the result of rapid developments of technology in both transportation and communication, combined and enhanced by, the lowering and in some cases, even the removal, of trade barriers in between the 1970s and 1980s (Palan et al., 2013; Van Dijck, 2016). Due to these events, the mobility of goods, services, and especially capital were greatly enhanced, as first they were restricted by national borders or difficulties inherent to operating in a global environment (Furceri & Loungani, 2015). All the above, shifted the organization and dynamics of the world economy, that at that time operated as separate national economic units, to an interconnected world that operates as a singular system with deeply integrated international markets (Van Dijck, 2016; Gilpin & Gilpin, 2001; Sayer, 2000). This interconnected world in combination with a global presence of MNEs provides them opportunities to avoid taxes which grants them a competitive advantage over SMEs that are not able to enjoy the benefits of tax avoidance (OECD, 2021).

Attention for tax avoidance is needed as not only the fairness of competition between SMEs and MNEs get undermined. Governments' tax bases erode due to tax avoidance and especially those from less developed countries miss funds to spend on education, infrastructure, pensions, and healthcare (OECD, 2021). Estimates are that tax avoidance accounts for 80 percent of all illicit financial outflows from less developed countries, which is larger than incoming foreign direct investment (FDI), and accounts for a government deficit of 100-240$ billion dollars annually (Weinzierl, 2018). This is extremely grievous as MNEs do extensively use the public goods and services in those countries. Also, citizens are disadvantaged as they often have to foot the bill by paying higher taxes for services that otherwise would have been funded by corporate income tax revenue, which decreases their disposable income and subsequently could lead to impoverishment (OECD, 2021).

1.1. Tax Evasion vs. Tax Avoidance & the Current International Tax System

Before discussing tax avoidance and its ramifications, it's of great importance to make a clear distinction, for the scope of this thesis, between tax evasion and tax avoidance. Tax evasion is by the letter of the law an illegal activity that often entails concealment, deception, and criminal activities (Hansen et al., 1992). Because of its illegal nature, most scholars consider tax evasion to be "profoundly unethical" (Bagus et al., 2011, p. 376). Therefore, there is relatively little literature reporting on the ethics of corporate tax evasion (Scarpa & Signori, 2020). Corporate tax avoidance on the other hand is considered as a tax minimization strategy, that arranges one's financial affairs to minimize tax liability, and is supported by both the letter of the law and court

(Blaufus et al., 2016). The key difference, therefore, is the illegal nature of tax evasion versus the legal nature of tax avoidance. However, ethical issues and conflict arise when companies and tax practitioners engage in tax minimization strategies that exploit and take advantage of the detailed, subjective nature of taxation laws and ignore the intended spirit of the law (Hansen et al., 1992). Especially, since not every actor in society has the same opportunities to engage in such tax minimization strategies.

MNEs, which are the focus of this thesis, do have more opportunities to avoid taxes due to economic globalization and national fiscal sovereignty, as they can exploit loopholes created by the current international tax system (Atkinson, 2015). These loopholes and the high mobility of capital provide MNEs opportunities to shift their profits across borders with ease and do it in a way that minimizes their tax burden. MNEs themselves defend their tax avoidance practices by arguing that they do comply with the letter of the fiscal law (Atkinson, 2015). Although tax avoidance is legal it doesn't necessarily mean that it is moral as "legal and ethical are not always equivalents" (Payne & Raiborn, 2018, p. 475). This makes tax avoidance by MNEs an issue of social justice. Therefore, there is much literature reporting on the ethical and moral aspects of corporate tax avoidance (Scarpa & Signori, 2020). Due to the consensus that tax evasion is unjust and immoral, this thesis will focus on the ethical and moral aspects of tax avoidance and will regard tax evasion as beyond the scope of interest (Bagus et al., 2011, p. 376).

Furthermore, this thesis will also normatively assess the current international tax system that facilitates tax avoidance. The reasoning underlying this approach is; if tax avoidance is a legal activity, this doesn't necessarily mean that it's just or fair and therefore the institutional framework that facilitates this behaviour should also be assessed. Especially as managers of MNEs have the moral obligation to their shareholders to maximize their profits (Hansen et al., 1992; Colle & Bennet, 2014). In practice, this means that minimizing the tax burden is a sound business plan that complies with the moral duty managers have to their shareholders. Therefore, it's also important to normatively assess the 'rules of the game' besides the 'behaviour of its players'. I thus argue that injustice that follows from tax avoidance by MNEs is to be attributed to the current international tax system. This also implies that if ramifications of tax avoidance are considered to be unjust or unfair, the current international tax system should be reshaped into a comparatively more just one (Atkinson, 2015).

1.2. The Scope & Structure

The scope of this thesis is to normatively assess the current international tax system and provide an alternative that is comparatively more just. It does this by assessing the ramifications of tax avoidance by MNEs that can be attributed to the current international tax system. This leads to the following research question:

"*How could the current international tax system be reshaped to be comparatively more just than it is now?"*

To answer this research question, chapter two provides a descriptive elaboration of the current international tax system and the possibilities it creates for MNEs to avoid taxes. Next, it will provide an overview of the ramifications of tax avoidance. This descriptive chapter is important as it defines the confines of the ramifications of tax avoidance that will be normatively assessed during the remainder of this thesis.

The conclusion from chapter two forms the foundation for the normative assessment in chapter three. This normative assessment includes the application of Rawls' ideal and nonideal theory on the current international tax system and its ramifications. This ideal and nonideal theory deals with compliance to the principles of justice and is suited to assess the justness and fairness of the ramifications of tax avoidance and the current international tax system on domestic justice[2] (Rawls, 1999). This normative chapter concludes that the current international tax system is unjust as the ramifications as established in the conclusion of chapter two, violate all the principles of justice.

Since in chapter three, the current international tax system is assessed as unjust, a case study will be performed in chapter four to assess if a newly proposed G7 tax system could be comparatively more just. The results of the normative assessment of this case study are that this newly proposed tax system has its caveats but proves that there is a tendency for global collaboration in targeting tax avoidance.

In chapter five the research question gets answered by providing an alternative international taxation system. This alternative taxation system is unitary taxation[3] with

[2] The conception of domestic justice as supported by Rawls entails; justice that could be accepted by proponents of all of the reasonable "comprehensive conceptions of the good" that are likely to flourish between the borders of a liberal society (Simmons, 2010, p.8). Further elaboration on what (domestic) justice entails can be found in chapter three.

[3] Unitary taxation means that MNEs are now treated as single corporations instead of separate entities. This restricts MNEs to report (most of) their profits in tax havens and forces them to pay taxes in countries in which they have an economic presence. Further elaboration on unitary taxation can be found in chapter five.

formulary appointment and requires the establishment of a global tax authority. This alternative system gets assessed regarding the same requirements as used for the case study and the current international tax system. The normative assessment concludes that unitary taxation with formulary appointment is comparatively the most just international tax system of the three explored alternatives. Since institutions are social constructions that are created by humans, this also means they can be changed if needed. Therefore, it seems obvious that if we can change the current international tax system into a more just one then, ceteris paribus, we should do so (Pogge, 1992; Van Dijck, 2016).

This thesis contributes to the current academic literature due to its 'setup', the subject of analysis, and the further exploration of mentioned recommendations from previous studies (Scarpa & Signori, 2020; Rixen, 2008; Pogge & Mehta, 2016; Zucman, 2015; Van Dijck, 2016). Furthermore, it provides additional ethical substantiation for claims made in the current literature to opt for an alternative international tax system (Pogge & Mehta, 2016; Cappelen, 2001; Zucman, 2015; Gillian, 2008).

2. The Current International Tax System and its Ramifications

This chapter will first elaborate on the current international tax system and the possibilities it creates for MNEs to avoid taxes. The second part will elaborate on the ramifications of these tax avoidance practices by MNEs for the general welfare and other socio-economic conditions.

2.1.1. Globalization

Among scholars, there is some debate on when globalization started. Some argue that it started in the 1400s with Ganghis Khan's invasions and travel along the silk road (World Economic Forum, 2019). Others argue it to be a far more contemporary phenomenon that began after the second world war (Mazlish, 2011). Although it is controversial on when globalization exactly started, it is clear that from the 1980s onwards, the world we live in is at an advanced stage of economic globalization (Van Dijck, 2016). This advanced stage of economic globalization is the result of rapid developments of technology in both transportation and communication, combined and enhanced by, the lowering and in some cases, even the removal, of trade barriers in between the 1970s and 1980s (Palan et al., 2013; Van Dijck, 2016). Due to these events, the mobility of goods, services, and especially capital were greatly enhanced, as first they were restricted by national borders or difficulties inherent to operating in a global environment (Furceri & Loungani, 2015). All the above, shifted the organization and dynamics of the world economy, that at that time operated as separate national economic units, to an interconnected world that operates as a singular system with deeply integrated international markets (Van Dijck, 2016; Gilpin & Gilpin, 2001; Sayer, 2000).

These rapid developments led in certain areas to the establishment of global political institutions, such as the World Trade Organization (WTO) in 1995 (WTO, 2021). These global political institutions are founded to either regulate certain parts of the interconnected world economy or act as an independent actor that can settle disputes in cases of disagreement between two or more involved parties. However, in the area of corporate income taxation, no such global political institution has been established while the effects of globalization in this area are no less profound (Van Dijck, 2016). This is extremely problematic as capital can cross national borders with ease due to its enhanced mobility, while the power to tax is bounded by these national borders (Rixen, 2008).

2.1.2. The Current International Tax System[4]

As mentioned in the previous chapter, a global political tax institution is absent, this is most likely the result of the general conviction that the power to tax is the central attribute of sovereignty for nation-states (Rixen, 2008, p.5; Van Dijck, 2016). In this globalized world, every sovereign state has the right to levy taxes on, for instance, labour, income, property rights, or capital. The rates of these taxes are also determined by nation-states themselves, as this is income for their public budget, which they use for funding public goods and services such as education, national defence, and healthcare (Rixen & Dietsch, 2015). Additionally, it is for sovereign democratic states also important to be able to change their tax rates, as tax rates are an important topic in times of elections. When political parties in democratic states are elected, they should have the capacity to set the tax rates for the national fiscal policies they support, as they are the representatives that have been chosen by the general public (Rixen & Dietsch, 2015; Rixen, 2016). This fiscal sovereignty is also important in times of economic crises, as sovereign states can lower tax rates to give their economy a boost. However, the fiscal sovereignty of nation-states also creates opportunities for them to lower their taxes to for instance attract Foreign Direct Investment (FDI) by MNEs. This tax rate lowering to attract the attention of MNEs is a phenomenon that is called 'tax competition' and is widely applied and often referred to as the 'race to the bottom' (Rixen, 2015). However, this sovereign right of nation-states to tax income and capital that is reported within its borders is a right established in a time before the mobility of capital was greatly enhanced by globalization (Van Dijck, 2016, p.5; Feld et al., 2013). Therefore, the current international tax system is outdated due to the collision of national fiscal sovereignty and a highly developed interconnected world economy (Van Dijck, 2016).

As mentioned above, the current international tax system is struggling with the interplay between national fiscal sovereignty and economic globalization. Due to the globalization of the economy, numerous areas such as trade also experienced globalization of politics. However, this wasn't the case for taxation and therefore tax sovereignty is still not transferred from a national to an international level (Van Dijck, 2016). This is problematic as current corporate tax legislations are mostly invented at the time of the first World War (Piketty, 2014). At that time, the world wasn't in a stage of advanced economic globalization and therefore tax

[4] When the term 'current international tax system' is used, this doesn't mean that there exists an international tax system governed by an organisation, such as the WTO exists for trade, it solely refers to the way the current international tax environment is shaped.

legislation focussed on closed economies. As a result, problems, such as double taxation began to occur when companies were operating in multiple countries. To tackle this problem, the League of Nations established three principles for international taxation in the 1920s (Van Dijck, 2016). These three principles still play a significant role in contemporary international taxation, which can be considered highly questionable due to the economic globalization of recent years (Rixen & Dietsch, 2015). For the next section of the thesis, an introduction of two of the just mentioned principles is important, to understand how MNEs exploit these principles to avoid taxes. These principles entail:

1) *Source principle:* taxes on business profits are levied in the country where the profits are generated, where the source of the profits is located (OECD, 2014; Van Dijck, 2016).

2) *Arm's length principle:* each entity (in different countries) must compute their profits separately. And, moreover, they must do so as if they were unrelated, which means that each entity must calculate its profits as if it were buying or selling at market price (OECD, 2009a; IMF, 2014; Van Dijck, 2016).

Since for MNEs it can be hard to determine what the source of revenue is, the arm's length principle must be seen as an addition to the source principle (IMF, 2014; Van Dijck, 2016). This comes in handy when an MNE for instance distributes products that are produced by a subsidiary in another country, as sometimes it is not clear or even very difficult to determine where profits are generated. In this case, the arm's length principle implies that both establishments should be regarded as separate entities, meaning that they have to calculate their profits independently. When the independent profits are determined they get taxed in the country in which they are 'generated'[5] (Van Dijck, 2016).

For decades the principles were not a topic of debate as the world economy was not yet in its advanced globalized stage. However, since the rapid developments in the 1970s and 1980s, the principles of the League of Nations began to show some weaknesses as capital became highly mobile (Furceri & Loungani, 2015). Around the same time in the 1980s when capital control decreased, a significant increase in tax havens (an area or country where taxes are levied at a low rate) was observed (Piketty, 2014). At this time, MNEs began to shift goods, services, and especially money to their subsidiaries in other countries. These shifts all occur in the company itself and are therefore often referred to as 'intrafirm trade', and constitute nowadays more than half of all international trade (McGrew, 2014). By shifting the capital from

[5] In practice, this implies that MNEs don't generate their profits in low tax jurisdictions but do report their profits in low tax jurisdictions.

one subsidiary to another, MNEs can benefit from tax regimes in the countries where those subsidiaries are located. Before I will elaborate on what various ways MNEs avoid taxes, it is important to introduce one last concept that facilitates the intrafirm shifting of capital, namely: substance requirements (OECD, 2013; Van Dijck, 2016).

It seems pretty obvious that when an MNE wants to make use of a beneficial tax regime (a tax haven for instance), the MNE must have a subsidiary located in the country of the beneficial tax regime, this is called having a *presence*. By being present in that country the MNE is subject to its tax regime. However, the requirements for starting a business or subsidiary are almost non-existent in all countries (Van Dijck, 2016, p.13). In practice, this means that that there are virtually no requirements for *economic substance*, so being legally present in a country is enough to make use of its tax regime (OECD, 2013). The results of this lack of substance requirements are the establishment of 'shell companies'. These shell companies are in reality not operational, but often are small rooms with a mail address, a table, chair, and plastic plant with the sole purpose of providing a legal *presence* in that country so the MNE can make use of its tax regime (Van Dijck, 2016). The Cayman Islands is a good example of a tax haven that registers a lot of shell companies. The Cayman Islands have more than 100.000 registered companies, which is nearly double of its population. There is also one address called 'Ugland House' that is home to almost 20.000 companies. All these companies are solely present to make use of the beneficial tax system of the Cayman Islands (The Guardian, 2016).

Concluding, the current international tax system is one where nation-states are financially sovereign and thus determine their tax regimes, and MNEs can shift their capital to all countries in which they have subsidiaries. Finally, the principles as established by the League of Nations do still apply and state that each subsidiary should report its profits at an arm's length price. These reported profits are taxed in the country in which they are reported (IMF, 2014; Van Dijck, 2016). In the next section, examples will illustrate how MNEs violate both the source and the arm's length principle to avoid taxes.

2.2. How do MNEs Avoid Taxes?

Since MNEs use numerous and highly sophisticated ways to avoid taxes, providing a complete and in-depth overview of the different tax avoidance strategies would be beyond the scope of this thesis (Hansen, 1992; Rixen & Dietsch, 2015). However, some basic concepts that MNEs exploit to avoid taxes will be highlighted, as these basic concepts underly almost every, and even, the most sophisticated ways MNEs avoid taxes. An understanding of these basic concepts

will provide sufficient knowledge to get a grasp of the nature of these tax avoidance strategies and the problems involved.

The underlying idea of all these tax avoidance strategies is the concept of profit shifting. This concept entails that MNEs reallocate their profits between the subsidiaries in countries that have a beneficial tax regime. This is done to have a high profit in a low tax jurisdiction and a low profit in a high tax jurisdiction (Scarpa & Signori, 2020).

2.2.1. Transfer Pricing

Nowadays more than half of all international trade consists of trade between subsidiaries of MNEs, also referred to as 'intrafirm trade' (McGrew, 2014). This intrafirm trade creates possibilities for MNEs to shift profits from high-tax jurisdictions to low-tax jurisdictions as they can set the prices of the goods and services that are sold between subsidiaries (Van Dijck, 2016; Contractor, 2016). Transfer pricing, or often referred to as "transfer mispricing", is generally seen as the most important and costly strategy MNEs use to avoid taxes (Zucman, 2014).

To start a basic (simplified) example of transfer pricing will be given. Assume there exists a multinational car company that is called LowTaxCars (LTC) and is founded in the United States. LTC owns two subsidiaries, Firm A in Mexico and Firm B in Canada. Let's assume that the corporate tax rate in Mexico is 10% and in Canada 25%. The two firms export car components to each other, for example, Firm A exports 10.000 components that cost $1.50 each to Firm B. Suppose LTC determines that it wants to pay less corporate income taxes, therefore they decide that they want to have more profit in Mexico as opposed to Canada due to the lower corporate tax rate. Therefore, they increase the price of each car component to $2.00 each. Firm A's profit would increase by $5000[6] and Firm B's profit would decrease by $5000. However, as both Firm A and Firm B are owned by LTC the total amount of pre-tax profit made by this transaction stays the same, only the after-tax profit differs as there is more profit to be taxed in Mexico after the price increase. **Error! Reference source not found.** provides an overview of the total profit of LTC in both scenarios.

[6] 10.000 x $0.5 = $5000

Table 1. LTC' Profits before and after Transfer Pricing

	Original Transfer Price (Component $1.50 each)		Changed Transfer Price (Component $2.00 each)	
	Firm A Tax Rate 10%	**Firm B Tax Rate 25%**	**Firm A Tax Rate 10%**	**Firm B Tax Rate 25%**
Pre-tax Profit	$15.000	$30.000	$20.000	$25.000
Tax	$1.500	$7.500	$2.000	$6.250
After-tax Profit	$13.500	$22.500	$18.000	$18.750
Total Profit LTC	$13.500 + $22.500 = **$36.000**		$18.000 + $18.750 = **$36.750**	

As can be seen in **Error! Reference source not found.** the transfer pricing method yields an extra $750[7] after-tax profit. Another ramification of this transfer pricing is that Canada's tax income from LTC decreases by $1.250. However, the extra profit created by LTC is only an example based on imaginary values that are much smaller than the profits MNEs have in reality. Especially if one considers that total world trade has a value of around $23 trillion and more than half of it consists of intrafirm trade (Contractor, 2016). This phenomenon becomes even more severe when MNEs have subsidiaries in tax havens like the Cayman Islands that have no corporate income tax (The Guardian, 2016). It is therefore needless to say that huge sums of tax income are avoided due to transfer pricing. However, one might wonder how this is possible when they have to respect the arm's length principle as discussed earlier. Due to the arm's length principle, MNEs can't vary the prices that much as they must reflect the market price. However, small variations in prices can still save a lot of tax costs when applied at high volumes. Additionally, a lot of intrafirm trade exists of intermediaries that often have unique and highly specific characteristics, making it hard or even impossible to find a comparative arm's length price, and therefore, the MNEs themselves can declare its shipment values (Contractor, 2016). This artificial pricing of intermediaries violates the spirit of the arm's length principle.

2.2.2. Royalty and Intellectual Property Rights Payments

The last tax avoidance strategy I wish to discuss also relies on the violation of the arm's length principle. Whereas the market price of intermediaries is already hard to determine, it becomes nearly impossible to determine a market price for intangible services, such as royalties,

[7] $36.750 - $36.000 = $750

intellectual properties, and patents (Van Dijck, 2016; Zucman, 2014; Contractor, 2016). For example: what would be the value (market price) of the name 'Nike' on clothing, or the name 'Microsoft' on computer software. MNEs do exploit the lack of a market price of intangible services to the fullest as most of their value resides in their technologies and intangible assets (Contractor, 2016). This becomes especially apparent as MNEs are allowed to transfer their intangible assets to subsidiaries in tax havens or shell companies that in turn will charge royalty payments for the use of those intangible assets. This is also facilitated due to most governments allowing deductions from tax liabilities for royalty payments, even if the subsidiary that holds the intellectual property rights is owned by the same MNE and none of the Research and Development (R&D) has been performed in the country of that subsidiary (Contractor, 2016; Colle & Bennett, 2014).

A basic and simplified example of royalty payments to avoid taxes will be provided with the use of the imaginary LTC MNE as mentioned before. Suppose LTC' headquarters is located in the US and their R&D department is also located in the US. Again, Firm A that is a subsidiary of LTC is located in Mexico. Now there will be two scenarios. In the first scenario, Firm A doesn't pay LTC royalty for the use of its American technology. In the second scenario, ceteris paribus except that LTC' headquarters signed an agreement with Firm A that it will pay a 10% royalty to LTC for the use of its American technology. Table 2 provides an overview of the total profit of LTC in both scenarios.

Table 2 LTC' profits before and after Royalty agreement

Scenario 1: Firm A pays no Royalty to LTC's Headquarters in the US		Scenario 2: Firm A pays a 10% Royalty to LTC's Headquarters in the US	
Firm A sales in Mexico	$10.000	Firm A sales in Mexico	$10.000
		Royalty (10% on sales)	$1.000
Total costs (no Royalty involved)	$7.000	Total costs (Royalty excluded)	$7.000
Profit before tax	$3.000	Profit before tax	$2.000
Mexico tax (at 10%)	$300	Mexico tax (at 10%)	$200
Profit after Mexican taxation	**$2.700**	Profit after Mexican taxation	$1.800
		Royalty remittance to LTC	$1.000
		Total remittance to LTC	**$2.800**

As can be seen in Table 2 the royalty payment yields an extra $100[8] after tax-profit. However, this method would only make any sense if in this example the effective tax rate would be lower in the US than in Mexico, therefore, this example only functions for illustrative purposes and would be unlikely in reality.

The most used tax avoidance strategy by the 'big six' in the US is an advanced version of the royalty payment agreement as illustrated above. This version is called the 'double Irish with a Dutch sandwich' (Colle & Bennett, 2014; Contractor, 2016). Again, the imaginary LTC MNE is chosen as an example to illustrate how this strategy works. For this strategy, LTC has a subsidiary in the Cayman Islands that offers 'specialized financial services' that supposedly assist LTC's headquarters with its financials. As these services are specialized and intangible, it is hard to determine a market price, especially as those services are only provided to LTC. The next step for LTC should be the establishment of two separate subsidiaries in Ireland called 'Ireland 1', and 'Ireland 2', which is controlled from the Cayman Island subsidiary, furthermore it needs the establishment of one subsidiary in the Netherlands called 'LTCDutch' (Contractor, 2016).

The subsidiary 'Ireland 1' holds the intellectual property rights of LTC. Taxes in Ireland are 10-12.5%, but 'Ireland 1' pays 'LTCDutch' a royalty for which it gets a tax deduction from the Irish government (Contractor, 2016). As it is hard to determine the market price of this royalty[9], LTC is free to choose the price of this royalty. Then 'LTCDutch' doesn't have to pay any taxes on this royalty as the Dutch government decided not to levy any taxes on income from property rights and royalties to incentivize R&D (Van Dijck, 2016). This absence of taxation on royalties and property rights makes the Netherlands one of the most prominent tax havens worldwide, and is the reason why so many MNEs have shell companies in the Netherlands[10] **(**NewScientist, 2020). Next, 'LTCDutch' pays the money to 'Ireland 2', which doesn't pay any taxes because it's controlled from abroad by the Cayman Islands subsidiary[11] (Contractor, 2016). Now the money is parked in the Cayman Islands, which have no corporate income taxes, and thus taxes are avoided. This is a clear violation of the source principle as established by the League of Nations.

[8] $2.800 - $2.700 = $100
[9] Think of the 'Nike' and 'Microsoft' examples mentioned earlier.
[10] However, the Dutch government signed a deal that from 2021 on it levies taxes on royalties to get rid of the negative publicity associated with tax avoidance (PWC, 2021).
[11] Irish legislation allows companies that are located in Ireland but controlled from outside, to pay taxes in the country of its 'controller/owner' (Contractor, 2016).

As can be seen, by the examples mentioned above, MNEs do much effort to avoid taxes. Over the years, they have developed very sophisticated ways to reduce their profits to zero, and some[12] even reported losses that granted them tax refunds (The Economist, 2015; The Guardian, 2019a). All these practices are possible due to the current international tax system that lacks a global political tax institution. The national fiscal sovereignty, the high mobility of capital, the global presence of MNEs[13], and the fact that subsidiaries of MNEs are treated as separate entities, push the principles as established by the League of Nations past its expiration date (Van Dijck, 2016).

2.3. Ramifications of Tax Avoidance

The ramifications of tax avoidance are negative for the general welfare and bad for business, governments, citizens, and especially for those in poor countries, developing, and emerging economies (Weinzierl, 2018; OECD, 2021). Therefore, the most profound ramifications will be highlighted, as providing an overview of all ramifications would be beyond the scope of this thesis.

2.3.1. Inequality

Governments provide social services by using revenue from their tax bases. The tax bases consist of the total amount of investment flows, income, and assets that are taxable on both the level of individuals and corporations (OECD, 2013; IMF, 2014). These are the most important sources that governments can tax that generates revenue for them. Of these sources, corporate profits are an essential part and play a key role in generating revenue in both developing and developed nations, as it is a primary way to tax capital (Van Dijck, 2016; Rixen, 2008; Zucman, 2014). Therefore, governments' tax bases get eroded when MNEs avoid taxes. The magnitude of this problem becomes more apparent when considering that in the US, a third of its tax revenue came from capital taxes, of which 60% came from corporate income taxes (Van Dijck, 2016; Zucman, 2014; Piketty, 2014). This percentage is already huge, but considering that only the 'big six' tech companies in the U.S. avoided more than $100 billion in taxes in the last decade, it is needless to say that this percentage would even be much higher if MNEs would pay their fair share of tax (The Guardian, 2019b).

[12] Amazon and Starbucks are some examples of MNEs that even receive tax refunds while being highly profitable (The Economist, 2015; The Guardian, 2019a).
[13] Even if they are only present in the form of a shell company, thus being legally present without any economic activity.

For governments, it's really hard to compensate for this loss in revenue, especially since their tax base is eroding at constant tax rates (OECD, 2013). In theory, governments could increase their tax rates to compensate for the missed revenue due to tax avoidance. However, in reality, this turns out to be even worse as an increase in tax rates incentivizes MNEs, even more, to shift their profits to lower tax jurisdictions. Therefore, corporate tax rates have been declining over the last decades (OECD, 2013; IMF, 2014; Piketty, 2014). With this constant lowering of the corporate income tax, governments try to keep the capital in their borders and sometimes even use this to attract FDI (Van Dijck, 2016). This results in tax competition that is a race to the bottom and can better be described as a prisoner's dilemma, (Rixen & Dietsch, 2015). In this prisoner's dilemma, there is no coordination between countries, and countries want to maximize their tax revenue. What now happens is the complete opposite of what these countries want to accomplish as they will all lower their tax rates to be as attractive as possible until they reach a tax rate that makes them worse off than if they would have cooperated.

As mentioned above, there is a clear decline in corporate tax rates in both developing and developed countries (OECD, 2013; IMF, 2014). However, these are still not near-zero (except for some tax havens). This decline has also ramifications for taxation at the individual level as otherwise wealthy individuals just could incorporate themselves to pay fewer taxes. Therefore, individual income taxes also declined (Piketty, 2014). Several studies state that the lowering of both corporate and personal income taxes are great contributors to the rising inequality since the 1980s (OECD, 2013; Piketty, 2014; Atkinson, 2015; Rixen, 2015; IMF, 2014; Van Dijck, 2016). This can be explained as most companies are owned by the wealthy, for example, the top 0.1% in the US owns around 50% of the corporate stocks, and the top 1% owns more than 90% of the total corporate stocks (Kinnickel, 2009; Van Dijck, 2016). This inequality is even worse in most developing countries (WorldFinance, 2015).

As mentioned earlier, governments need tax revenue for their tax bases. With substantially less revenue from levied taxes, governments will not be able to fulfil their role as public providers (Rixen, 2014). To compensate for this missed revenue, governments can either increase their debt or increase other taxes. Since there exists a strong preferential among governments to minimize its sovereign debt, they more than often chose to increase taxes on those that are less mobile, such as labour, SMEs, and consumption (Rixen, 2014; Piketty, 2014; Atkinson, 2015). This is backed by international data that shows governments' revenue being stable while corporate taxes declined. (IMF, 2014; Van Dijck, 2016; OECD, 2013). As one would already expect, this went hand-in-hand with an increase in taxes on labour and consumption (Piketty, 2014; Atkinson, 2015). This means that the tax burden is shifting from

MNEs to citizens and those companies that can't avoid taxes[14]. It is needless to say that labour is not able to avoid taxes in a way capital can, and SMEs are not able to avoid taxes in a way MNEs can. This results in a regressive tax system that increases inequality. Especially as taxation is an important redistribution tool that governments have to decrease inequality if applied progressively (Piketty, 2014; Van Dijck, 2016). This is a problem in both developed and developing countries. However, poor countries and developing and emerging economies are relatively even worse off compared to developed countries (Weinzierl, 2018; OECD, 2021; WorldFinance, 2015). I will elaborate on this in the next section.

2.3.2. Government Deficits and Free Riding

As mentioned earlier governments use tax revenue to provide public goods and services. Examples of these public goods are health care, education, infrastructure, a legal system, and national defence (Van Dijck, 2016). Some of these public goods are greatly dependent on the government as there would be no market in the private sector. Take for instance the domain of infrastructure, everyone benefits from the presence of streetlights, but if these streetlights had to be provided by a private firm that needs to make a profit, it would be doubtful if this firm would survive in a free market (Auerbach et al., 2013). This is just a simple example that illustrates the need for a government that can provide public goods and services that were otherwise barely available or non-existent in a free market. In developed countries, the effectiveness of these public goods is in general far-reaching, as can be seen by high-quality infrastructure, a relatively highly educated population, and a well-functioning health care system (Van Dijck, 2016). However, far-reaching public goods require higher degrees of taxation, meaning that everyone that has a taxable presence needs to pay more. The underlying idea is that everyone should pay their fair share of tax as everyone makes use of these public goods. Although it seems logical, this is exactly what tax avoidance by MNEs undermines.

Due to the undermining of paying taxes, governments face deficits that have to be compensated for in other ways. However, if governments can't compensate for this loss in revenue, they are often not capable of providing these public goods (Rixen, 2015). These damaging effects are felt in nearly every country, however, the ramifications of tax avoidance in developing countries are the most severe (WorldFinance, 2015). Alison Holder, a tax and inequality policy manager at Oxfam, stated: "Tax avoidance also has very direct and life or

[14] However, since 2019, the average tax burden on labour slightly decreased in 29 of the 37 OECD countries with an average of 0.39 percentage points annually. This can partly be attributed to policy changes in response to the COVID-19 pandemic, such as the lowering of income taxes in some countries (Taxfoundation, 2021).

death impacts in poorer countries: developing countries are most in need of predictable sources of tax revenue to invest in essential healthcare, education, and infrastructure" (WorldFinance, 2015, p.1). This statement is supported by several studies that show the disproportionately large effect tax avoidance has on developing economies (WorldFinance, 2015; Atkinson, 2015; Rixen & Dietsch, 2015; Payne & Raiborn, 2018). The Global Financial Integrity organization even estimates that developing countries face a yearly lost revenue of close to $100 billion (Global Financial Integrity, 2014). There are two main reasons why developing countries are disproportionally affected. Firstly, corporate income tax revenue accounts for a bigger share of the total tax revenue in developing countries compared to developed countries[15] (WorldFinance, 2015; The Washington Post, 2016). Secondly, governments in developing countries more often lack the capability to tackle tax avoidance head-on due to poorly developed legislative and administrative resources, and their dependence on FDI from these MNEs (Global Financial Integrity, 2014). This increases the inequality between rich and poor in these countries even further.

Everyone that uses public goods should pay their fair share for them. However, the current situation is one where some can use the public goods for a far lower price than would be fair, and some even use them for free (Rixen & Dietsch, 2015; Atkinson, 2015). So, besides the potential tax base deficits tax avoidance creates, it also allows those that participate in tax avoidance to free ride on those public goods. It also happens to be that these MNEs are the most intensive consumers of public goods (Zucman, 2014; Van Dijck, 2016). MNEs do intensively use the infrastructure for their operations, employ well-trained and healthy employees and rely on a functioning law system to protect their property rights (Atkinson, 2015). Nonetheless, they heavily rely on and intensively use these public goods, they don't pay for them or at least not the amount that would be fair. This is not only unethical but also threatens the compliance of other taxpayers who trust that everyone will pay their fair[16] share (Gribnau & Jallai, 2017).

[15] It doesn't necessarily need to mean that developing countries on average have a higher 'tax revenue as % of GDP', it could even be that developed countries on average have a higher 'tax revenue as % of GDP'. However, in developing countries, the corporate income tax rate usually accounts for a bigger share of the total tax revenue compared to developed countries. This can be explained, as in developing countries often a majority of the citizens work in the "informal economy" and don't pay taxes. Furthermore, collecting taxes is often too expensive for governments in developing countries, especially from those living in rural areas (The Washington Post, 2016).
[16] A profound assessment and conceptualization of fairness and justice will be provided in the next chapter.

3. Tax Avoidance and the Current International Tax System: a Normative Assessment

This chapter will first elaborate on why there is a need for an ethical assessment considering that tax avoidance is a legal activity. Accordingly, a brief overview of the current ethical debate will be provided that includes both arguments defending and attacking tax avoidance. At last, the ethical framework of ideal and non-ideal theory will be explored and applied.

3.1. Why Ethics?

As mentioned in the introduction, tax avoidance is a legal practice. Therefore, these practices also have the blessings of the court as stated by the Judge Learned Hand in the case *Commissioner v. Newman*, 159 F.2d 848 (CA-2, 1947; Hansen et al., 1992):

> *Over and over again the courts have said that there is nothing sinister in so arranging one's affairs as to keep taxes as low as possible. Everybody does so rich or poor; and all do right, for nobody owes any public duty to pay more than the law demands: taxes are enforced extractions not voluntary contributions. To demand more in the name of morals is mere cant.*

However, being legal is not automatically considered to be a moral activity. This distinction is important as the general perception over the years has changed that MNEs which fail to pay their fair share[17] of tax[18] are increasingly considered to be immoral, unfair, and outrageous (West, 2018 p. 1143; Scarpa & Signori, 2020). Besides the negative ramifications tax avoidance has on society as explained in chapter two, MNEs themselves also face negative ramifications of this changed perception as their legitimacy gets damaged which has far-reaching consequences for their (direct) profits, sales, (non)-legal agreements, conventions, commitments and codes of conduct (West. 2018). Good examples of friction between legally avoiding taxes and the general perception are the cases of Starbucks and Amazon.

When media reported accusations that Starbucks avoided taxes by reporting yearly losses due to insanely high royalty payments to its Dutch subsidiary, that even granted them tax refunds, their sales instantly dropped, and polls also showed that a third fewer people rated Starbucks as their preferred coffee shop compared to the polls before the tax avoidance allegation publication (The Economist, 2015). This negative sentiment and drop in sales even forced the management of Starbucks to transfer its European headquarters from Amsterdam to

[17] What 'fair' means will be elaborated on in a later section in this chapter.
[18] Thus, complying with the letter of the law but violating the spirit of the law.

London in the hope it would repair its reputation and regain its legitimacy[19] (The Economist, 2015). Amazon also had to deal with consequences due to its bad reputation obtained by its infamous tax avoidance strategies. When Amazon tried to open a new headquarters in New York in 2019, they faced heavy resistance from politicians and the local community. Activists of the local community, some lawmakers, and politicians even engaged in anti-Amazon protests causing Amazon to pull out of its plans to establish new headquarters in New York City, despite their great desire for talent in the New York metropolitan area (The New York Times, 2019).

The generally held perception is that every citizen and company engaging in a society has the moral obligation to pay taxes, as Honoré (1993, p. 5) argues "in principle a moral obligation ... to contribute to the expenses of meeting collective needs" (Scarpa and Signori, 2020). Therefore, "the role of the government is to construct a tax system such that the moral obligation of paying taxes is translated into legal norms to refrain from arbitrariness and to create a trust for all taxpayers that everyone will pay their fair share" (Gribnau & Jallai, 2017, p.18). However, creating a tax system without loopholes, inconsistencies, information asymmetries and imperfect laws for one country is already an incredibly hard task, enforcing an international tax system that consists of differing countries, regimes, and conflicts of interest can be regarded as nearly impossible. Therefore, the lack of an international tax system gets exploited by MNEs which grants them opportunities to avoid taxes that are non-existent for smaller companies and citizens (Aharony & Geva, 2003; Scarpa & Signori, 2020).

A perfect functioning international corporate tax system would not be necessary if MNEs would not only comply with the letter of the law but also with the spirit of the law. This is exactly the crux of the matter as MNEs argue that they comply with the letter of the law and therefore its practices are legitimate and legal, whereas opponents argue that they not only have to comply with the letter of the law but also in the spirit of the law, especially as not everyone has the same opportunities to avoid taxes (Falk, 1986). This is the point where ethics arise as the general perception entails and expects that MNEs should pay their fair share of tax and, therefore, often have to pay more than legally required. This general perception is held, based on the underlying belief that only complying with the letter of the law does not necessarily mean that the activity is fair or just (Payne & Raiborn, 2018). Especially these concepts of

[19] Despite the effort of Starbucks' management to repair its legitimacy and reputation loss by transferring its European headquarters, this didn't change Starbucks' tax avoidance practices in the long term. Starbucks still faces heavy criticism as in 2019 they did only pay £4m of tax despite ranking £387m in sales in the UK. Starbucks UK paid in the same year about seven times more in royalty payments than in tax. Starbucks justifies this by announcing that it "refreshed their global strategic priorities to refocus on maximising total shareholder return" (The Guardian, 2019c).

fairness and justice play a central role in the debate and are at the core of ethics. Therefore, an ethical assessment targeted at tax avoidance is required.

3.2. The Current Ethical Debate

Before ethically assessing tax avoidance by MNEs and taking a stance in the debate, it is worthwhile to provide a brief overview of some commonly used arguments and lines of reasoning that, both sides of the debate, use and rely on. Some of these arguments will be referred to later on in this thesis. First, I will discuss several (moral) arguments defending and morally justifying tax avoidance, which I will follow up with several (moral) arguments opposing tax avoidance.

3.2.1. (Ethical) Arguments Defending Tax Avoidance

Although generally seen as a highly doubtful practice, there are some arguments to be made in favour of tax avoidance (Scarpa & Signori, 2020). These arguments are often used by MNEs themselves as justification for their tax practices (Shirodkar et al., 2020).

(I) Tax is a legal issue and not a moral one

"Tax avoidance is a legal issue and not a moral one", scholars who advocate this statement argue, that since tax avoidance is legal, it is morally neutral, meaning that it is not subject to moral evaluation (Scarpa & Signori, 2020). The reasoning starts with the mandatory aspect of paying taxes as costs imposed by the government, and the only responsibility MNEs have is minimizing the costs while still complying with the letter of the law, therefore there are no moral constraints on exploiting legal opportunities (Anesa et al., 2019). Hansen et al. (1992, p. 683) state "even an extreme moralist could not expect the taxpayer to opt for the costliest election". The implications of this train of thought are, that once certain tax-avoiding practices are considered to be immoral or unacceptable, it would be the task of the government to change legislation and make these practices illegal (Stainer et al., 1997, p. 214; Scarpa & Signori, 2020). This argumentation is one of the most common non-market strategies[20] MNEs use to justify their tax practices (Shirodkar et al., 2020).

[20] Non-market strategies refer to a firm's activities outside of the marketplace that can help it gain a competitive advantage. This includes public political strategies (lobbying), media strategies (influencing), and private-public strategies (engaging with activists) (Baron, 2009).

(II) Maximizing shareholder value

An often-used argument to defend tax avoidance is based on the fundamental assumption that the only obligation managers (agents) of MNEs have, is to maximize its 'principals' (shareholders) profits. This is often called their 'fiduciary duty' (Hansen et al., 1992; Colle & Bennett, 2014). In practice, this means that minimizing the tax burden is a sound business plan that complies with the fiduciary duty agents have to their principals. Although most MNEs don't explicitly include such practices in their codes of conduct, some do. Vodafone for example is one of the few MNEs that specifically mentioned[21] in its code of conduct that it uses tax minimization strategies to maximize shareholder value (Colle & Bennett, 2014).

(III) Government inefficiency

"The government is inefficient in redistributing and the reallocating of resources", scholars who advocate this statement argue, that governments are inefficient in reallocating resources and tasks among the private and public actors. Therefore, it is morally justified and acceptable to keep as many assets as legally possible in the private sector (Stainer et al., 1997). The implications of this train of thought are, that MNEs are morally justified to minimize tax obligations if they use the acquired tax savings to increase general and social welfare, by, for instance, investing in research and development, infrastructure, and job creation (Davis et al., 2016, p. 49; Scarpa & Signori, 2020).

(IV) Liberalism

The last moral justification of tax avoidance provided is rooted in the philosophical liberalism theory. Locke, by many regarded as the father of liberalism, argues that all individuals have 'natural rights'[22] which are granted at birth (Scarpa & Signori, 2020). When building on this train of thought, scholars argue tax avoidance as a morally justified form of 'self-defence' as the government imposing income taxes is a violation of those natural rights, this as earnings that individuals acquire themselves are handed to others without having a free choice on who receives them (Machan, 2012). Also, libertarian scholars argue that taxation imposed by governments is an "unjustified interference in the free-market order of things"

[21] Whereas in 2014 Vodafone explicitly stated in its code of conduct to use "tax minimization strategies to maximize shareholder value", in 2020 Vodafone is less explicit in its code of conduct and state that they "base their investment decisions, acquisitions and business relationships to provide the best possible return for their shareholders in the longer term" (Vodafone, 2020).

[22] Examples of natural rights are liberty, property, and the right to life (Scarpa & Signori, 2020).

(McGee, 2010, p. 34). Therefore, MNEs do have the right and moral support to avoid taxes as an expression of liberty, especially as they create employment and boost economic activity (Scarpa & Signori, 2020; Colle & Bennett, 2014).

3.2.2. (Ethical) Arguments Opposing Tax Avoidance

Although there exists moral reasoning justifying tax avoidance, most scholars agree that tax avoidance is a highly doubtful practice (Hansen et al., 1992; Scarpa & Signori, 2020). The following (ethical) arguments argue that although being legal, engaging in such practices can be regarded as immoral behaviour and should be ostracized. As chapter two already includes a significant section dealing with the ramifications of tax avoidance for the general welfare and socio-economic conditions, the following arguments opposing tax avoidance will be of an ethical nature.

(I) Utilitarianism

The 'Utilitarianism perspective' argues that a practice is right or wrong depending on the social consequences. Therefore, agents (MNEs) should act in a manner that maximizes utility or welfare or at least minimizes the amount of harm for the greatest number of agents affected by its practices. However, utility is an abstract concept and in reality, there is no quantitative measure that compares the benefits with the harm of one's practices. Therefore, it is hard to determine when utility is maximized. Still, there is a consensus among scholars that the negative consequences of tax avoidance outweigh the positive short-term gains (Preuss, 2012; Godar et al., 2005; Payne & Raiborn. 2018; Scarpa & Signori, 2020). The reasoning behind this consensus is, that tax avoidance, is typically only beneficial for MNEs' shareholders and its managers that directly benefit due to bonus structures related to the profit an MNE makes (Weinzierl, 2018). Although there are arguments to make that the broader community also benefits from tax avoidance from MNEs, these benefits seem to be neglectable when compared to the negative ramifications for companies, governments, and citizens as already explained in chapter two.

(II) Kantianism

The 'Kantianism perspective' is based on a theoretical framework provided by the famous German philosopher Immanuel Kant. This 'Categorical Imperative' framework means, "an objective, rationally necessary and unconditional principle", is used to determine and derive moral duties and rules for all ethical issues (Johnson & Cureton, 2004; Scarpa & Signori,

2020). The main principle of this theory is to act only according to the maxim (in this case tax legislation laws) that you would like to see as a universal law (Kant ,1786/2012, pp. 421-429; Scarpa & Signori, 2020).

Using this line of reasoning and to assess whether tax avoidance is an immoral practice or not, two questions have to be raised and answered. The first would be if we would want that everybody is engaged in tax avoidance, so no exceptions or contradictions, this is called the consistency principle. The second would be scrutinizing if tax avoidance would be a respectable practice, fully respecting human dignity, this is called the human dignity principle (Scarpa & Signori, 2020).

A lot of scholars answered these questions and concluded that tax avoidance is an immoral practice as it violates both the consistency principle and the human dignity principle. The violation of the consistency principle can be found in the unequal opportunities SMEs and citizens have compared to MNEs, therefore, only MNEs can create a competitive advantage and creates inconsistencies in society (Preuss, 2012). Furthermore, the human dignity principle is violated as avoiding taxes is not a respectful practice for human beings, as every human, good or bad should be treated as an end, and follow the moral principles that give appropriate recognition to the autonomy of each person and shape their life by general policies that rationally can be regarded as permissible and should be followed by everyone (Kant, 1786/2012, p. 421-429). In the case of tax avoidance by MNEs, humanity is not treated as an end and general policies are not followed. Also, general society loses and governments for instance cannot provide certain public goods and services anymore due to their eroded tax base (Payne & Raiborn, 2018; Preuss, 2012).

(III) The undermining of compliance

As mentioned earlier "the role of the government is to construct a tax system such that the moral obligation of paying taxes is translated into legal norms to refrain from arbitrariness and to create a trust for all taxpayers that everyone will pay their fair share" (Gribnau & Jallai, 2017, p. 18). However, tax avoidance by MNEs undermines the integrity of the tax system and therefore could weaken compliance (Colle & Bennett, 2014). This reasoning is also supported by the OECD (2011) as they stated that these tax practices not only erode the tax base but also threatens the perceived fairness of the tax system. A ramification of this perceived unfair tax system is that people are less compliant with tax laws as they experience to have a higher tax burden than others (Colle & Bennett, 2014).

(IV) Theory of Justice

The last ethical argument opposing tax avoidance that will be provided in this thesis is rooted in the ethics of justice which focuses on justice and fairness. This stream in ethics uses a deontological framework (stresses that what makes a choice right is its conformity with a moral norm), based on three principles that are founded by John Rawls and introduced in his monumental work called the '*Theory of Justice'* (Simmons, 2010; Stemplowska & Swift, 2012). These principles will be used in combination with Rawls' ideal and nonideal theory, for the ethical assessment of tax avoidance by MNEs and the case study. This is the most suitable ethical school of thought due to its focus on fairness and justice which are crucial concepts that shape underlying principles and beliefs that play a central role in the tax avoidance debate. Therefore, a more detailed and thorough assessment will follow in the next section that will help to determine what principles could be established in addition to the principles shaped by the League of Nations. Adding new principles can help to ultimately achieve a more just society compared to society as its nowadays. Ideal theory will be provided as this is considered as a necessary precursor that gives direction and an end goal to nonideal theory (Stemplowska & Swift, 2012). This nonideal theory will be at the centre of the ethical assessment as it deals with a nonideal world[23] and can create a better understanding of what measures should be taken to achieve an ideal or a comparatively (more) just world (Stemplowska & Swift, 2012).

3.3. Ideal Theory

Rawls's conception of ideal theory assumes strict compliance, to the principles of justice, by all those in society (especially institutions), meaning that everyone should act to the best of their ability to create a just and well-ordered society under favourable circumstances (socioeconomic limitations) (Rawls, 1999; Simmons 2010). Those principles of justice are more precisely formulated and entail (Rawls, 1999, p. 266):

1) *Each person has the same indefeasible claim to a fully adequate scheme of equal basic liberties, which scheme is compatible with the same scheme of liberties for all (the liberty principle),* and

2) *Social and economic inequalities are to satisfy two conditions:*
   a. *They are to be attached to offices and positions open to all under conditions of fair equality of opportunity;*
   b. *They are to be to the greatest benefit of the least-advantaged members of society (the difference principle)* (Rawls, 2001, p. 42-43).

[23] The world we live in nowadays can also be regarded as a nonideal world.

When strict compliance is achieved, a just society arises, which Rawls describes as a "realistic utopia". This realistic utopia is characterized as a society "that is the best we can realistically hope for", taking into account human nature and the laws as they might be (Rawls, 1999, p. 89). This ideal world is a thought experiment that relies on speculation and conjecture to determine what would be "practically possible" based on realistic assumptions to avoid idle utopianism (Simmons, 2010). Important to note is that these principles of justice are aimed to establish *domestic* distributive justice (Rawls, 1999). Therefore, concerns may arise that applying *domestic* principles of justice to this *international* problem of tax avoidance by MNEs is a wrong approach[24]. However, this thesis aims to scrutinize if the current international tax system is just, and if not, what measures could be taken to create a comparatively more just system. Therefore, it is important to keep in mind that this current *international* corporate income tax system, has an effect on domestic justice and results often in domestic injustice which is suitable for normative assessment and application of the principles of justice as theorized by Rawls.

The two most important assumptions of ideal theory are strict compliance and favourable circumstances, these are used among others to distinguish ideal theory from non-ideal theory. Both these assumptions are to a certain extent idealizing and insensitive to the real world. For example, the strict compliance assumption is obviously departing from reality as in every society there is a widespread unwillingness to behave justly (Simmons, 2010). Whereas, the favourable circumstances assumption is a lot more realistic as there are countries and societies in the modern world that are regarded as having favourable circumstances (Stemplowska & Swift, 2012). Although both assumptions are idealizing to a certain extent, Rawls attempted to limit the degree to which those assumptions could depart from real-world constraints by requiring the assumptions to be practically possible (Rawls, 1999, p. 89). For example, the strict compliance assumption should be used as a means to identify the requirements that are necessary for people to comply healthily with the proposed principles of justice. Indicating that for complying with those proposed principles a mere sense of justice is

[24] There is extensive literature reporting on the importance of global collaboration to tackle the international tax avoidance problem (Pogge & Mehta, 2016; Cappelen, 2001; Gillian, 2008). Therefore, applying domestic principles of justice may seem like a wrong approach. However, this section is not aimed to come up with an approach to tackle the tax avoidance problem, it is aimed to normatively assess the ramifications of this international problem on domestic justice. This enables me to ultimately compare different international taxation systems based on their ramifications on domestic justice. This comparative stance further allows me to endorse an alternative system that is in normative terms comparatively more just (this alternative system does indeed require global collaboration). Therefore, applying the domestic principles of justice to this international problem isn't a wrong approach and provides additional substantiation and confirmation, by the means of ethics, to the claims made in the literature.

needed, not a psychologically burdensome attempt for moral heroism (Stemplowska & Swift, 2012). This is important as complying with the principles of justice shouldn't require great difficulty as it would otherwise be highly unlikely that the imposed constraints of these principles of justice would receive support in the long term (Simmons, 2010). The same holds for the favourable circumstances' assumption, as this does not mean that circumstances should be perfect, instead it should identify socioeconomic contingencies that make justice harder to achieve, for instance: poverty, corruption, and culture (Simmons, 2010). Although critics are attacking the assumptions by the means of their unrealistic and idealizing nature, they are widely accepted as fairly plain and necessary boundaries for ideal theory (Simmons, 2010; Sen, 2006).

The goals of these two idealizing assumptions are to determine the requirements for perfect justice in an ideal world. To find perfect justice, an assumption of strict compliance is necessary as, without strict compliance, the requirements for perfect justice are not met. However, due to unfortunate circumstances, such as poverty, corruption, culture, or recovery from (natural) disasters, a perfectly just society is sometimes made impossible. Therefore, the favourable circumstances assumption is introduced to deal with socioeconomic conditions (Rawls, 1999; Stemplowska and Swift, 2012). When these assumptions hold the requirements for an ideal world with perfect justice become evident. This is important as the ideal theory is according to Rawls, and scholars of the Rawlsian theory of justice, a necessary precursor to nonideal theory, as it provides an aim and target for nonideal theory (Rawls, 1999, p. 90; Simmons, 2010; Stemplowska & Swift, 2012). In Rawls his other monumental work called the '*Law of the people*' he stated, "until the ideal is identified … nonideal theory lacks an objective and aim, by reference to which it queries can be answered" (Rawls, 1999, p. 90). In this manner, the imaginary ideal world could be of guidance as an endpoint when confronted with a nonideal world in which choices have to be made to reach the desired endpoint.

3.3.1. Ideal Theory: a Thought Experiment

As mentioned earlier, ideal theory can be of guidance as an endpoint when confronted with a nonideal world. Therefore, a thought experiment will be provided with as aim to create an ideal world based on the principles of justice and under the assumptions of strict compliance and favourable circumstances. This ideal world that I will try to establish is the product of a thought experiment when applying Rawls' principles of justice to the topic of tax avoidance and the current international tax system. This serves as an end goal that can be used to give a direction to solutions found after assessing the current tax situation with nonideal theory to ultimately

realize a comparatively more just system. Although, this will not mean that this ideal world is without its flaws and is completely fair or just.

As can be read in the previous section, Rawls established two principles of justice to which strict compliance is required. Assume that this imaginary society in an ideal world has wealth, political stability, no corruption, and is not recovering from a (natural) disaster, therefore meeting the assumption of favourable circumstances (Rawls, 1999; Stemplowska & Swift, 2012). In this world there exists a government that raises tax revenue by levying taxes that it uses for the provision of public goods and services. In this world, companies, and individuals pay taxes to the government that generates its tax bases. When applying the difference principle on a topic such as taxation, inequalities in society that are the result of a tax policy are only allowed if those benefit the least-advantaged members of society (Rawls, 2001). This would mean that there will be either no income taxes for companies and individuals or, if present, progressive income taxes for both. To refrain from taking a stance in the debate on the abolition of income taxes, I argue that both a progressive income tax and the abolition of income taxes would be options to create a more just society as they both don't violate the difference principle (The Economist, 2012). However, as not only the international tax system but also tax avoidance by MNEs is a subject for normative assessment in this thesis, I will assume from here on, that in this ideal world there will be progressive taxation as otherwise discussing tax avoidance in the absence of taxes would make no sense.

When there exists progressive taxation, companies and individuals would only be allowed to avoid taxes if the opportunity of avoiding taxes is equal for all, so not violating the equality of opportunity principle (Rawls, 1999). Furthermore, avoiding taxes would only be allowed if the ramifications of tax avoidance would not include any form of inequality. However, an exception would be if the least-advantaged in society would benefit from this inequality, therefore not violating the difference principle (Rawls, 1999). Although, it would be highly likely that tax avoidance would violate at least one of these principles and, therefore will be non-existent in this ideal world, as it is classified as unjust. It could theoretically be possible that in an ideal world there would still exist tax avoidance as actual circumstances should always be taken into account when informing the requirements of ideal theory (Rawls, 1999, p. 377). However, tax avoidance would only be justified if it would help to transform a less fortunate society into one in which basic liberties can comparatively better be enjoyed (Rawls, 1999). Although, in the case of tax avoidance this is unlikely as MNEs mostly avoid taxes to maximize shareholder value and will most likely not benefit society in general (Hansen et al., 1992; Colle & Bennett, 2014). However, there still exists the possibility that some

societies could benefit from tax avoidance by MNEs, as an MNE can decide to invest the money it saves by avoiding taxes into the society by, for instance, improving education or infrastructure[25] (Davis et al., 2016**)**. In this way, the tax avoidance would be justified by the liberty principle of ideal theory.

Concluding, in this ideal world there would be strict compliance and favourable circumstances. Furthermore, it could be the case that income taxes are abolished, but if present, levied in a progressive manner such that any inequality benefits the least-advantaged in society. In the case of progressive taxation, it would be highly unlikely that tax avoidance will be existing as in almost every case it will violate at least one principle of justice and thus will be classified as unjust (Rawls, 1999). Justification of tax avoidance can only be achieved if basic liberties can be better enjoyed compared to the situation without tax avoidance, so based on the liberty principle. Any further exploration of how an ideal world would look like or what actual circumstances would justify tax avoidance is beyond the scope of this thesis.

3.4. Nonideal Theory

Whereas the concept of ideal theory assumes strict compliance, to the principles of justice under favourable circumstances, nonideal theory deals with obstacles occurring in the form of injustice due to partial compliance and unfavourable circumstances (socioeconomic limitations) (Stemplowska & Swift, 2012). Therefore, nonideal theory gives guidance on how to deal with injustice, and accordingly what is needed to make those that partially comply, "strictly complying" (Rawls, 1999, p. 8; Simmons, 2010). It also helps to determine what injustices are more grievous and therefore have higher urgency to be dealt with. It accomplishes this by mandating three requirements for the proposed directions of action, namely: (I) "politically possible", (II) "morally permissible" and (III) "likely to be effective" (Rawls, 1999, p. 89; Simmons, 2010). If a proposed direction of action meets these criteria, the likelihood that it will lead towards perfect justice is significantly higher opposed to a direction of action that doesn't meet those criteria. Therefore, nonideal theory can help with the transition from injustice to justice.

For nonideal theory to be applied, it is first required to assess if tax avoidance by MNEs and the current international tax system are either just or unjust. Tax avoidance and the current international tax system will be classified as unjust if violating one or more of Rawls' principles of justice. In addition, as mentioned earlier, justice and fairness are important ethical values

[25] Thus, taking over the role of the government (Davis et al., 2016).

underlying commonly held beliefs that are at the centre of the tax avoidance debate. Therefore, it's important to conceptualize justice and fairness[26] for the remainder of this thesis. From here on, a practice will be regarded as either 'just' or 'fair' if the practice doesn't violate one of the principles of justice as established by Rawls (Rawls, 1999). If tax avoidance and the current international tax system get ethically assessed as unjust, nonideal theory will be used when proposing alternatives to the current international tax system to ultimately achieve a comparatively more just international tax system compared to the former.

3.5. Tax Avoidance: a Normative Assessment

As mentioned earlier, Rawls' theory of justice concerns domestic justice and not international justice (Rawls, 1999). Therefore, it may seem wrong to apply Rawls' principles of justice to the current international tax system and tax avoidance. However, the aim is to assess the domestic ramifications of tax avoidance that are the result of the current international tax system, which makes the application of Rawls' principles of justice perfectly possible. In the next sections, there will be often referred to the principles of justice as defined in section 3.3, and to the ramifications of tax avoidance as mentioned in section 2.3.

3.5.1. Inequality

As explained in section 2.3, inequality is one of the most profound ramifications of tax avoidance. When relating inequality to the second principle of justice, an assessment of the justness of tax avoidance and the current international tax system can be provided. If applying the 'equality of opportunity' principle to inequality, it is clear that tax avoidance is not available to "offices and positions open to all" (Rawls, 1999, p. 266). This as SMEs and individuals are not able to benefit from tax avoidance in a way MNEs can. MNEs can do this as they have a global presence and tax avoidance requires the possibility to cross borders as already explained in section 2.3. This becomes even more apparent as capital has much higher mobility compared to for instance labour. This is important as MNEs can easily move their profits to a low tax

[26] In Rawls' paper 'Justice as fairness', Rawls claims that the impression that justice equals fairness is mistaken. Rawls argues that the fundamental idea in the concept of justice is fairness and he indicates this by the notion that involves the mutual acceptance of the principles of justice and the practice under normative evaluation. Therefore, Rawls argues that when individuals differ in the ethical values they support, justice doesn't necessarily equal fairness. However, accounting for this distinction in the normative assessment only increases complexity and goes beyond the scope of this thesis, and I, therefore, assume that every actor supports the same ethical values and beliefs. Therefore, for the remainder of this thesis, only justice will be identified by the means of the principles of justice. This implies that justice equals fairness and will in the context of this thesis be used interchangeably (Rawls, 1958).

jurisdiction of choice, such as Bermuda, to benefit from their highly favourable tax regime. However, it's much harder for a nurse to benefit from the highly favourable tax regime in Bermuda due to the low mobility of labour. Since mobility is the key factor to avoid taxes, it also increases inequality between 'capital earners' and 'labour earners', even more, as those 'capital earners'[27] can avoid taxes whereas this is incredibly hard for 'labour earners'. Therefore, the possibility to avoid taxes for a nurse is almost non-existent, whereas the Chief Executive Officer (CEO) of an MNE does have the possibility to avoid taxes. This inequality that results from tax avoidance, which in turn results from the way the current international tax system is shaped, violates the equality of opportunity principle and can therefore be classified as unjust.

As mentioned above, MNEs can avoid taxes whereas this is incredibly more difficult for SMEs. A ramification of this inequality of opportunity is the undermining of competition by violating the principles of fair competition as established by the Institute of Business Ethics (IBE) (IBE, 2018). This occurs as MNEs compete with SMEs but pay relatively less tax and therefore gaining a competitive advantage (OECD, 2009b). These same MNEs already have a competitive advantage over SMEs due to increasing returns to scale and even outperform them more as they have a relatively lower tax burden (OECD, 2009b). Therefore, the bigger the company is the more opportunities it has to avoid taxes, which in turn makes the company even bigger as the costs of producing decrease even further (increasing returns to scale). This could ultimately lead to a situation in which the market is dominated by one immensely large MNE that acquired a monopoly by buying all its competitors or pushing them out of the market. This monopoly would be a highly unfavourable outcome as this MNE could abuse their market position at the costs of individuals, and therefore increasing inequality even more. Although this may seem a bit exaggerated, there are clear examples that this is happening in reality. Take for instance the rise of Amazon since the 2000s. First starting as an online retailer but now expanded its practices to cloud computing, owning a streaming service and movie studios, retail and logistics that arms everything from podcasting to low-orbit, satellite-delivered broadband, home security, microchip development, prescription drug distribution, and military contracting. Amazon is an economy in itself and a perfect example of inequality as most of its more than one million employees earn a minimum wage while its CEO Jeff Bezos is the richest man on earth (The Guardian, 2021a). The rise of Amazon can for a significant amount be attributed to tax avoidance, as Bezos located Amazon in Seattle to take advantage of a sales tax loophole.

[27] Capital earners are mostly already in the upper end of the income distribution (Piketty, 2014).

This provided Amazon a competitive advantage as it didn't have to pay sale taxes except for the state it is located in, which is Washington: a relatively small state (The Guardian, 2021a). Of course, is tax avoidance not the sole reason for Amazon's success but it plays a huge role in it. This example illustrates that the opportunity to avoid taxes creates a competitive advantage that is not "open to all offices and positions" and therefore violates the equality of opportunity principle (Rawls, 1999). Due to violating this principle, there is additional substantiation why tax avoidance can be classified as unjust.

But some might argue, that everyone has the same opportunities to become a nurse or a CEO of an MNE (Van Dijck, 2016). Therefore, having the same opportunity to avoid taxes, and thus not violating the equality of opportunity principle. I argue that this reasoning is flawed. It is indeed true the opportunity to avoid taxes is tied to being a CEO of an MNE, and if everyone has the equal opportunity to become a CEO of an MNE, everyone also has the equal opportunity to avoid taxes. However, in reality, there are numerous reasons why not everyone has the equal opportunity to become a CEO of an MNE. For example, becoming a CEO of an MNE usually requires a degree from a university or a highly valued business school (Van Dijck, 2016). This type of education is not available to all as some might face unfavourable socioeconomic circumstances such as poverty. However, in a lot of developed countries, governments provide public provisions such as education. But this becomes increasingly hard if tax avoidance erodes their tax bases (Atkinson, 2015). When faced with an eroded tax base, governments will not be able to fulfil their role as the provider of public goods and services, resulting in losses for those least-advantaged in society that needs them most. This is as individuals that are born in wealthy families don't have to rely upon, or at least to a lesser degree, on this public provision of education provided by the government compared to the least-advantaged in society. The above is only one example out of many that equality of opportunity does not exist, and thus creates an inequality of opportunity to avoid taxes[28]. This is again a violation of Rawls' second principle of justice and is another example of injustice caused by tax avoidance. However, in this last case, the inequality of opportunity and corresponding injustice is a result of the current international tax system and its relation to domestic justice and can't only be attributed to

[28] A difficulty with an analysis like this is the agency issue: who bears moral responsibility for profits and losses from tax avoidance, and who/what is subject to moral evaluation when condemning tax avoidance. One could argue that MNEs and their CEOs are responsible, however, I refrain from this stance as these organisations and individuals fulfil their fiduciary duty to their shareholders to maximize shareholder value, and do need to stay competitive. Therefore, I argue that tax avoidance and its negative socioeconomic ramifications are to be attributed to the current international tax system that facilitates it. Implying that if a change is desirable, the 'game' should be changed, instead of the behaviour of its 'players'.

unequal chances of becoming a CEO of an MNE. Therefore, it seems that both tax avoidance and the current international tax system can be classified as unjust.

3.5.2. Governments' Tax Base

The inequality resulting from tax avoidance and the current international tax system not only violates the equality of opportunity principle but also the difference principle. As mentioned above, not everyone does have the opportunity to avoid taxes. In practice, this implies that a small part of society, mostly located in the upper segment of the income distribution, avoids taxes whereas the rest, including the least well off, need to pay their taxes. As explained in section 2.3. this means that those least-advantaged are increasingly burdened with state financing to enable the provision of public goods and services by the government (Rixen, 2014; Piketty, 2014; Atkinson, 2015). The result is that the least advantaged pay relatively more tax but receive less in return, thus making them less off compared to the situation without tax avoidance. Even if a domestic government applies progressive taxation, this gets undermined by the current international tax system as it allows those at the top of the income distribution to avoid taxes. Therefore, creating a regressive taxation system with the lowest tax rates applying to those at the top of the income distribution (Piketty, 2014; Rixen, 2016). This regressive taxation that results due to the current international tax system is violating the difference principle and can be classified as unjust as it makes the least-advantaged in society even worse off. In some extreme cases such as in developing economies where tax avoidance also has a very direct impact on life or death, its violation of the principles of justice is even more severe (WorldFinance, 2015). This as basic liberties are endangered due to the ramifications of tax avoidance and therefore also violating the liberty principle of justice.

When comparing the current regressive tax system to the progressive one as hypothesized in section 3.3.1., a redistribution is needed to correct for the unjust inequality it creates. Rawls would argue that the domestic inequality and injustice that are the result of tax avoidance and the current international tax system needs to be addressed by shifting the tax burden from those least well off to the wealthy, and this is exactly what a progressive tax system entails (Van Dijk, 2016). The redistribution that is taking place only increases the inequality even more due to the current international tax system. Revisioning the current redistribution is one of the most important tasks of national governments. However, due to the current international tax system, the governments' capacity to enforce progressive taxation is

constrained as it risks losing its tax base to lower-tax jurisdictions[29] (Van Dijck, 2016). Exactly this progressive taxation could satisfy the difference principle but gets undermined by the current international tax system. Governments, therefore, face rough choices that could cost them their tax base if opting for a progressive tax system. However, progressive taxation seems to be a requirement for domestic justice and therefore international cooperation is necessary to enable governments to execute their tax plans (James, 2013; Van Dijck, 2016).

To conclude, tax avoidance and the current international tax system can be classified as unjust on multiple levels. This is as they create unjust inequality that violates both the equality of opportunity and the difference principle. Of course, not all domestic inequality is the result of tax avoidance and the current international tax system. However, the current international tax system also undermines the opportunity to correct this unjust inequality by constraining governments in its possibilities to shift the redistribution from a regressive to a progressive one.

3.5.3. Free Riding

As elaborated on in section 2.3., MNEs do make intensive use of public goods and services. These public goods and services benefit all in society. Therefore, it seems logical that everyone pays their fair share to contribute to the expenses of meeting collective needs (Scarpa and Signori, 2020). However, as it's a collective obligation there always exists an incentive to free ride since the non-compliance of an individual doesn't seriously affect the governments' tax base (Rawls, 1999). A good example of an individual not complying with its tax duty and still benefitting from public goods and services is the protection of national defence. An individual will never be excluded from protection by the national defence in case of danger, even if the individual pays no tax (Van Dijck, 2016). Therefore, the trust that all taxpayers will pay their fair share is particularly important as when this trust is lost it endangers the compliance of those that pay their taxes. This is logical as those paying their taxes want reassurance that everyone does so, otherwise, they experience this as unfair (Rawls, 1999). Therefore, a just tax system is needed that enforces payment and reassures that everyone pays their fair share.

However, the current international tax system undermines this just tax system. Despite there being a difference between tax evasion and tax avoidance, the result of both for the governments' tax bases and the general perception of this practice remains the same. MNEs avoid taxes while it's one of the most intensive users of public goods and services in a country

[29] This gets supported by the study of Abbas & Klemm (2013) who illustrated by the means of regression analysis that opting for progressive taxation has adverse effects for domestic investment, FDI, and tax revenue in emerging and developing economies. This can partly be attributed to the existence of tax havens (Abbas & Klemm, 2013).

(Van Dijck, 2016). This is unfair as not everyone has the same opportunity to avoid taxes as already mentioned earlier in section 3.5.1. Especially as justice requires that everyone is treated as equals and pay their fair share (Gribnau & Jallai, 2017). Therefore, MNEs not paying their fair share and undermining the tax system violates the requirements of justice and can thus be classified as unjust or unfair.

3.6. Conclusion

Although there exists moral reasoning justifying tax avoidance, most scholars agree that tax avoidance is an unjust practice (Hansen et al., 1992; Scarpa & Signori, 2020). Since the confines of this thesis don't allow a deep exploration of a large number of theories, I chose to highlight some important theories in combination with an application of Rawls' theory of justice and ideal/nonideal theory. Utilitarianism, Kantianism, and Rawls' theory of justice all conclude that tax avoidance and the current international tax system are unjust. The diversity of these theories strengthens the conclusion of the normative assessment. Despite they differ in some respects and might not agree with each other in every aspect, they still all conclude that tax avoidance and the current international tax system are unjust. This as tax avoidance and the current international tax system creates inequalities that undermine competition, the governments' capability to execute its tax plans, and facilitates free riding on public goods and services, therefore violating all principles of justice.

Now tax avoidance and the current international tax system are classified as unjust, nonideal theory will be applied to the case study and chapter five. This as nonideal theory can guide the transition from this injustice to justice. This will be done by challenging the current international tax system as this enables tax avoidance. The reasoning will be that if the proposed alternatives to the current international tax system do not or at least to a lesser degree violate the principles of justice this will be, ceteris paribus, a comparatively more just system. It could be the case that the alternatives will still be to a certain extent unjust, but if they are less unjust compared to the current situation it will still be a progression.

4. The Case: G7 Tax Deal

As explained in chapter two, tax avoidance erodes governments' tax bases which makes it hard for them to fulfil their role as the provider of public goods and services (Rixen, 2015). Despite this being a huge problem, it took years of discussion between nations to reach an agreement to tackle tax avoidance. However, in early June 2021, a "historic" agreement between the G7 countries was made that would "overhaul" the "broken" current international tax system and transform it into "a fairer tax system fit for the 21st Century" (The Guardian, 2021b). Since fairness and justice play a central role in this thesis, the 'G7 tax deal' is perfectly suitable for a case study. First, the content of this G7 tax deal will be discussed and followed up by an overview of the stakeholders' receptions. At last, the G7 tax deal will be subjected to nonideal theory to assess its potential of transforming the unjust current international tax system into a comparatively more just one.

4.1. What Does the G7 Tax Deal Entail?

The G7[30] is a group of the world's leading industrial nations that consists of Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States. The leaders of these seven nations annually meet in the form of G7 summits to determine the course of multilateral discourse and to shape political responses to global challenges (European Commission, 2021). After the last G7 summit these nations reached an agreement that targets the largest MNEs and could yield billions of dollars for governments' tax bases (Reuters, 2021a). Despite the belief of the G7 leaders that this agreement will change the world, it will still probably take years of talks and negotiations for this agreement to be globally enforced. This as the agreement still has to be proposed in the G20 summit in October 2021, that not only consists of western economic powers but also from nations like Brazil, Russia, India, and China. These nations could have different takes on certain aspects of the agreement that even within the G7 nations remain as sticking points (The Guardian, 2021b).

The G7 tax deal mainly consists of two changes to the current international tax system. From now on, for the sake of clarity, I'll use the terms first and second pillar when referring to the two changes of the G7 agreement. First, the G7 nations agreed on a global minimum corporate tax rate of at least 15%. This 15% will be a minimum but is still able to increase as

[30] Group of seven of the world's leading industrial nations.

some nations such as the United States and France opt for a higher minimum corporate tax rate (Reuters, 2021a). This measure is aimed to stop the 'race to the bottom' of tax competition between nations. Second, the G7 nations agreed on a proposal to enable nations to tax at least 20% of MNEs' profits of those MNEs whose global profit margins exceed 10% (The Guardian, 2021b). This second pillar is aimed to stop MNEs from reporting their profits in tax havens in which they only have a legal presence but don't operate from, and thus enables nations to tax the profits of those MNEs that are generated within the borders of those nations (The Guardian, 2021b). Due to these two principles nations could also collect underpaid taxes of their MNEs. For example, assume again that the imaginary LTC MNE has its headquarters in the United States and a subsidiary in Ireland. The United States can now levy an additional tax on LTC's profits if taxes in Ireland are lower than the 15% global minimum corporate tax rate to reach the minimum corporate tax rate of 15%. Also, if LTC would decide to move its headquarters to a lower tax jurisdiction such as Ireland and establish a subsidiary in the United States, the United States are now allowed to levy the minimum corporate tax rate to LTC's operations within its borders if Ireland does not apply the minimum corporate tax rate. The additional raised tax revenue of this agreement could be huge as the OECD estimates that the first pillar could yield additional annual tax revenue of $42-70 billion whereas the second pillar could yield additional annual tax revenue of $5-12 billion (OECD, 2021; The Guardian, 2021b).

It's interesting to explore which MNEs would get affected by this G7 tax deal. The first pillar will probably affect around 8000 MNEs whereas the second pillar probably affects only 100 MNEs according to the US Treasury Secretary, Janet Yellen (The Guardian, 2021b). Whereas the first pillar is a more general approach to end the 'race to the bottom' of tax competition between nations, the second pillar is a more targeted approach to levy taxes on the largest and most wealthy MNEs. Among those 100 MNEs are companies such as Apple, Microsoft, Netflix, and Alphabet, however, concerns exist that Amazon is not caught by this second pillar since it reported a global profit margin of only 6.3% in 2020, which is lower than the required 10% (The Guardian, 2021b). Therefore, there are concerns if the G7 tax deal will be able fulfil the promises made by the G7 leaders.

4.2. Stakeholders' Reactions

In this part, a brief overview of some reactions of stakeholders regarding the G7 tax deal will be provided as this gives insights into differing interests from those involved. These insights will be referred to in the last section of this chapter when applying nonideal theory on the G7 tax deal.

(I) G7 nations

It is hardly surprising that representatives of the G7 nations are all in favour of the G7 tax deal as this was unanimously agreed upon (The Guardian, 2021b). Rishi Sunak, the UK. Finance Minister stated, "After years of discussion, G7 finance ministers have reached a historic agreement to reform the global tax system to make it fit for the global digital age" (Reuters, 2021b). This sentiment is shared among those representatives of the G7 nations. However, two sticking points remain open for debate among these nations. First, the minimum global tax rate of 15%, the United States and France both opt for a higher minimum tax rate whereas the United Kingdom wants it to keep as close to the 15% as possible (CNBC, 2021). Second, in the United States itself, the G7 tax deal still needs to pass the Senate that also consists of a lot of republicans that already vowed to oppose the Biden Administration's tax deal for differing reasons (Reuters, 2021c).

(II) G20 nations

Among G20 nations there is disharmony regarding the G7 tax deal. Nations like Mexico, Indonesia, and South Africa already announced to support the G7 tax deal (Reuters, 2021d). However, support from China and the European Union[31] (EU) is crucial for the G7 tax deal to succeed. China already announced its concerns as it doesn't want to give up on its national fiscal sovereignty. The ability to lower taxes enabled China to establish low taxation zones that are at the centre of their economic development over the last decades, and it, therefore, wishes exemptions for these low taxation zones (Reuters, 2021d). Furthermore, several nations of the EU including Poland, Hungary, and Ireland already announced that they will oppose the global minimum tax rate as long as this G7 deal doesn't include exemptions. They support this with the reasoning that smaller economies need the ability to stay competitive with their tax rates to protect business activity within their nations and to attract FDI (ITR, 2021). This is problematic as the EU's decision needs to be unanimous, or it will encounter immense difficulties when implementing new tax legislation (CER, 2021).

(III) Low tax nations and tax havens

As already mentioned above, low tax nations like Poland, Hungary and Ireland already announced to oppose the G7 tax deal to stay competitive and protect their favourable tax regimes (ITR, 2021). Swiss, another low tax country that distinguishes itself due to its

[31] The European Union operates as a single member in the G20

favourable corporate tax rates already announced by its finance ministry that "Switzerland will take the necessary measures to continue to be a highly attractive business location" (Reuters, 2021e). Although there are lots of examples of low tax nations opposing the G7 tax deal, it is striking that amongst some tax havens there is support for the G7 tax deal. The finance ministers from the Netherlands and the Cayman Islands both announced to support the decision made by the G7 (The Japan Times, 2021; CNS, 2021). However, the finance minister of Bermuda strongly opposes the G7 Tax deal and claims that its sovereignty will be endangered (The Irish Times, 2021).

(IV) NGOs and campaigners

The G7 tax deal doesn't get much support from Non-Governmental Organization(s) (NGO) and campaigners. They claim it to be "absurd" to state that this tax deal will "overhaul" the broken current international tax system as "the 15% minimum corporate tax rate is similar to the soft tax rates of Ireland, Switzerland, and Singapore" (BBC, 2021). Oxfam's executive director also stated that "they are setting the bar so low that companies just step over it" (BBC, 2021). Another critique that Oxfam, Eurodad, and the Tax Justice Network mention is the extreme unfair nature of the G7 tax deal as it will benefit the wealthiest nations in the world leaving little for developing nations where MNEs also operate[32] (Reuters, 2021f).

(V) MNEs

The G7 tax deal aims to increase the tax burden of MNEs. These MNEs collectively are expected to pay around $47-82 billion more annually due to these additional taxes (OECD, 2021; The Guardian, 2021b). Therefore, one may expect strong opposition from representatives of these MNEs. However, spokespersons from MNEs such as Amazon, Google, and Facebook all publicly supported the G7 tax deal (Reuters, 2021b). A response from a Google spokesperson that is exemplary even stated: "We strongly support the work being done to update international tax rules. We hope countries continue to work together to ensure a balanced and durable agreement will be finalised soon" (Reuters, 2021b).

[32] The minimum tax rate of 15% is applicable at the headquarters jurisdiction level. This implies that the treasuries of jurisdictions where many large MNEs are headquartered will benefit most in terms of increased revenue. Since most MNEs are headquartered in the US or Europe, they will gain the most. Therefore, developing nations in which MNEs mostly have subsidiaries for production will receive less. Furthermore, do developing nations lose one of their 'unique selling points' as these nations are no longer able to attract FDI from MNEs by the means of lower tax rates, thus reducing the incentive for MNEs to operate in those countries (Taxjournal, 2021).

4.3. G7 Tax Deal and Nonideal Theory

As mentioned in section 3.4., nonideal theory can be of guidance when applied to a policy that is aimed to transition an unjust situation to a comparatively more just one, by mandating three requirements, namely: (I) "politically possible", (II) "morally permissible" and (III) "likely to be effective" (Rawls, 1999, p. 89; Simmons, 2010). If a policy meets these criteria, the likelihood that it will lead towards perfect justice is significantly higher opposed to a policy that doesn't meet those criteria. Therefore, nonideal theory will be applied to the G7 tax deal to assess its potential of transforming the unjust current international tax system into a comparatively more just one.

(I) Politically possible

Before the G7 tax deal gets implemented, it needs support from politicians. Without political support, the chances of transforming the current international tax system by the means of the G7 tax deal will become neglectable. In this particular case, this means that the G7 tax deal needs support from both politicians domestically and internationally. Therefore, it seems questionable that such a deal will enjoy global support, especially as there are numerous nations involved that have differing interests (ITR, 2021). Things are even more complicated as the G7 tax deal entails two pillars that could each create controversy. Therefore, I'll separately discuss both pillars and the likelihood of receiving political support.

The first pillar will probably face the most resistance as a lot of nations use their tax regimes to attract FDI and foster economic development (Reuters, 2021d; Reuters, 2021e; ITR, 2021). Additionally, setting up a global minimum corporate tax rate endangers national fiscal sovereignty by restricting fiscal policy options (Rixen & Dietsch, 2015). This restriction of national fiscal sovereignty endangers the benevolence of nations to agree upon such a proposal (ITR, 2021). The second pillar will probably face comparatively less resistance as most nations tend to agree that the largest and wealthiest MNEs should be taxed proportionally. Also, governments' tax bases increase due to the second pillar without sacrificing national fiscal sovereignty, and therefore increasing the chances of receiving support (The Guardian, 2021b).

Since, there are many nations involved with differing agendas, the chances that the current G7 tax deal will receive global support are questionable[33] (ITR, 2021; Reuters, 2021d). However, if the G7 is willing to negotiate and form exemptions, the chances of receiving global support will increase significantly. This is extremely important as support from a nation like

[33] Although chances are questionable due to the many different agendas and conflicts of interest. The G7 nations are influential and consensus among them mostly leads to consensus among the G20 nations (Sarson, 2021).

China is a requirement for the agreement to succeed (ITR, 2021). If the G20 is on board, pressure on domestic politicians will increase to support the G7 tax deal. This is also important as in certain G7 nations domestic politicians do not yet or to a lesser degree support the G7 tax deal. The United States for instance has a senate that is republican whereas the president and its administration are democratic (Reuters, 2021c). With the support of the global elite, the Biden administration is more likely to successfully guide the tax deal through the senate.

(II) Morally permissible

Since the normative assessment concluded the current international tax system to be unjust, it is worthwhile to assess the ethical aspects of the G7 tax deal. This as the new policy needs to be comparatively more just than the former. However, multiple NGOs already expressed their concerns regarding the G7 tax deal (Reuters, 2021f; BBC, 2021). These concerns are formed due to the redistribution structure of the extra revenue generated by levying additional taxes. This as the G7 tax deal entitles the home countries of the MNEs, to have the largest share of the additional tax revenue (Reuters, 2021f; Reuters, 2021b). These home countries are mostly the United States or members of the EU, which leaves a small part of the additional tax revenue for developing countries in which MNEs are also embedded (Reuters, 2021f). NGOs and campaigners argue this to be unfair as smaller and developing countries are pressured by the rich and powerful G7 nations to support their tax deal, while it's certainly not in their best interest. Especially as these smaller and developing countries can't afford to isolate themselves from the G7 nations. The ramifications of this G7 tax deal also entail "a massive money transfer to rich countries" as a spokesperson of Oxfam stated (Reuters, 2021f). Therefore, the critique "that it is unfair of the G7 nations to determine a global minimum tax rate" as expressed by NGOs, campaigners, and less powerful poorer nations seems to be justified, especially when applying the principles of justice (Reuters, 2021b).

When normatively assessing the fairness of the G7 tax deal by Rawls' theory of justice, it's important to remember that the principles of justice only apply to domestic justice[34] (Rawls, 1999; Simmons, 2010). Therefore, it's only possible to assess what effects the G7 tax deal would have on the domestic justice of separate nations. It is thus not suited to assess international justice by comparing the effects on the domestic justice of several nations. The effects of the G7 tax deal on domestic justice differs for certain nations and should thus be scrutinized as individual cases.

[34] The same line of reasoning that is used in chapter three is applied here to increase the comparability of normative assessment between the two alternative international tax systems on domestic justice.

For wealthy nations like the United States, this would mean that the government's tax bases increase at the expense of the wealthiest MNEs. In this case, no principles of justice would be violated and therefore *could* be regarded as a comparatively more just tax system. However, in poorer nations in which MNEs also are embedded, the ramifications would be different as they will receive less of the additional tax revenue due to the redistribution formula (Reuters, 2021f). Therefore, the MNEs will still be able to free ride on public goods and services in these countries. Furthermore, it could increase inequality as MNEs are now expected to pay more taxes to the governments of their home countries, leading to a government deficit in poorer countries that has to be compensated for with additional taxation on the least-advantaged (WorldFinance, 2015). In these countries, the G7 tax deal will violate all principles of justice and *could* lead to a comparatively less just tax system.

Another ethical issue arises as the G7 tax deal could hit MNEs unevenly and therefore violate the principles of fair competition as established by the IBE (IBE, 2018). An example of the uneven impact of the G7 tax deal could be illustrated by the tax increase of respectively Google and Johnson & Johnson. When both pillars of the G7 tax deal would be applied, Google's tax expenses would increase by less than $600 million, which is only 7% more than its global tax bill in 2020 (Reuters, 2021g). Whereas Johnson & Johnson its tax expenses would increase by $1 billion, causing a more than 50% rise of its global tax bill in 2020 (Reuters, 2021g). The differing impact of the G7 tax deal has to do with the income of MNEs that is reallocated and the countries its located in. This most likely will result in practices from MNEs that are aimed to reduce the amount of reallocated income to stay competitive that is comparable to tax avoidance nowadays.

(III) Likely to be effective

A G7 tax deal can sound promising and historical, however, its success mainly depends on its effectiveness. The leaders of the G7 have full confidence that their tax deal is going to be effective as it allows them to collect underpaid taxes of MNEs that operate in countries that apply lower tax rates than the globally minimum tax rate of 15% (The Guardian, 2021b; Reuters; 2021b). This also implies that not every country needs to support and comply with the G7 tax deal for it to be effective, thus increasing the chances of effectiveness.

However, it would be peculiar if the G7 leaders themselves wouldn't be enthusiastic about their tax deal that could potentially benefit them tremendously. In practice, the effectiveness of the G7 tax deal will probably depend on the details as many experts emphasize (Reuters, 2021b; Reuters, 2021g; Reuters, 2021d). Especially, as it is likely that MNEs and

their accountants will come up with a whole new suite of tax avoidance schemes. Setting up a global minimum corporate tax rate of 15% sounds like a solution to get rid of 0% tax-havens. However, most subsidiaries that are located in those tax havens are part of complex and sophisticated jurisdictional arbitrage schemes that not only are established there because of a 0% corporate income tax rate (The Conversation, 2021). Therefore, it is difficult to tell how this tax deal for instance will affect the "Double Irish with a Dutch sandwich" tax scheme or Amazon's sophisticated ways of dealing with financial instruments that enable them to modify every aspect of their acquired profits (The Conversation, 2021).

As mentioned earlier, Amazon's reported profit margin in 2020 was only 6.3%, which excludes them from the second pillar and would enable them to dodge additional taxes (The Guardian, 2021b). It is therefore likely that other MNEs will also try to lower their profit margins and thus dodge additional taxation. Especially as additional taxation could have huge ramifications for their tax bills and competitiveness as shown by the Google and Johnson & Johnson example earlier (Reuters, 2021g). It is also imaginable that the largest MNEs will 'break up' into technically independent corporations that act as an alliance to ensure that the whole operation doesn't meet the requirements of additional taxation (The Conversation, 2021). Practices like this already occurred earlier in the form of 'shadow banking' when independent companies acted like banks and worked together to avoid the need for a banking license (IMF, 2018).

Due to the history of MNE's tax avoidance behaviour it's hard to imagine that they will fully comply with the spirit of the law. Therefore, the details of the G7 tax deal will be crucial for its effectiveness as it is more than likely that MNEs will push the boundaries to minimize their tax liability. Since it's extremely challenging to establish a 'waterproof' global taxation system that doesn't include loopholes, inconsistencies, or information asymmetries it's more than likely that new tax avoidance schemes will arise, and therefore endangering its effectiveness (Scarpa & Signori, 2020).

4.4. Conclusion

In its current form without exemptions, the chances that the G7 tax deal will receive global support are questionable, and will all depend on the G20 summit in October (Reuters, 2021b; ITR, 2021). In wealthy nations. this G7 tax deal could transform the unjust international tax system into a comparatively more just one if, ceteris paribus, it mitigates inequality and free riding on public goods. However, in developing nations, the G7 tax deal could transform the unjust international tax system into a comparatively less just one if, ceteris paribus, it increases

inequality and free riding on public goods. Therefore, its effect on justice is ambiguous and differs per nation. Its effectiveness will depend on the details of the G7 tax deal and to what extent it's 'waterproof', as it's unlikely that MNEs out of a sudden will act to the spirit of the law (Reuters, 2021b; Reuters, 2021g; Reuters, 2021d). Therefore, its potential to transform the unjust international tax system into a comparatively more just one all depends on the exemptions, details, and the nation of interest. Therefore, the G7 tax deal could be promising but as none of the three requirements are completely convincingly addressed, its potential remains questionable. Chances could increase when exemptions are formed, however, these exemptions could simultaneously decrease their effectiveness (Reuters, 2021d; ITR, 2021). Despite the concerns regarding its potential, it's a positive sign that for the first time in decades there is global collaboration in targeting tax avoidance. In the next chapter, an alternative to the current international tax system will be provided, which I believe to have a higher potential of transforming the unjust tax system into a comparatively more just one.

5. Global Tax Authority & Unitary Taxation with Formula Appointment

Tax avoidance and the current international tax system are normatively assessed as unjust. An attempt by the G7 leaders to transform the unjust international tax system into a comparatively more just one is a historic event, however, its potential remains questionable (The Guardian, 2021b). Therefore, I'll provide an alternative system that could be better suited for the task. It's important to emphasize that the proposed alternative system does not need to be the best option in theory, and there could even be better alternatives. However, it's an example that illustrates that a comparatively more just tax system is possible and not a utopia. It does so, by the means of ceteris paribus reasoning, meaning: that if the proposed alternative system mitigates inequality, free riding on public goods and services, and the undermining of competition, ceteris paribus, it's comparatively more just and should thus be implemented. Furthermore, it is assumed that MNEs will maximize shareholder value and thus try to reduce their tax liability as much as legally required. This can be classified as unjust but is made possible by the unjust current international tax system (Rixen, 2016). Therefore, the proposed alternative tax system aims to change 'the rules of the game' instead of 'the behaviour of its players'.

The proposed alternative system is called "unitary taxation with formula appointment" and requires the establishment of a global tax authority (Rixen 2008; Rixen, 2016; Weinzierl, 2018). Therefore, first, the establishment of a Global Tax Authority (GTA) will be discussed, and second, the application of unitary taxation with formula appointment. At last, nonideal theory will be applied to assess its potential and how this may lead to updated principles of international taxation.

5.1. Establishment of a Global Tax Authority

It's important to recall that globalization didn't lead to the establishment of a global political tax institution. This is extremely problematic as capital can cross national borders with ease due to its enhanced mobility, while the power to tax is bounded by these national borders (Rixen, 2008). Therefore, it's of great importance to establish a GTA that coordinates international tax policy and closes information asymmetries between countries and can settle disputes[35]

[35] Establishing a GTA also serves as a solution for a moral difficulty associated with Rawls' theory of justice (Cappelen, 2001). Cappelen (2001) argues that Rawls' theory rises issues regarding countries' 'right to tax'. However, the issues Cappelen (2001) mentions will be solved when a GTA is established, as this GTA can act as an independent organization that could settle disputes consequently between countries that face conflicts over the taxable presence of MNEs (Pogge & Mehta, 2016).

(Weinzierl, 2018). Countries that incorporate the GTA should transfer the part of their tax bases that represent the income from MNEs located in that country to the GTA. Due to the country-by-country (CBC) reporting, MNEs need to report their profits and incomes both in aggregate and broken out for each country in which they are located. The GTA should share this information among all members to ensure that tax administration is more effective and affordable (Weinzierl, 2018). By doing this the GTA will be able to tax the aggregate of MNEs' profits over all jurisdictions, this is called unitary taxation (Rixen, 2008; Weinzierl, 2018). By unitary taxing MNEs there is no incentive for them to shift profits to lower tax jurisdictions or tax havens since their global income and profits will be taxed and, therefore, are not able to exploit the source and arm's length principle. Furthermore, it also addresses the tax competition between countries as MNEs will not be able to retain tax savings (Weinzierl, 2018; Rixen, 2008). This as countries will no longer be constrained by the tax rates others impose, as tax avoidance now gets addressed collectively (Gillian, 2008). This also implies that the capability of developing countries to collect domestic taxes now significantly increases, as these countries are not always able to collect all the taxes they are owed (especially taxes from MNEs) (Pogge & Mehta, 2016). The collection of the owed taxes could help developing countries to systemically address problems they face, such as poverty, underdeveloped healthcare, and education (Gillian, 2008).

To clarify the above, I'll return to the imaginary LTC example as used before. In the current international tax system, LTC reported small profits in the United States and huge profits in the Cayman Islands, resulting in a low tax burden for LTC. However, when unitary taxation would be applied, all countries in which LTC is located need to report the profits of LTC and its subsidiaries to the GTA, which in turn establishes a common consolidated tax base for LTC that represents their global profits and income.

5.2. Unitary Taxation with Formula Appointment

Now a GTA is established the requirements are met to successfully implement unitary taxation with formula appointment. As shortly explained above, unitary taxation treats an MNE as a single company that operates in multiple countries, instead of separate companies operating internationally. When treated as a single company, their profits can be pooled together and distributed among the countries in which the MNE operates (Weinzierl, 2018; Zucman, 2015). This distribution will be done based on a formula that represents real economic activity.

The exact form of the redistributive formula is open for debate and probably needs a couple of iterations before reaching a just and desirable consensus (Zucman, 2015). However,

the underlying idea for this formula would be that MNEs are taxed based on economic presence. Variables that could proxy for economic presence and could in combination be included in the formula are production, sales, payrolls, and assets located in each country (Rixen, 2008; Weinzierl, 2018; Zucman, 2015). Furthermore, the number of factories and shops in a country could proxy for the production and distribution activities of an MNE. However, proxies for intellectual property rights are somewhat less obvious. Therefore, Zucman (2015) suggests looking at R&D activities and assess where and how value is added. Meaning, that if an MNE makes profit by collecting payments for the use of its patents or royalties, the taxations of these profits should take place in the country in which these are developed, instead of being held (Zucman, 2015; Weinzierl, 2018; Rixen, 2008; Van Dijck, 2016).

In the current international tax system, the only requirement to benefit from a highly favourable tax regime is being legally present, which allows the existence of shell companies. Formulary appointment based on real economic activity enables the GTA to redistribute tax revenue among the countries in which real economic activity takes place and end the viability of shell companies. This satisfies the commonly held belief that profits should be taxed where they are created and mitigates free riding on public goods and services.

To clarify how the whole system of unitary taxation with formula appointment will work, I'll again use the example of the imaginary LTC MNE. Imagine that LTC has its headquarters in the United States and has subsidiaries in Mexico, the Cayman Islands, and Ireland. The production and sales mostly take place in the United States and Mexico, whereas the subsidiaries in the Cayman Islands, and Ireland are mainly established to benefit from their highly favourable tax regimes. In the current international tax system, LTC would report its profits in the Cayman Islands and Ireland because of their tax regimes which only require legal presence. However, if applying unitary taxation with formula appointment, the GTA would first establish a common consolidated tax base of LTC' profits globally on a CBC basis. Accordingly, it will distribute these profits regarding the economic activity. This would mean that the United States and Mexico would receive most of the tax revenue, and the Cayman Islands and Ireland receive only a small part. This as the production, distribution, and R&D department are all located in the United States and Mexico, that represents high economic presence. However, if LTC wouldn't like the applied tax rates in the United States and Mexico, and would prefer to benefit from the highly favourable tax regimes in the Cayman Islands or Ireland, it needs to move most of its production, distribution, and R&D departments to these countries. Especially in the case of the Cayman Islands, this would be problematic as this is a small country with a small population. This small population also means a small qualified and

suitable employee pool and a very limited market to sell its cars. This will probably hold LTC back from moving its operations from the United States and Mexico to the Cayman Islands. Therefore, the real economic activity remains in the United States and Mexico and grants them the major share of LTC' profits. Important to emphasize is the fact that this alternative system doesn't violate the national fiscal sovereignty of countries as they are still able to levy tax rates that they see fit. The United States and Mexico can now use this tax revenue for the provision of their public goods and services. In the current international tax system, LTC extensively used the public goods and services in these countries without paying their fair share for it. However, this injustice is solved due to unitary taxation with formulary appointment.

5.3. Unitary Taxation with Formula Appointment and Nonideal Theory

In this section, I apply nonideal theory to unitary taxation with formula appointment, to assess its potential of transforming the unjust current international tax system into a comparatively more just one. The same criteria for assessment will be used as in the G7 tax deal case.

(I) Politically possible

A requirement for unitary taxation with formula appointment to be successful is the establishment of a GTA (Weinzierl, 2018; Rixen, 2008; Pogge & Mehta, 2016). As proved by the G7 tax deal, there is consensus between some of the economically most powerful nations that tax avoidance needs to be addressed, which increases the chances of successfully establishing a GTA. If the G7 nations indeed support the establishment and incorporation of a GTA, lots of countries will most likely follow. Especially, if the United States and Europe incorporate the GTA, economic pressure for incorporation rises in other smaller countries and tax havens[36]. These smaller countries depend heavily on foreign markets, which should make it easy to get them on board once the powerful and big economies on which they rely incorporate the GTA (Zucman, 2015).

The G7 tax deal mainly faces political opposition due to the concerns that countries will lose their national fiscal sovereignty and, therefore, cannot levy tax rates as they see fit (Rixen & Dietsch, 2015; Reuters, 2021d; Reuters, 2021e; ITR, 2021). However, this argument does not apply to unitary taxation with formulary appointment, as countries will retain their national

[36] The incentive for the smaller countries to follow the US or Europe could differ for each of them. However, they all have one thing in common; they depend in one way or another on the relationship with those economic superpowers. Examples of their dependence could be trade, foreign aid, or military support. Therefore, obstructing the agendas of these economic superpowers, and possibly deteriorating their relationship, could be more detrimental for them than receiving less tax revenue (Zucman, 2015).

fiscal sovereignty (Zucman, 2015). Countries will still be able to levy the tax rate of their choice. However, one might argue, that transferring a part of their tax bases to the GTA is also a violation of the national fiscal sovereignty. Although this is true to a certain extent, it still is a minor sacrifice that enables countries to regain control over tax policies (Rixen, 2016). It is especially a minor sacrifice when comparing it to the G7 tax deal that completely violates national fiscal sovereignty. Furthermore, it also puts an end to tax competition and enables governments to levy the tax rate they see fit without having them fear an outflow of capital. This as MNEs also have to move their economic activity as already explained in the LTC example before. Due to these benefits and only violating national fiscal sovereignty to a small extent, the political chances of successful implementation are relatively high.

History proves that unitary taxation with formula appointment is politically possible and a viable solution for tax competition. Since the 19th century, the United States and Canada both use unitary taxation with formula appointment to coordinate interstate tax policy (Weinzierl, 2018). Both countries faced heavy interstate tax competition that eroded their tax bases (Zucman, 2015). When unitary taxation with formula appointment was implemented, they pooled the nationwide tax bases and distributed it among the states by the use of a formula. These states in turn decided for themselves what tax rates they saw fit, which led to the end of the tax competition and eroded tax bases (Weinzierl, 2018; Zucman, 2015). Of course, would global implementation be more challenging than national, however, with the support of the G7 the chances of succeeding would certainly be high. Especially as gaining support from other countries is easier when they don't have to give up on their national fiscal sovereignty.

However, the establishment of a GTA would probably take a considerable time, and it would therefore be an option to update the principles of international taxation to bridge the gap. A good start would be to add a fourth principle that treats MNEs as a single company instead of multiple separate companies. This fourth principle would form a solid basis for a transition period that prevents further violation of the arm's length principles by MNEs.

(II) Ethically permissible

As mentioned earlier, when unitary taxation with formula appointment gets implemented, MNEs don't have an incentive anymore to shift their profits to lower tax jurisdictions (Rixen, 2008). This mitigates free riding on public goods and services, and ends tax competition between countries (Zucman, 2015). Therefore, unitary taxation with formula appointment reduces MNEs' ability to shift profits, and thus mitigates the violation of the principle of equal

opportunity and is thus comparatively more just than the current international tax system (Rawls, 1999).

Another advantage of restricting MNEs from shifting their profits to low tax jurisdictions is fairer competition. Especially as unitary taxation requires MNEs to report profits in aggregate and on a CBC basis (Weinzierl, 2018). This will benefit the fairness of competition as now 'all players of the game' carry a relatively even tax burden. This makes unitary taxation with formula appointment comparatively more just than the current international tax system as it doesn't undermine the principles of fair competition (IBE, 2018; OECD, 2009b).

Besides the mitigation of free riding on public goods and services and the undermining of competition, unitary taxation with formulary appointment also allows countries to implement progressive tax systems. This as countries still have their national fiscal sovereignty and therefore can levy the tax rates they see fit (Weinzierl, 2018). Due to this and the requirement of real economic activity, countries don't have to fear a capital outflow when determining their tax rates. Especially as tax rates in this alternative tax system are not a major driver to attract capital. Of course, tax rates are still a driver to attract capital, as if a country would levy a tax rate of 60% or above, MNEs will still benefit by moving abroad. However, the extent to which tax rates can attract capital or FDI is now greatly restricted (Atkinson, 2015). Therefore, countries are now able to tax progressively[37]. This also implies that those that were previously burdened with increased taxes to compensate for lost tax revenue due to tax avoidance by MNEs, now have to pay less. Therefore, inequality will be mitigated as now those most wealthy and advantaged in society pay relatively more taxes instead of the least-advantaged (Rixen, 2016). Due to the mitigation of inequality, unitary taxation with formula appointment is comparatively more just than the current international tax system.

(III) Likely to be effective

When assessing an alternative tax system, it's of great importance to assess its effectiveness, as a system that is politically possible and morally permissible but not effective will not transform an unjust tax system into a comparatively more just one. Unitary taxation with

[37] Reasoning exists that higher taxes could undermine the incentives to innovate, and since innovation is an important contributor to long-term economic growth this could be harmful. However, in a study by Akcigit et al., (2021) it is concluded that higher taxes can negatively impact the quantity and the location of innovation but not the average quality of innovation. Therefore, higher taxation could indeed undermine the incentive to innovate but since the quality of average innovation remains unaffected this doesn't need to be a bad thing. Therefore, it depends on one's preferences and interests whet ether the possible undermining of the quantity and location of innovation is more important than the benefits progressive taxation could realize.

formula appointment has advantages that make it likely to be effective in mitigating tax avoidance by MNEs (Weinzierl, 2015; Rixen, 2016).

Unitary taxation with formula appointment doesn't require an arbitrarily chosen threshold value that indicates which MNEs should be taxed additionally (Weinzierl, 2018; Zucman, 2015). This makes it universally applicable and as clear as possible for the GTA to tax MNEs. In the case of the G7 tax deal, there are arbitrarily chosen threshold values such as the 10% global profit margin that endanger the effectiveness of the system. As explained does this requirement exclude Amazon from additional taxation, and is it more than likely that other MNEs will engage in ambiguous tax practices to report lower global profit margins to be excluded from additional taxation (The Guardian, 2021b). However, unitary taxation with formula appointment doesn't involve any arbitrarily chosen threshold value which makes it significantly harder for MNEs to 'game' the system (Zucman, 2015).

As unitary taxation with formula appointment requires MNEs to have a real economic presence they can't just shift their profits to lower tax jurisdictions or tax havens as now they have to pay taxes in the countries in which they generate profits (Weinzierl, 2018). As most of these lower tax jurisdictions and tax havens are small countries that don't provide the essentials for MNEs' real economic activities, MNEs will not move their departments and thus have to pay taxes in the country in which it makes profits (Zucman, 2015). The removal of incentives for MNEs to shift profits is expected to be extremely effective in restricting its tax avoidance behaviour, and therefore increases the chances of successfully transforming the unjust current international tax system into a comparatively more just one (Pogge & Mehta, 2016).

5.4. Conclusion

Unitary taxation with formula appointment could be a promising international tax system that is comparatively more just than the current international tax system. This mitigates free riding on public goods and services, inequality, and the undermining of fair competition. However, despite that it is comparatively more just than the current international tax system, it doesn't mean that it's the best system. This example is only used to illustrate that there exist realistic alternatives for the current international tax system that could be of help to achieve a more just and ideal world.

6. Conclusion and Discussion

6.1. Conclusion

This thesis provides a comprehensive overview of the justness and fairness of the ramifications of tax avoidance by MNEs that can be attributed to the current international tax system. It did this by first elaborating on the globalization of the world economy and outlining what ramifications this has on international corporate taxation. Due to globalization, the mobility of capital is highly increased and could therefore cross national borders with ease. However, nations' capabilities to tax are restricted by those national borders (Rixen, 2008). This limited capability in combination with the outdated 'source' and 'arm's length' principle creates opportunities for MNEs to avoid taxes due to their global presence and the high mobility of capital. The artificial shifting of profits is one of the most common schemes MNEs use to exploit loopholes in the current international tax system to avoid taxes (Zucman, 2014). The ramifications of tax avoidance are the undermining of fair competition, erosion of governments' tax bases, the increase of inequality, and the facilitation of free riding on public goods and services.

After descriptively approaching tax avoidance and its ramifications, a normative assessment was necessary as tax avoidance is a legal activity. Therefore, the crux of the issue is based on the (perceived)[38] fairness. The underlying idea is that every actor in society should pay their fair share of tax. This fair share of tax could thus be more than legally required (Payne & Raiborn, 2018). Therefore, ideal theory is used as an endpoint to determine how a just and fair society should look like (Simmons, 2010). Subsequently, the current international tax system and the ramifications of tax avoidance are assessed as unjust due to them violating all the principles of justice (Rawls, 1999). This is due to the current international tax system facilitating the undermining of fair competition and free riding on public goods and services, the erosion of governments' tax bases, and the increase of inequality. This conclusion subsequently formed the foundation for the claim that an alternative international tax system is more just, if ceteris paribus, it mitigates these ramifications of tax avoidance.

Now the current international tax system was classified as unjust, nonideal theory was used to deal with the noncompliance to the principles of justice to ultimately achieve a just and ideal world (Simmons, 2010; Stemplowska & Swift, 2012). This nonideal theory is applied to

[38] Fairness and its perception can differ for individuals depending on what ethical theory those individuals support (Rawls, 1958).

two alternative taxation systems to assess their potential of succeeding. The newly proposed 'G7 tax deal' could be promising depending on the exemptions and details of the deal, as these could increase the effectiveness and the chance of global political acceptance. However, in terms of justice and fairness, the G7 tax deal could yield both a comparatively more just and less just tax system than the current one. Therefore, its potential remains questionable as none of the three criteria provided by nonideal theory gets convincingly addressed.

At last, unitary taxation with formula appointment is normatively assessed based on the same requirements as the 'G7 tax deal'. This assessment concluded that the potential of achieving a more just society is higher when implementing unitary taxation with formulary appointment. This mitigates the undermining of fair competition, the free riding on public goods and services, the increase in inequality, and the erosion of governments' tax bases and is thus, ceteris paribus, comparatively more just. This conclusion is formed as unitary taxation with formulary appointment most convincingly addresses all three requirements of nonideal theory. Therefore, the research question can be answered by globally implementing unitary taxation with formulary appointment. The 'G7 tax deal' has shown that there exists shared sentiment among politicians that tax avoidance needs to be tackled, this increases the chances of successful implementation if these politicians would collaborate on globally implementing unitary taxation with formulary appointment. Since institutions are social constructions that are created by humans, this also means they can be changed if needed. Therefore, it seems obvious that if we can change the current international tax system into a more just one then, ceteris paribus, we should do so (Pogge, 1992). I do believe that unitary taxation with formulary appointment in terms of social justice is the best alternative I've come across. However, I also do believe that the G7 tax deal could be promising if the details and exemptions don't hamper its effectiveness. Despite that both alternatives are promising, I do believe that there are far more alternatives to be explored that are potentially comparatively more just than the current international tax system.

6.2. Discussion

This thesis contributes to the current academic literature due to its 'setup', the subject of analysis, and the further exploration of mentioned recommendations from previous studies (Scarpa & Signori, 2020; Rixen, 2008; Pogge & Mehta, 2016; Zucman, 2015; Van Dijck, 2016). Furthermore, it provides additional reasoning and substantiation, by the means of ethics, to claims made in the current literature to opt for an alternative international tax system (Pogge & Mehta, 2016; Cappelen, 2001; Zucman, 2015; Gillian, 2008).

It does this by normatively assessing three[39] different international taxation systems[40] from a comparative stance. By applying the same criteria of Rawls' (1999) ideal and nonideal theory[41] to the three different international taxation systems, depth has been added to the initial exploration of the fairness of the current international tax system (Scarpa & Signori, 2020; West, 2018; Van Dijck, 2016). Furthermore, it takes four different[42] socioeconomic ramifications on domestic justice in account, which is quite comprehensive when comparing it to the existing literature[43] (Sayegh, 2016; Van Dijck, 2016). The usefulness of ideal and nonideal theory has often been criticised for being "too theoretical" and not having any "practical implications" (Sen, 2006, p. 217). However, this thesis explored the application of ideal and nonideal theory to the contemporary problem of tax avoidance by MNEs. It proved that ideal and nonideal theory can be of use when trying to improve justice in the 'real' world, therefore, contradicting claims made by Sen (2006). This is important as there is extensive literature reporting on possible alternative taxation systems and their benefits, however, this literature often lacks additional ethical substantiation that could strengthen made claims (Rixen, 2008; Zucman, 2015). Furthermore, it comes to the positive conclusion that political ethics and philosophy can yield concrete positive normative policy recommendations for real-world issues.

This thesis also further explores a recommendation for future research as mentioned in a very comprehensive recent systematic literature study by Scarpa & Signori (2020). It does so by normatively assessing the G7 tax deal while including stakeholders' perspectives and therefore addressing compelling issues on stakeholders' agendas. This stakeholder approach is currently quite underexplored and could when convincingly addressed add significant value to the academic debate (Scarpa & Signori, 2020).

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[39] I couldn't find any other literature that compared three alternative taxation systems using the same normative framework.

[40] Including the newly proposed G7 tax deal. This newly proposed alternative taxation system has not been subjected to a (comparative) normative assessment (at least to the best of my knowledge) in the current academic literature, which increases the relevance of this thesis by providing a state-of-the-art analysis.

[41] So far, there is extensive literature reporting on unitary taxation with formulary appointment, however, none of this literature applies nonideal theory to this alternative to assess its potential of succeeding. To assess the potential of succeeding by using a normative framework is fundamentally different from opting for an alternative taxation system based on, for instance; its potential to close information asymmetries. This approach strengthens the claims made in these studies by providing additional ethical substantiation (Pogge & Mehta, 2016; Rixen, 2008; Rixen & Dietsch 2015; Zucman, 2015).

[42] This analysis also includes the ramifications of tax avoidance on 'the fairness of competition'. This aspect gets often overlooked in normative analyses and deserves more attention in my opinion.

[43] These studies only take two socioeconomic ramifications in account and only assess the current international tax system, these studies note in the 'recommendations for future research' section that broadening the scope could strengthen the claims made in their studies. Therefore, this thesis expends the initial exploration of previous studies.

However, I do acknowledge that this thesis has some limitations that could influence found results and formed conclusions. Some of these limitations, however, are the result of the limited confines inherent to writing a master's thesis. Therefore, some of the limitations will also form the foundation for my recommendations for future research.

First of all, the normative assessment is mainly based on ideal and nonideal theory from Rawls' theory of justice. Although in the overview of the current ethical debate some other theories get shortly mentioned, it doesn't represent a profound assessment. Therefore, the conclusion, that the current international tax system is unjust, is for the most part only based on one theory of justice. Therefore, it could be possible that when one applies another theory of justice to the issue of tax avoidance one can come to completely different conclusions. There exist numerous theories of justice and therefore the results of this thesis could get undermined if a significant portion of them would conclude that tax avoidance is just. However, including a profound assessment of multiple theories of justice wasn't possible due to the limited time and the confines of this thesis. Therefore, future research could broaden the normative assessment of tax avoidance and the international tax system by applying other theories of justice. This could either strengthen or undermine the found results of this thesis.

Second, this thesis heavily relies on ceteris paribus reasoning. Meaning that it only takes the following ramifications of tax avoidance into account: the undermining of competition, an increase of inequality, erosion of governments' tax bases, and free riding on public goods and services. Therefore, when I compared the three international taxation systems, I assumed that all other variables would remain the same. However, it could be possible that when unitary taxation with formulary appointment gets implemented, this harms other socioeconomic factors that due to the ceteris paribus reasoning were assumed to be equal. These other socioeconomic factors could each endanger justice and could in theory even cause severe injustices that make unitary taxation with formulary appointment comparatively less just. Thus, stating that unitary taxation with formula appointment is a more just tax system heavily relies on the assumption that all other socioeconomic factors remain the same. Therefore, a more comprehensive and in-depth exploration of both alternative international taxation systems and their ramifications should be pursued to more convincingly claim that unitary taxation with formulary appointment is a more just system than the current international tax system. Despite it could be argued that including and taking into account all relevant variables is nearly impossible, and therefore ceteris paribus reasoning can't be avoided, it still is without a doubt limiting the relevance of the found results. Therefore, future research could focus on including more relevant

socioeconomic factors for normative assessment to increase the relevance and practical implications.

At last, the normative assessment of the two alternative international taxation systems is in comparison with the normative assessment of the current international taxation system relatively superficial. A more profound normative assessment of both systems would increase their credibility and legitimacy. However, the confines of this thesis limited the profoundness of the normative assessment for both these systems and thus only allowed an initial exploration. Therefore, future research could focus on a more profound normative assessment as this will increase the strength of opting for an alternative international taxation system.

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