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The Human Rights Implications of Corporate Tax Avoidance

by Paul George

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In this article, the author considers the human rights implications of tax avoidance, looking at the responsibilities of countries and multinational enterprises using the framework laid out in the United Nations' Guiding Principles on Business and Human Rights.

Sustainable development can only happen when national economies are strong. Fair tax is at the heart of this equation. It requires multinational companies to turn away from tax schemes and tax havens, treating their tax obligations as part of the "corporate social responsibility" that they are so keen to advertise.

— Richard Brooks, *The Guardian*[1]

Taxes provide governments with the most sustainable source of revenue to help them fulfil their primary duty of ensuring the realization of an array of human rights for their citizens. Taxation also plays an essential role in redistributing resources in ways that can preclude and remedy gender, economic, and other inequalities, thus reducing disparities in the enjoyment of human rights that flow from these characteristics.[2] Yet despite their fundamental importance in a civilized society, issues involving taxation are rarely featured in United Nations human rights declarations. Unjust tax systems, on both the national and global level, too often promote rising inequality in human rights enjoyment, shifting the tax burden onto society's most destitute and concentrating wealth in the hands of the well-off few.

The governments of developing countries urgently need to increase their tax bases so that essential public services are available for all. These essential services are the keys to tackling poverty and promoting a more efficient allocation of resources that will inhibit human rights abuses from the start. Yes, the taxes imposed on multinational enterprises that maintain operations in developing countries provide significant contributions to those countries' treasuries to help support public services. However, prevalent corporate tax avoidance — facilitated by complex business structures and offshore tax havens — has denied these countries over $160 billion in tax revenue per year.[3] The consequences of losing this revenue usually include imposing higher taxes on lower-income households and impeding savings and wealth accumulation. In the absence of higher taxes, public spending must fall.

Tax avoidance and the use of tax havens have become commonplace for today's MNEs. In recent years, however, these practices have come under heavy scrutiny and garnered considerable media attention worldwide. Not only do these selfish and greedy practices foster human rights abuses, but they are also detrimental to corporations and their shareholders when they tarnish corporate reputations and constrain product placement

[1] Richard Brooks, "Tax and Aid: To Trade With Loaded Dice," *The Guardian*, Nov. 29, 2010.

[2] *See* Lima Declaration on Tax Justice and Human Rights (June 2015).

[3] Rachel Noble, "Taxing Human Rights?" Institute for Human Rights and Business (May 1, 2013).

opportunities. There are a few mechanisms that can deal effectively with these corporate tax abuses, including the United Nations' Guiding Principles on Business and Human Rights,[4] which will be discussed in detail throughout this article.

The three foundational principles of the U.N. guiding principles provide a crucial analytical framework for investigating the human rights implications of corporate tax avoidance. Applying the first principle — the state's duty to protect human rights — requires revisiting the obligation of the state to maximize and efficiently allocate resources to achieve social, economic, and cultural coherence. The only way that states can truly attain this goal is by addressing the fiscal and tax measures that divert funding from national infrastructures and distort the allocation of wealth in societies. The second principle — corporate responsibility to protect human rights — can be addressed once business enterprises, as well as financial advisers and tax attorneys, recognize that their tax planning strategies are negatively affecting human rights and appreciate the need to conduct extensive human rights due diligence before launching any new project. The third and final principle — access to remedy — can be strengthened once states and businesses join the U.N.'s effort to ensure greater access to effective remedies for those negatively affected by corporate tax avoidance practices.[5] Developing transparency and increasing the nonfinancial disclosures about MNEs' operations on a country-by-country basis will provide those crucial first steps in tackling this issue.

The U.N. Human Rights Council's endorsement of the guiding principles is an important step in the right direction. There is an increasing acceptance of the once-disputed idea that companies have human rights obligations, and an assortment of legal and policy measures are being employed to ensure that corporations respect human rights. Yet, as alluded to earlier, the link between human rights abuses and corporate tax avoidance has not been at the forefront of the global discussion. Therefore, it is necessary to consider what a business-and-human-rights approach might add to the discussion of tax avoidance.

This article will view tax avoidance by multinational corporations through the lens of business and human rights. Section I discusses the mechanics of tax avoidance, using the example of the relationship between Apple and Ireland, including an examination of the particular harms caused by tax havens and the factors that lead MNEs to avoid taxes. Section II will focus on corporate social responsibility (CSR) and the limitations of using CSR to address corporate tax avoidance. Section III will highlight the human rights impact of tax avoidance and tax abuse in developing countries, as seen in SABMiller's egregious tax dodges in Ghana and other African regions. Section IV will look specifically at the application of the United Nations' Guiding Principles on Corporate Tax Avoidance. Finally, Section V evaluates solutions and provides recommendations for tackling the culture of corporate tax avoidance.

I. The Mechanics of Corporate Tax Avoidance

A. Tax Avoidance vs. Tax Evasion

Before diving into the underlying mechanics and strategies used in these sophisticated corporate tax avoidance schemes, we must first differentiate between tax avoidance and tax evasion. Tax avoidance generally refers to legally reducing tax payments whereas tax evasion refers to illegally reducing tax payments using methods like deception, concealment, or destruction of records. Tax avoidance practices, in contrast, generally seek to accomplish one of three objectives: payment of less tax than required by a reasonable interpretation of a country's law, payment of a tax on profits declared in a country other than where they were really earned, or a tax payment that occurs (unduly) later than the profits were earned.

U.S. courts have developed various tests to distinguish illegal tax evasion from legal tax avoidance activity. The most established precept

[4] *See* U.N., "Guiding Principles on Business and Human Rights: Implementing the United Nations 'Protect, Respect and Remedy' Framework," HR/PUB/11/04 (2011). This document, referred to herein as the U.N.'s Guiding Principles on Business and Human Rights or simply the U.N. guiding principles, originally appeared as an attachment to "Report of the Special Representative of the Secretary-General on the Issue of Human Rights and Transnational Corporations and Other Business Enterprises," A/HRC/17/31 (Mar. 21, 2011).

[5] Lloyd Lipsett, "Tax Abuse as a Business and Human Rights Issue," *Shift* (Oct. 2013).

is the "substance over form" test established in the landmark Supreme Court decision *Gregory v. Helvering*, 293 U.S. 465 (1935), which allows the legal form of a transaction to be disregarded in favor of recognizing its underlying economic substance.[6] Since that case, various courts have disallowed a tax benefit when a transaction's form differs from its substance. A classic example involves a debt versus equity characterization. An investor's contribution to a corporation could be viewed either as a loan (debt) to the business — in which case the corporation will generally take a deduction for interest it pays on the loan — or as an investment (equity) in the business. If the investor really has equity but the business labeled it debt, then the court will recharacterize the debt as equity for tax purposes.[7] This will, in effect, prevent the business from taking a deduction for the alleged interest payable on the debt.

Despite the limiting doctrines developed by the courts over time, corporations and their tax advisers have created clever, sophisticated schemes to exploit the gray areas of the tax code.

B. Methods of Avoidance

The present international taxation rules are out of touch with modern-day globalized business activity in that the rules allow companies to avoid paying taxes where the economic activity actually occurs.[8] According to the OECD, globalization has caused products and operational models to change and evolve, creating prime conditions for the development of international strategies that aim to maximize profits and minimize tax expense. Yet the rules on the taxation of profits stemming from cross-border activities remain the same — they have not adapted to the changes in business practices brought about by the globalization and digitalization of the economy. Thus, in the midst of economic globalization, international taxation rules have been relatively dormant and have not yet tamed these aggressive avoidance practices.

Transfer pricing is one of the main tools that companies use in these aggressive tax avoidance schemes. Globalization has been a catalyst for manipulative transfer pricing. With the help of financial service firms, transnational companies transfer company capital to group holding companies and report higher costs in countries with higher taxes and larger profits in low-tax jurisdictions, thus reducing the MNE's total tax liability. Transfer prices — cross-border payments between parts of the same MNE — are not subject to the same market forces that shape prices and relations between two independent companies. MNEs should use the arm's-length principle when pricing these transactions: The intragroup price should reflect the price that would be paid on the open market between unrelated parties. However, issues occur because MNEs can easily abuse the arm's-length principle by manipulating the value they assign to assets — especially intellectual property — when few comparative markers are available. For example, after selling its rights to market IP in the United States to its Microsoft Puerto Rico subsidiary, Microsoft U.S. immediately repurchased a portion of those rights, enabling Microsoft to save over $5 billion in taxes on products sold in the United States over a three-year span.[9] The International Bar Association reports that transfer pricing is among the most serious international tax abuses, concluding that mispricing accounts for 80 percent of illicit financial flows out of developing countries over the last decade for a total of around $4.7 trillion.[10]

Another way MNEs shift income from high-tax to low-tax jurisdictions is by offshoring intangible assets. A growing number of MNEs locate their algorithms, trademarks, and patents in tax havens to strip earnings away from countries, such as the United Kingdom and the United States, where they are actually generated. Discussed in the following section, one of the most spectacular and shameful cases of offshoring

[6] J. Bruce Donaldson, "When Substance-Over-Form Argument Is Available to the Taxpayer," 48 *Marq. L. Rev.* (1964), at 41, 45.

[7] Wei-Chih Chiang and Hui Di, "Debt or Equity Financing? Analyzing Relevant Factors," The Tax Advisor (June 1, 2010).

[8] Shane Darcy, "The Elephant in the Room: Corporate Tax Avoidance & Business and Human Rights," 2(1) *Bus. and Hum. Rts. J.* 1 (2017).

[9] Jasmine M. Fisher, "Note, Fairer Shores: Tax Havens, Tax Avoidance, and Corporate Social Responsibility," 94 *B.U. L. Rev.* 337 (2014).

[10] *See* International Bar Association, "Tax Abuses, Poverty and Human Rights" (2013).

IP to reroute income from high- to low-tax jurisdictions involves Apple.

C. Apple's Stateless and Tax-Less Subsidiaries

With the IRS's approval, Apple injected equity capital into a subsidiary incorporated in Ireland that otherwise had very little business activity. The subsidiary then used the capital to purchase a share in intangible assets that the U.S. parent developed using the human capital of its American employees. What Apple essentially did was to transfer the rights to its IP — including things like the patents for its iPhone technologies — to a subsidiary, Apple Operations, incorporated in Ireland. Although the subsidiary was not subject to immediate U.S. taxation, it was managed from California.

Apple engineered the complex transaction to allow the income earned by the subsidiary to be shifted outside Ireland, essentially allowing the subsidiary to become stateless — for tax purposes, it was located nowhere.[11] Instead of paying the ordinary Irish tax rate of 12.5 percent, Apple negotiated with the Irish government and received special corporate tax rate of 2 percent or less, and it did so while keeping its bank accounts and holding board meetings in California.[12] The Irish subsidiary maintained the rights to the company's patents and trademarks in Asia, Africa, and Europe, but not in North America or South America: Apple kept those rights in the United States. Because the United States bases residency on where the company is incorporated and Ireland focuses on where a company is managed and controlled, the structure of Apple Operations exploited both countries' rules. Overall, Apple's tax avoidance efforts shifted at least $74 billion out of the IRS's reach between 2009 and 2012.[13] As discussed later in this article, the European tax authorities eventually caught up to Apple.

Even though the United States taxes MNEs on foreign earnings, it was previously unlikely to tax the accumulated earnings of Apple's stateless subsidiaries. Before the 2017 tax reform legislation, companies like Apple had no incentive to repatriate earnings accumulated outside of United States because the United States would subject those earnings to a 35 percent corporate tax upon repatriation. In accordance with generally accepted accounting principles, most transnational companies treated offshore earnings as "permanently reinvested," an accounting treatment that meant the company did not need to book U.S. tax on these amounts because they were not going to be repatriated.[14] Now, however, the participation exemption in the Tax Cuts and Jobs Act (P.L. 115-97) exempts dividends and income that foreign companies repatriate into the United States from U.S. corporate income tax, subject to some restrictions.

The debate surrounding Apple's tax avoidance practices often centers on one simple question: Did Apple cross the line? The answer depends on a multitude of factors, including personal political and economic preferences. It also depends on the extent to which other companies employ similarly aggressive tax avoidance strategies. Some shareholders may believe that Apple and other MNEs should pay more taxes and that their practices are unethical. Others may think that Apple should be directly rewarded for creating thousands of jobs in the United States, not indirectly rewarded through tax reduction opportunities that involve moving intangibles to stateless subsidiaries in Europe. Legally speaking, Apple's Irish structure did not violate any provisions of the U.S. IRC, and its accounting methods are fully compliant with GAAP. But one can argue that from a substantive perspective Apple has committed gross tax evasion.

U.S. law does not require corporations to disclosure their tax minimization strategies on Form 10-K filings. Instead, this information is made available primarily through periodic media coverage. In reality, it is not part of the public conversation. Thus, today's financial disclosure

[11] Ilan Benshalom, "Who Should Decide Whether the Apple Is Rotten? Disclosure and Corporate Political Agency," 6 *Colum. J. Tax. L.* 86 (2014).

[12] Nelson D. Schwartz and Charles Duhigg, "Apple's Web of Tax Shelters Saved It Billions, Panel Finds," *The New York Times*, May 21, 2013, at A1.

[13] *Id.*

[14] Deloitte, "U.S. Tax Reform: Major U.S. Tax Reform Impacts" (Jan. 23, 2018).

rules only give CEOs like Apple's Tim Cook an incentive to increase shareholder wealth, making the decision to engage in tax avoidance practices easy to understand. Cook is a staunch defender of his company's tax planning practices. When an interviewer asked him about a Bloomberg Television report in which Nobel Memorial Prize-winning economist Joseph Stiglitz called Apple's profit reporting in Ireland a "fraud," Cook responded, in part:

> We have money internationally because we have two-thirds of our business there. So we earn money internationally. We didn't look for a tax haven or something to put it somewhere. We sell a lot of product everywhere. And we want to bring it back, and we've been very honest and straightforward about that.[15]

Still, referencing the money kept abroad and the U.S. corporate tax rate at the time of the 2016 interview, Cook said, "We're not going to bring it back until there's a fair rate." In essence, he said Apple would do whatever was legally possible to minimize taxes on its income — at least until the United States lowered its corporate tax rate.

D. The Irish Example

Other MNEs that have their European headquarters in Ireland, including Google, have faced criticism for their aggressive tax avoidance strategies. In August 2004 Google transferred its search and advertising technologies to a subsidiary, Google Holdings, that is incorporated in Ireland but is, for Irish tax purposes, a resident of Bermuda.[16] Thereafter, the profits generated by these assets ended up in Bermuda, after a tax-free detour through the Netherlands. This avoidance strategy — called the "double Irish Dutch sandwich" — allowed Google to cut its effective tax rate outside the United States to 6.4 percent in 2015, according to its annual Form 10-K filings.[17] Essentially, the "double Irish" structure involves forming a pair of Irish companies that turn payments on IP into tax-deductible royalty payments. The U.S. parent forms a subsidiary in Ireland and signs a contract giving the European rights to its intangible property to the new company. In return, the new subsidiary agrees to market or promote the products in Europe. Thus, all the European income that would have been taxed in the United States is taxed in Ireland instead. Next, the Irish company changes its headquarters to Bermuda, so that it does not trigger Irish tax, Bermuda tax, or U.S. tax. Finally, the parent forms a second Irish subsidiary that elects to be treated as a disregarded entity under U.S. tax law, further sheltering it from U.S. taxation. The first Irish company — now in Bermuda — can license products to the second Irish company for royalties. This results in a 12.5 percent tax rate in Ireland as opposed to a pre-TCJA rate of 35 percent in the United States (now 21 percent).

More broadly, tax havens deprive the European Union of 20 percent of the corporate tax revenue it currently collects.[18] Although the focus of this article is on the human rights impact of corporate tax avoidance on developing nations, one can also see its impact on the developed nations of Europe. In the United Kingdom, Spain, Germany, and France, about 40 percent of the wealth of the richest 0.01 percent of households is held abroad.[19] Once again, governments must make up the lost revenue from the taxes that multinationals (and the ultra-wealthy) avoid by imposing higher taxes on lower-income households, depriving these individuals of vital disposable income and potential savings. If governments cannot replace the tax revenue lost because of MNEs' tax avoidance, public spending for essential government functions and programs, such as education, must fall. Ultimately, tax inequality leads to a massive intergenerational transfer of wealth that prevents the most destitute citizens from living a better life.

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[15] Jena McGregor, "Tim Cook, The Interview: Running Apple 'Is Sort of a Lonely Job,'" *The Washington Post*, Aug. 13, 2016.

[16] Gabriel Zucman, "The Desperate Inequality Behind Global Tax Dodging," *The Guardian*, Nov. 8, 2017.

[17] Robert W. Wood, "How Google Saved $3.6 Billion Taxes From Paper 'Dutch Sandwich,'" *Forbes* (Dec. 22, 2016).

[18] Zucman, *supra* note 16.

[19] *Id*.

E. Apple Versus the EU

The Irish example demonstrates the emergence of corporate tax avoidance as a business and human rights issue. Although recently Ireland has committed to closing some tax loopholes and gradually eliminating the double Irish structure, it should also acknowledge the spillover effect of its policies on the wider world. Lately, the European Commission seems to have taken matters into its own hands.

On August 30, 2016, the European Commission alleged (C(2016) 5065 final) after an investigation that some tax rulings that Ireland gave to Apple amounted to unlawful state aid under EU law. The European Commissioner for Competition had opened the investigation on behalf of the commission in June 2014. The commissioner believed that Apple violated article 107(1) of the Treaty on the Functioning of the European Union, which states that aid granted by member states cannot distort or threaten to distort competition. This high-profile EU state aid case against Apple has significant implications not just for the company, but for all MNEs with a dominant presence in the European Union.

Since the European Commission can only order recovery of illegal state aid for 10 years preceding the date of first inquiry, the commission found that Apple had been given preferential state aid in the form of its tax rulings from Ireland from 2003 to 2013. So the commission imposed an assessment of some €13 billion on Apple, representing the tax bill that should have been collected by Ireland. Ireland has appealed the ruling, claiming that Apple is just one of many companies that have established substantive operations in the country and helped to build a thriving local economy. This position could be seen to both contradict and reverse Ireland's previously announced efforts to close the exploitive tax loopholes.

Policies that give large multinationals, such as Apple and Google, a free pass on tax are especially damaging to developing countries. These countries rely heavily on investment from MNEs, and MNEs' profits are often the best opportunity for tax to actually be collected in those developing countries. When developed countries, including Ireland and the Netherlands, tolerate transfer pricing, IP mechanisms, and other arrangements that enable those MNEs to essentially avoid taxes that would otherwise be due to the developing country, they do a tremendous disservice to society.

II. Tax and Corporate Social Responsibility

In the past, tax avoidance has rarely been discussed as a matter of CSR for transnational corporations. Lately, however, as a byproduct of the public scandals over the widespread use of tax avoidance measures by leading multinational corporations such as Apple, Google, and Amazon, the issue of CSR and taxation has moved to the forefront.

A. What Is CSR?

For decades, CSR has been the dominant framework for considering the intersection of business and human rights. The general premise underlying CSR is that corporations can no longer operate as isolated economic entities detached from broader society; hence, traditional views about competitiveness, survival, and profitability are being swept away. CSR can be characterized as a voluntary, business-led approach that contributes to sustainable development by delivering economic, social, and environmental benefits for all stakeholders.[20]

This approach has often been criticized for not being bolstered by a set of universal principles, and human rights is a relatively recent addition to the discussion of CSR. Yes, CSR and human rights responsibility, as adopted by the U.N. in 2008 in the Protect, Respect and Remedy Framework, can be seen as distinct concepts of business and human rights. Yet there are overlapping, shared concerns; the influence of the human rights responsibility agenda on the modern-day understanding of CSR is becoming more apparent.

In a 2011 report, the European Commission stated: "Through CSR, enterprises can significantly contribute to the European Union's treaty objectives of sustainable development and

[20]David L. Engel, "An Approach to Corporate Social Responsibility," 32 *Stan. L. Rev.* 1 (1979).

a highly competitive social market economy."[21] According to the commission's report — which notes that CSR is part of its Europe 2020 strategy, a broad agenda for growth in this decade — one of the factors that will help increase the impact of its CSR policy is devoting greater attention to human rights. Thus, the commission advanced a new definition of CSR as "the responsibility of enterprises for their impacts on society." The report calls on enterprises to put in place a process to integrate social, environmental, ethical, and human rights concerns into their business operations and core strategy in close collaboration with their stakeholders to maximize the shared value for shareholders, stakeholders, and society at large.

For MNEs that want a more widely recognized approach to CSR, there is also more authoritative guidance in the form of internationally recognized principles, such as the United Nations' Guiding Principles on Business and Human Rights.

B. CSR Statements Remain Hollow

Many of the CSR statements that major transnational corporations have released lack authenticity in the face of their reported tax avoidance practices. For example, as Shane Darcy notes, Apple places strong emphasis on its environmental and supplier responsibility, as well as its commitment to the right of its workers to have a safe and healthy work environment.[22] Advancing this statement while simultaneously engaging in aggressive tax avoidance schemes in Ireland and the Netherlands makes Apple's CSR statement ring hollow. Likewise, HSBC is said to have provided its customers with a "tax avoidance and tax evasion service," yet the company claims that its corporate citizenship entails responsibility not just toward customers, employees, and shareholders, but also the countries in which it operates.[23] And finally, public accounting firm PwC was accused by the United Kingdom Public Accounts Committee of helping its clients avoid tax "on an industrial scale."[24] This certainly would not align with the company's 2014 code of conduct, which sets out how the company can behave in a socially responsible way. Given their large-scale, deliberate corporate tax avoidance measures, these companies' CSR policies and codes of conduct seem duplicitous.

Entangled in these high-profile tax avoidance scandals, PwC, Barclays, and other prominent transnational firms have made significant leaps of progress in addressing tax integrity issues in their CSR policies. PwC's implementation of a supplemental code of conduct for its tax practice group, aptly called the global tax code of conduct, may be emblematic of this. Constructed in the context of its global purpose statement — "to build trust in society and solve important problems" — PwC's global tax code of conduct expressly notes that:

> Tax advice involves discussion of the wider considerations involved, as appropriate in the circumstances, including economic, commercial and reputational risks and consequences arising from the way stakeholders might view a particular course of action.[25]

PwC seems to be considering the implications of its tax advice through the lens of its clients' stakeholders, a significant development and step in the right direction toward human-rights-related CSR commitments.

Barclays — which has also been involved in a tax avoidance scandal — recently implemented several "tax principles" into its corporate citizenship policy. These principles emphasize that the company's approach to taxation is publicly available and that "tax reporting is transparent and helpful to stakeholders."[26] Furthermore, Barclays asserts that its tax planning must "comply with generally accepted custom and practice, in addition to the law and UK Code

[21] European Commission, "A Renewed EU Strategy 2011-2014 for Corporate Social Responsibility," COM(2011) 681 final (Oct. 25, 2011).

[22] Darcy, *supra* note 8.

[23] *Id*.

[24] Vanessa Houlder, "PwC Sold 'Tax Avoidance on Industrial Scale,'" *Financial Times*, Dec. 8, 2014.

[25] PwC, "What We Stand For: Tax Code of Conduct for the Global PwC Network" (2015).

[26] Barclays, "Barclays Tax Principles" (2017).

of Practice on Taxation of Banks," which in turn states that:

> the bank should not engage in tax planning other than that which supports genuine commercial activity and that is inconsistent with the underlying economic consequences unless there exists specific legislation designed to give that result.[27]

Despite these efforts to include taxation as part of MNEs' code of conduct policies, most major companies still disregard the role of tax in CSR. There is, it seems, an inherent hesitation by many companies to modify business practices that are central to generating profits and maintaining competitiveness. Diminishing aggressive tax avoidance practices for the purposes of CSR would be one of those modifications.[28] Moreover, even companies that are considered leaders in CSR rarely devote any attention to tax as a fundamental CSR issue.

In a study published in *Third World Quarterly* in 2013, Rhys Jenkins and Peter Newell noted that only 35 of the U.N. Conference on Trade and Development (UNCTAD) World Investment Report's top 100 transnational corporations appeared on the FTSE4Good Index, which tracks environmental, social, and governance practices.[29] Out of those 35 CSR leaders, Jenkins and Newell found that only 13 mentioned tax in their CSR reports, and only four of those made explicit statements regarding their tax policies. Compared with the CSR reports, even fewer companies made any mention of tax issues in their respective codes of conduct. Further, most of the tax references merely alluded to the need to comply with the law, pay a fair share of taxation, and minimize tax costs in the effort to maximize shareholder value.

Many have praised Unilever, the transnational consumer goods behemoth, for its human rights progress report, which includes a comprehensive analysis of its efforts to implement the U.N.'s Guiding Principles on Business and Human Rights and the challenges it has faced. While Unilever's 2015 inaugural report was the first by a business to use the reporting framework from the U.N. guiding principles comprehensively, the document is nevertheless in tension with Unilever's code of conduct. As Jenkins and Newell point out, Unilever's code "encourages our businesses to represent their views on the formulation and administration of tax laws, either directly or through trade associations and similar bodies."

What this all indicates is that very few transnational companies see their tax strategies as being in any way related to their CSR activities. There is no commitment to limit tax avoidance and most MNEs seem to take the view that they fulfill their social contribution by paying the taxes that are legally due. Recent public backlash against aggressive tax avoidance may be making some companies more prudent in their tax policy statements, but they still do not see tax as an aspect of CSR.

Yet, as Jenkins and Newell observe, there are several compelling arguments for including tax issues within the scope of CSR. One is that taxation is part of the "social contract" between the citizen and the state, creating an obligation on the part of citizens to pay their fair share of taxes.[30] Therefore, a claim to corporate citizenship generates an obligation to pay tax in the jurisdiction where the company operates. In exchange for paying taxes, companies can expect the government to deliver a secure environment, a well-educated workforce, and a widespread transportation infrastructure — vital conditions that are necessary for businesses to grow. A second argument for viewing taxation as a CSR issue is grounded in CSR's emphasis on considering the interests of all stakeholders. While from a shareholder's point of view tax costs should be minimized, from a stakeholder's perspective taxes and wages add to the total value produced in that particular state. Finally, the same kinds of business reasons used to justify CSR more generally can be used to justify adding tax to

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[27] *See* "Code of Practice on Taxation for Banks" (accessed Aug. 1, 2018).

[28] Darcy, *supra* note 8, at 19.

[29] Jenkins and Newell, "CSR, Tax and Development," 34(3) *Third World Quarterly* 378 (2013). The FTSE4Good Index is one of several indices that FTSE Russell produces for use by investors and investment professionals.

[30] *See also* Dermot Egan, "Does a Company's Responsibility to Society Start With Paying Its Taxes?" *The Guardian*, Sept. 9, 2011.

the CSR calculus. These include, among other things, the reputational risk associated with the negative publicity that a company may face if its aggressive tax avoidance strategies become public, the risk of litigation if the local tax authorities challenge the tax strategies, and uncertainty about how future tax liabilities may affect earnings per share.

Although many companies spend a lot of time and money to improve their corporate image and stress their commitment to the community, it is difficult to take them seriously if they are simultaneously depriving their communities of tax income that could be spent on development. The next section considers the destructive effects that tax abuses, including aggressive avoidance strategies, have on developing countries and their most destitute residents.

III. Tax Abuses in Developing Nations

Taxation plays a crucial role in funding state institutions, public services, and infrastructure. Enhancing the revenue-raising capacities of developing countries is essential to advancing sustainable development and tackling poverty, efforts that directly affect human rights efforts. The taxes levied on MNEs operating in poor countries already make a significant contribution to national treasuries but, in reality, pervasive corporate tax avoidance facilitated by an array of tax havens competing for business denies developing countries over $160 billion in tax revenue each year.[31] Corporate tax receipts are a significant component of government revenues, comprising around 10 percent of the total tax intake for OECD countries and generally around 25 percent for developing countries.[32] Globalization has made it increasingly difficult for jurisdictions to obtain tax revenues. The increased mobility of capital — often termed "capital flight" — and the widened geographical spread of major MNEs has increased the opportunities for tax avoidance and even tax evasion. Furthermore, increased competition to attract foreign direct investment has led to some countries offering more tax breaks and incentives to MNEs. These changes are of particular concern for developing countries, where tax authorities are generally very weak and extremely vulnerable to corruption and the use of undue influence to secure tax exemptions for large businesses and elite investors.[33]

A. Global Impact of Transfer Mispricing

As discussed earlier, transfer mispricing may be the primary mechanism for corporate profit shifting. Transfer mispricing significantly damages the efficacy of tax collection around the world and has wide-ranging economic and social effects beyond the lost revenue.

International standards, particularly the OECD's Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, set the arm's-length standard as the guiding principle for setting the appropriate price when transferring goods, intangibles, and services among related enterprises. If the price allocated to an intragroup transaction reflects an arm's-length price that would have been paid on the open market, the price should not be problematic. But tax authorities can challenge as price manipulation intragroup transactions that do not reflect the arm's-length principle — hence the term "transfer mispricing."

Africa may be the region that has witnessed the most significant effects of transfer mispricing. An article by Monica Iyer of Global Financial Integrity — a nongovernmental organization headed by businessman and financial crime authority Raymond Baker — studied five African countries from 2002-2011.[34] The NGO determined that, in an average year, Ghana lost $386 million, Kenya lost $435 million, Mozambique lost $187 million, Tanzania lost $248 million, and Uganda lost $243 million in potential tax and tariff revenue because of transfer mispricing. Quoting a former U.N. official, the article reports that "the annual loss to Africa from transfer mispricing has been estimated at $38 billion, higher than the flow of development assistance to the region over the same period." These revenue losses have broad effects on national budgets, economies, and

[31] Noble, *supra* note 3.

[32] Darcy, *supra* note 8.

[33] International Bar Association, *supra* note 10, at 25.

[34] Iyer, "Transferring Away Human Rights: Using Human Rights to Address Corporate Transfer Mispricing," 15 *Nw. J. Hum. Rts.* 1 (2017).

societies: Governments often try to make up for these lost revenues by increasing personal income taxes or reducing welfare spending. Further, Iyer notes that tax-driven behavior can result in lower wages and increased employment instability, as well as the "de-skilling" of the sub-Saharan African countries if companies offshore high-value functions to low-tax jurisdictions.

B. The SABMiller African Case Study

Tax in developing countries — particularly transfer pricing — is becoming a contentious topic in the international development sphere.

In a 2010 study, ActionAid discovered that SABMiller had been engaging in some of the most egregious tax avoidance schemes in Africa, avoiding millions of dollars of tax through a network of tax-haven subsidiaries.[35] SABMiller is the world's second largest beer company,[36] with interests across six continents. Its brand portfolio includes the major international names Grolsch, Peroni, and Miller, as well as iconic African beers Castle and Stone Lager and the soft drink Appletiser. Africa is its heartland — the place where it began and where it dominates the brewing industry. Yet at the time of the report, the group had more companies in tax havens — a whopping 65 of them — than it had breweries and bottling plants in Africa. As ActionAid's investigation showed, creative accounting allowed SABMiller to siphon profits from African and Indian companies to its tax haven companies, a practice that, according to the study, reduced the company's African corporate tax bill by as much as one-fifth. This abhorrent practice deprived African countries of $20 million — enough money to send a quarter of a million children to school. In the glossary that accompanies the report, ActionAid explained its use of the phrase "tax avoidance":

> The starting point is that tax avoidance activities are designed to comply with the letter of the law, not to break it, as in the case of tax evasion. We use the term to cover strategies that are legally permissible, but which ActionAid regards as ethically questionable.

Arguably, there is a thin line between (legal) tax avoidance and (illegal) tax evasion. In form, avoidance is legal; in substance, the practice should be considered illegal.

As ActionAid reported, Ghana has experienced a strong rise to economic stability and prominence. In 1933 its capital, Accra, became the site of West Africa's first brewery. In 1957 Ghana became the first African nation to gain its independence from colonial rule. Since its independence, many have come to see Ghana as a model for economic and political development. The proportion of Ghanaians going hungry has fallen by three-quarters in the past two decades, and eight out of every 10 children are now enrolled in primary school. Its tax revenue base has also improved, now amounting to 22 percent of national income — a much higher percentage than most of its neighbors. But Ghana still needs to do more in its fight against poverty. Children there are 13 times more likely to die before age 5 than children in Britain. The U.N.'s Human Development Index ranks Ghana 130 out of 169 countries, placing it in the "low human development" category. Ghana's government gets half its revenue from taxes, and it could address these issues and improve its standing as a developing nation if it had more of it.

Accra Brewery, SABMiller's subsidiary in Ghana, is one of the country's 365 largest taxpayers and Ghana's second largest beer producer. It sells $40 million of beer per year. Yet it had an operating loss in the two years before the ActionAid report and paid corporate taxes in only one of the four years from 2007 to 2010. According to ActionAid's report, SABMiller's subsidiaries in Ghana and India have been operating free of income tax, in part because of the company's use of tax havens. Its profit-shifting techniques depend on the secrecy of tax havens and on employing highly paid accountants and lawyers to exploit loopholes in the law or play one country's tax system against another's. To further

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[35] ActionAid, "Calling Time: Why SABMiller Should Stop Dodging Taxes in Africa" (2010). The hyperlinked version, available on ActionAid's website, includes an April 2012 update and a discussion of SABMiller's response to the 2010 report, which ActionAid calls "a combination of denial and obfuscation."

[36] Unless otherwise noted, statistics in this section are based on the ActionAid report and reflect the state of affairs at that time.

illustrate the problem of tax inequity in Ghana and other African countries, ActionAid interviewed Marta Luttgrodt, who operated a food and beverage stand next to the Accra Brewery in Ghana's capital city. She managed to make $310 a month and paid $23 per quarter to the Ghana Revenue Authority. Meanwhile, Accra Brewery paid no income tax in Ghana in the two years before the report.[37]

ActionAid identified several strategies that allowed the Accra Brewery to pay less tax on its beer profits than Marta did on her beverage stand. ActionAid called one strategy "the Swiss role," in which African and Indian subsidiaries pay huge "management service fees" to their European sister companies, most of which are located in Switzerland. In Ghana, these fees amounted to 4.6 percent of the company's net annual revenue during the studied period. They were paid to Bevman Services AG, an SABMiller subsidiary located in the Swiss town of Zug, a place renowned for the tax incentives it offers to "management companies" and where corporate income tax can work out to just 7.8 percent.[38] While SABMiller claimed that the management fees to its Swiss Bevman subsidiary reflected the fair value of the services provided, ActionAid estimated that management fees paid by SABMiller companies in Africa and India amounted to $66 million each year. These fees were enough to wipe out taxable profits, depriving those governments of $13 million of tax revenue.

A second strategy, which ActionAid calls "going Dutch," involves moving the ownership of brand names and trademarks away from the countries where the goods are produced and holding those assets in the Netherlands.[39] The onshore subsidiaries are required to pay royalties to the separate, brand-controlling subsidiary. The Netherlands' generous tax rules, specifically its rules on the amortization of trademarks, allow MNEs like SABMiller to pay almost zero tax on royalty income. For example, SABMiller International BV, a Dutch subsidiary, holds the rights to international sales of many African beverage brands, such as Castle, Stone, and Chibuku.[40] According to ActionAid, six SABMiller companies in Africa paid the Dutch subsidiary $50 million in royalties in 2009, creating an estimated tax loss of $15 million to African countries in that year.[41]

Finally, the third tax dodge that ActionAid found in the SABMiller case is widely known as thin capitalization. Accra Brewery borrowed money from a related company in Mauritius, a tiny island nation in the Indian Ocean. The amount of the loan was more than seven times Accra Brewery's total capitalization. Therefore, Accra Brewery was making interest payments on debt exceeding amounts it would have been able to borrow on the open market from a stand-alone company.[42] This is, in a way, a kind of transfer mispricing; Accra Brewery was essentially deducting all of its intragroup interest payments from its taxable profits, wiping out $82,000 of its tax liability each year.

SABMiller denied any wrongdoing. As an article in *The Guardian* noted:

> It completely rejected ActionAid's interpretation of its business structures. "SABMiller does not engage in aggressive tax planning in any part of its operations and the report includes a number of flawed assumptions," it said in a statement. "SABMiller companies pay a significant level of tax." It added that SABMiller was a major direct investor, employer and taxpayer in Africa and other developing countries, making a substantial economic contribution to the continent and elsewhere.[43]

The latter argument is the same trite explanation that many MNEs have offered when facing similar criticism. In reality, the effect of these schemes has been to deprive developing countries of tax revenue for investments in

[37] *See also* Felicity Lawrence, "Brewer Accused of Depriving Poor Countries of Millions in Revenue," *The Guardian*, Nov. 28, 2010.

[38] ActionAid report, *supra* note 35.

[39] Lawrence, *supra* note 37.

[40] *Id.*

[41] *Id.*

[42] International Bar Association, *supra* note 10.

[43] *Id.*

essential services, including education, healthcare, infrastructure, and other programs crucial to poverty reduction. Tax authorities in these developing countries, especially in Africa, have been fighting hard to put an end to tax dodging committed by the world's largest MNEs. But these countries are in a David-versus-Goliath battle with transnational companies. The international standards governing the taxation of MNEs, including the OECD transfer pricing guidelines, are arranged in a way that allows targeted manipulation to the detriment of these developing nations.

C. Addressing the Transfer Pricing Problem

Christian Aid — an NGO founded by a group of churches in the United Kingdom and Ireland — has expressed concern that the existing transfer pricing mechanisms are responsible for a significant shift in taxing rights away from the developing countries where they are most important for poverty suppression.[44] The complexity of the international tax system combined with the lack of capacity and specialized expertise in these countries exposes the nations to abusive tax practices.

Christian Aid offers several recommendations for addressing this capacity concern. The first is that developing countries must have access to auditors who have experience in transfer pricing matters and thus can detect when the apportionment of taxing rights is inappropriate. The second recommendation is to provide assistance to developing countries when they need to pursue these disputes through the courts. This recommendation also calls for more effective transfer pricing regulations that go beyond the lax guidelines implemented by the OECD. Regardless, legal assistance from transfer pricing attorneys would significantly help reduce the existing power asymmetry between developing countries and large multinational corporate taxpayers. Thirdly, Christian Aid notes that CbC reporting would offer the revenue authorities more information about MNEs' activities, and it would allow them to target their auditing resources toward the structures that are most likely to involve the inappropriate allocation of profits. It would also deter companies from considering antisocial tax practices. Finally, according to the NGO, interregional cooperation between revenue authorities aimed at identifying appropriate comparables would help the tax authorities in developing countries determine appropriate transfer prices, curtailing the risk for mispricing.

IV. Applying the U.N.'s Guiding Principles

Despite the absence of any direct reference to corporate taxation or tax avoidance in the U.N.'s Guiding Principles on Business and Human Rights, its concepts have still been applied to contested multinational tax practices. In 2005 the U.N. secretary general appointed John Ruggie of Harvard University to be the special representative on human rights and transnational corporations. The U.N. asked Ruggie to devise a framework detailing standards of responsibility and accountability for transnational corporations regarding human rights, as well as the role of states in regulating companies in relation to human rights. The U.N. guiding principles are, as previously noted, based on three pillars: the state's duty to protect human rights, the responsibility of corporations to respect human rights, and the need to ensure adequate remedies. While not a legally binding treaty or a newly created legal obligation, the U.N. guiding principles mandate that states do have a legal obligation to protect people from human rights violations. The dual emphasis on state and corporate actors is particularly meaningful within the realm of tax avoidance, which occurs when the government's rules facilitate the corporate desire to maximize shareholder returns.

Several U.N. and non-U.N. bodies — including the United Nations Working Group on Business and Human Rights — have begun to apply the guiding principles for this purpose. In its 2015 report to the U.N. Human Rights Council, the working group acknowledged that tax avoidance is an area in which there is a need "to better delineate roles, responsibilities and appropriate accountability systems for both States

[44] David McNair, Rebecca Dottey, and Alex Cobham, "Transfer Pricing and the Taxing Rights of Developing Countries," Christian Aid (Nov. 1, 2010).

and business enterprises."[45] Likewise, the OECD's 2011 Guidelines for Multinational Enterprises[46] are a set of recommendations that governments have presented to MNEs operating in or from adhering countries. They include nonbinding principles and standards for responsible business conduct in a global context consistent with applicable laws and internationally recognized standards.

Further, the U.N. Human Rights Council established the Intergovernmental Working Group with the goal of working toward an international treaty on business and human rights. However, most western states, including the United States and the EU member states, have avoided these treaty discussions, preferring to pursue the enactment of the U.N. guiding principles.[47] These supplemental efforts indicate how influential the U.N. guiding principles have become in a relatively short time.

A. State Duty to Protect Human Rights

The first pillar of the U.N. guiding principles — the states' duty to protect human rights — requires states to take the appropriate and necessary steps to prevent, investigate, punish, and redress human rights abuses through effective policies, legislation, regulations, and adjudication. This duty is mandatory, and thus it forms a legally binding obligation on all states under international human rights law. As discussed previously, tax abuse negatively affects economic, social, and cultural rights by diverting resources away from the public purse — funds that are needed to back essential social programs. Thus, states have several obligations when it comes to combatting aggressive tax avoidance practices.

As discussed in Section I, Ireland collaborated with Apple to craft one of the most egregious examples of corporate tax avoidance. Although Ireland has a legally binding duty to protect human rights, there is still no explicit, international, legally binding obligation to prevent it from facilitating tax avoidance and cooperating in a tax haven strategy with a company such as Apple. This is one of the major criticisms of the U.N. guiding principles: Unlike an international tax treaty, they have no legal effect and thus limited ability to deter states from participating in these abusive tax deals. The U.N. guiding principles do provide a great framework illustrating the need for states to combat tax abuse to protect their citizens and people around the world from human rights abuses. But without a formal international tax treaty specifically targeting widespread tax avoidance, countries like Ireland will not be deterred from participating in these schemes with other large MNEs in the future.

In 2013 the International Bar Association's Human Rights Institute Task Force on Illicit Financial Flows, Poverty, and Human Rights conducted an in-depth study on the responsibilities of states to address tax abuses. The previously cited "Tax Abuses, Poverty and Human Rights" report discusses this work.[48] According to the task force, the obligation of states to confront tax abuses stems from the interpretation of human rights law in the International Covenant on Economic, Social, and Cultural Rights and from the Maastricht Principles on extraterritorial obligations of states in the area of economic, social, and cultural rights. The covenant says that states have an obligation to take steps toward fully realizing all of their available resources, to include sufficient resources in their national budgets to allow for the realization of these rights, and to seek international assistance and cooperation to help them achieve the goal of maximizing their available resources. From these general principles regarding the scope of states' obligations, it is possible to infer that states have a responsibility to combat tax abuses, because the practices deprive states of the available resources necessary to realize economic, social, and cultural rights.

The Maastricht Principles take more of an extraterritorial approach to combatting tax abuses. They are particularly useful for analyzing international cooperation in tax matters —

[45] U.N. Human Rights Council, "Report of the Working Group on the Issue of Human Rights and Transnational Corporations and Other Business Enterprises," A/HRC/29/28 (Apr. 28, 2015).

[46] OECD, "Guidelines for Multinational Enterprises" (2011).

[47] Darcy, *supra* note 8, at 14.

[48] International Bar Association, *supra* note 10, at 105.

including the need for an exchange of information to confront tax abuses and secrecy jurisdictions — because they remind states to consider the impact that their tax laws have on the citizens of other states. Notably, the Maastricht Principles explicitly mention taxation as an area in which states are obligated to cooperate internationally. However, as University of Notre Dame law professor Doug Cassel notes, international human rights law generally does not require states to regulate the extraterritorial activities of businesses domiciled in their territory or jurisdiction.[49]

Ultimately, countries around the world must work together to rewrite the international tax rules and effectively implement the first pillar of the U.N. guiding principles.

B. Corporate Duty to Respect Human Rights

The key premise behind the guiding principles' second pillar — that is, the corporate responsibility to respect human rights — is that business enterprises should, in fact, respect human rights. However, unlike the states' duty to protect human rights, this second pillar is not a matter of legal obligation.

According to the U.N. guiding principles, the responsibility to respect human rights is not limited to the parent corporation but extends to every branch or subsidiary of an entire enterprise, including other companies with which it has business relations.

The U.N. guiding principles also introduce an element of proportionality into the idea of a corporate responsibility to respect human rights, which would unmistakably be relevant in the framework of tax avoidance. The responsibility of business enterprises to respect human rights applies to all enterprises regardless of their size, sector, operational context, ownership, or structure. However, some companies are more directly involved than others in facilitating avoidance, and the scale of tax avoidance by larger MNEs would presumably lead to a greater impact. While all enterprises bear human rights-related responsibilities, the level of responsibility is proportional to size and the severity of their actions' impact.

Another key element of the second pillar is the notion that companies should carry out human rights due diligence procedures to identify, prevent, mitigate, and account for how they address any adverse human rights impacts. This is reflected in the Lima Declaration on Tax Justice and Human Rights, which calls upon companies to address tax abuse in their policy statements, due diligence, and grievance processes.[50] Once companies recognize the adverse human rights results of tax abuse, the Lima Declaration recommends that "companies should then conduct their tax arrangements in transparent and accountable ways so as to not jeopardize government revenue collection, even when such arrangements are technically lawful yet contravene human rights principles." The recently revised OECD Guidelines for Multinational Enterprises also emphasize this transparency component. The guidelines suggest that companies should provide substantial information to tax authorities and comply with the arm's-length principle.

Large MNEs also exert substantial influence over the substance of both domestic and international tax laws. The Lima Declaration calls for all companies to "refrain from interfering in the public interest of tax policy-making, be that directly through special interest lobbying or indirectly through provoking tax competition." Likewise, the U.N. guiding principles state that, as part of the corporate responsibility to respect human rights, business enterprises should refrain from interfering with the ability of states to meet their own human rights obligations.

C. Access to Remedy

The third and final pillar of the U.N. guiding principles focuses on providing access to remedy.

In reality, it will be extremely difficult to determine a causal link between a single company's tax avoidance practices and the specific violation of a community's or individual's human rights. Tax abuse tends to have more of a cumulative effect on human rights in general as

[49] Doug Cassel, University of Notre Dame Law School lecture (Feb. 6, 2018).

[50] Lima Declaration on Tax Justice and Human Rights, *supra* note 2.

opposed to a specific impact. However, the International Bar Association notes that several U.N. mechanisms — for example, the Committee on Economic, Social, and Cultural Rights, which has a specific mandate that includes monitoring the fulfillment of states' obligations under the International Covenant on Economic, Social, and Cultural Rights — could indeed have the authorization and information needed to articulate the links between tax abuses and human rights on a commanding basis.[51] These mechanisms could be an appropriate avenue for seeking a remedy in the tax abuse and human rights setting should an individual or organization bring a case before one of them.

V. Conclusion and Recommendations

Corporate tax avoidance has become a highly contested topic in the global realm of business and human rights. Its complex nature and the multinational corporations that have been implicated in such schemes — as illustrated by the examples of Apple and SABMiller — collectively present serious challenges for the business and human rights movement, which has only recently begun to address tax abuses. Nevertheless, with the business and human rights agenda growing, advocates may begin to target the issue of corporate tax avoidance and challenge the fairness of tax laws and practices. Viewing tax abuses through a human rights lens can help spread awareness of a serious international challenge that needs to be addressed — namely, the fact that developing countries are losing vital corporate tax revenue that they need to support essential government functions such as education, infrastructure, and healthcare. The U.N. guiding principles provide a useful framework for tackling this issue because they address the obligations and responsibilities of both states and corporations when it comes to activities that may harm human rights.

Today's international corporate tax system is — given the modern nature of the global economy — painstakingly outdated. It gives highly sophisticated MNEs an advantage over the tax authorities in developing countries. The Lima Declaration suggests that "rigorous, evidence-based scrutiny of the impacts tax laws, policies and practices have on human rights and equality abroad should replace the all-too-often unsubstantiated assumptions about the economic benefits of maintaining the prevailing international tax system." It also calls for the United Nations to form a fully inclusive global tax body to rewrite the old international tax rules.

Another major step toward reversing the general trend toward corporate tax avoidance would be the widespread adoption of general antiavoidance or abuse rules.[52] The GAAR empowers tax authorities to consider whether the main purpose of a given transaction is to avoid or reduce a tax liability. If so, the GAAR allows the authorities to impose additional tax on the company that undertook the transaction, thus counteracting the avoidance the entity sought to achieve. This would give the tax authorities a concrete tool that allows them to enforce both the letter and the spirit of the law. It would also shift avoidance transactions from the legal realm of tax avoidance to the illegal realm of tax evasion.

Also, developing countries should not waive their right to tax royalties and management fees, especially when negotiating advance pricing agreements with companies such as SABMiller. Finally, ActionAid suggests improving the transparency of corporate reporting by making companies' financial reports such as their Forms 10-K accessible to the public and creating a global CbC financial reporting standard.[53]

As countries around the world face significant fiscal deficits, tax avoidance has become an issue that governments, the U.N., and ordinary people are finally noticing. ■

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[51] Darcy, *supra* note 8.

[52] John Christensen and Richard Murphy, "The Social Irresponsibility of Corporate Tax Avoidance: Taking CSR to the Bottom Line," 47(3) *Development* 37 (2004).

[53] ActionAid, *supra* note 35.