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International Fiscal Association
Curaçao-Aruba-Sint Maarten

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LETTER FROM THE EDITOR

Dear reader,

2025 has just begun, and the tax world is prepared to face plenty of pending issues. To begin with, this year is probably decisive for the future of the OECD Pillar One project. Although the expectations regarding the implementation of Amount A through a Multilateral Convention (MLC) agreed by all members of the Inclusive Framework (IF) are very low, countries have demonstrated some willingness to recognise the contribution of Amount B as a formulaic solution to the long-lasting problem of fixing a price for marketing and distribution activities in inter-company transactions. This includes some developing nations like Mexico, among other Latin American countries.[1]

Leopoldo Parada

Similarly, the OECD Pillar Two is not left behind. Indeed, although more successful than its counterpart —at least from an implementation perspective— the OECD Pillar Two still raises questions in some major economic actors globally. One of them is China. Indeed, as the second-world largest economy in the world, many are waiting to see whether China will respond positively to the implementation trend, or whether it will finally abstain from the 'global minimum tax trend'. Reaction from China and other BRICS countries will draw the path for what may come regarding the OECD Pillar Two, especially among developing countries. This can be particularly interesting since nothing about the global minimum tax is written in stone, as the Trump administration in the United States has already demonstrated, officially withdrawing from the OECD initiative.[2]

Finally, we should keep an eye open on the United Nations (UN) and the whole reforming process taking place in there. In fact, unlike some minority sceptical voices around, an overwhelming majority has recently approved the Term of References (ToR) for a UN Tax Convention on International Tax Cooperation in the Second Committee of the General Assembly, paving the path for the new Tax Convention, which should start in February 2025.[3] In this context, it is important to understand the role and symbolism of the UN Tax Convention, which represents an expected reaction to a much-needed decentralisation of the international tax policy debate in the hands of the OECD, creating forum that —hopefully— provides the necessary counterbalances in the current dynamics of power at the international tax level.[4] This also includes a call for developing nations in Latin America and the Caribbean both to involve in the process as well as to look to the right place when influencing their own tax policy decisions. This can be particularly relevant considering the role of the European Union (EU) and the series of initiatives supporting the recent OECD developments.

In this number, our authors aim to provide different perspectives on these and other interrelated matters. Andrea Riccardi raises some alarms for Latin American and Caribbean countries to be aware of the EU recent tax initiatives, especially considering the influence of the EU in the international tax arena as well as in the global agenda setting. For this purpose, she concentrates on two initiatives: the Council Directive 2022/2523 on ensuring a global minimum level of taxation for multinational enterprise groups and large-scale domestic groups in the Union ("minimum tax directive),[5] and the Public Country-By-Country Reporting (CBCR) Directive, which amends the Council Directive 2013/34/EU on disclosure of income tax information by certain undertakings and branches.[6] She does not only identify potential effects on the tax policies of Latin American and Caribbean countries, but also provides three specific recommendations for them to follow, namely identify the immediate effects; anticipate future demands derived from this influence, and be aware of practices from which the region can eventually take advantage of.

Yi Zheng takes the lead on one of the big elephants in the room: what will China do about the OECD Pillar Two proposal? Zheng's article provides an assessment of the global minimum tax in China, exploring the interaction of China's various tax incentives and the global minimum tax with a particular focus on the right for economic growth and the right to apply tax policy to balance and correct economic weakness. She anticipates the challenges of such an initiative in an economy like China and explores some strategic responses. Ricardo García Antón brings us a fresh perspective on arbitration as an efficient way to solve tax disputes, particularly in the Caribbean region where scepticism regarding arbitration has historically prevailed. García Antón argues that arbitration is crucial to be endorsed as a dispute resolution mechanism in double tax treaties ("DTCs"), provided a MAP ends without an agreement, examining why arbitration has been traditionally discarded as a dispute resolution mechanism in international taxation, and proposing several alternatives that can be applied in the region to increase its acceptance.

John Arias offers an interesting perspective on fiscal advances and challenges faced by Ecuador, emphasising the transformative impact of technology, transparency, and fiscal education in the relationship between the State and taxpayers.

Finally, Germaine Rekwest elaborates on the important steps undertaken by Curaçao on matters related to automatic exchange of information (AEOI), highlighting one of the most important outcomes for the country recently, namely its removal from the European list of non-cooperative jurisdictions.

This number is full of provocative and interesting perspectives in a tax world that is in constant evolution. I hope you enjoy our first number of 2025.

Leopoldo Parada

Editor of the Caribbean Tax Law Journal

[1]Stephanie Soong, Mexico to Issue Secondary Regs on ICAP and Amount B in 2025, 116 Tax Notes Int'l 1785 (2024).
[2]Memorandum for the Secretary of Treasury, The United States Representative, Subject: The Organization for Economic Co-operation and Development (OECD) Global Tax Deal (Global Tax Deal), 20 January 2025, available here. See also Mindy Herzfeld, Trump Executive Orders Bring U.S. Course Change on International Tax, 2025 TNTI 17-1.
[3]In this regard, see, e.g., Leopoldo Parada, U.N. International Tax Cooperation: The Terms of References Final Draft, 116 Tax Notes Int'l 771 (2024). In a more pessimistic view, see, e.g., Philip Baker, Reform of the International Tax Architecture: The UN Fails to Reach Consensus, 1676 Tax J., at 13 (2024).
[4]Leopoldo Parada, International Cooperation on Tax Matters at the UN, Caribbean Tax Law Journal 5 (2024), pp. 11-12.
[5]Council Directive (EU) 2022/2523 of 14 December 2022 on ensuring a global minimum level of taxation for multinational enterprise groups and large-scale domestic groups in the Union,
[6]Council Directive (EU) 2021/2101 of the European Parliament and of the Council of 24 November 2021 amending Council Directive 2013/34/EU as regards disclosure of income tax information by certain undertakings and branches, https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32021L2101 (accessed 29.12.2024).

WHY SHOULD LATIN AMERICA AND THE CARIBBEAN BE AWARE OF THE EUROPEAN UNION TAX INITIATIVES?

By Dr. Andrea Laura Riccardi Sacchi, Tax advisor to the General Directorate of Taxation within the Uruguayan Ministry of Economic and Finance.[1]

1. INTRODUCTION

The European Union (EU) has become a relevant player in the international tax arena and may influence the tax agenda setting in third jurisdictions. This is why Latin America and the Caribbean (LAC) should be aware of the EU tax initiatives.

On the one hand, the EU Standard of Tax Good Governance (comprising three key criteria: tax transparency, fair taxation and the implementation of the OECD Base Erosion and Profit Shifting minimum standards) and the establishment of the so-called "EU list of non-cooperative jurisdictions for tax purposes" may push non-member jurisdictions with economic ties with the EU to adopt certain tax policy choices that otherwise they would not have adopted. For instance, in Latin America, Uruguay and Costa Rica would not have probably modified their long-standing application of the source principle if it were not for the process of scoring, screening and listing pursued by the EU Code of Conduct Group on Business Taxation (CoCG).[2] Or Saint Lucia and Curaçao would not have introduced economic substance requirements to their foreign source income exemption regimes.[3] Furthermore, the EU may condition the agenda-setting at international organizations or bodies (e.g. UN, OECD, G20, G7). For example, EU members have shown a common position during the debates under the current UN process for the promotion of inclusive and effective international tax cooperation.[4]

On the other hand, EU legislation such as Directives and other non-binding instruments such as Communications from the European Commission, may also inspire non-EU jurisdictions' tax policy and systems and serve these jurisdictions' interests.

In this line and based on two of the latest Directives adopted by the EU, the aim of this contribution is to share some insights on how the EU may influence LAC tax policy decisions in the near future. Specifically, the initiatives referred to are: the Minimum Tax Directive and the Public Country-by-Country Reporting Directive. This contribution is not at all intended to be an exhaustive analysis of this matter but only an illustration of how the EU tax policy may impact LAC tax systems and, therefore, why it may be relevant for the region to be aware of what is going on in the EU.

2. THE MINUMUM TAX DIRECTIVE

On 14 December 2022, the Council of the European Union approved the Directive 2022/2523 "on ensuring a global minimum level of taxation for multinational enterprise groups and large-scale domestic groups in the Union"[5], formalizing the EU's implementation of the so-called "Global Minimum Tax" (GMT) – technically speaking, the GloBE rules of Pillar Two – of the Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy that was agreed by the Inclusive Framework

on BEPS of the OECD/G20 (OECD/G20 IF) in October 2021. The Directive established the application of the new rules as of fiscal years starting in January 2024, placing EU jurisdictions among early adopters of the GMT. How may this Directive impact LAC tax policy?

First, the early adoption by the EU contributed to the critical mass of jurisdictions that needed to introduce the model rules to materialize the OECD/G20 IF initiative. Once a Directive is adopted, EU jurisdictions are obliged to transpose it to national law.[6] The GMT can still be object of criticism but no one can question that the "GloBE machine" started working, deploying its global effect, including in the LAC region.

Second, the EU implementation of the GloBE rules and more precisely the so-called Income Inclusion Rule has an immediate and significant effect on the LAC region. Europe host many in-scope multinational groups that operate either via foreign subsidiaries or permanent establishments located across the Atlantic Ocean. This has put immediate pressure on LAC jurisdictions to abandon their "wait and see" position so far maintained. Though incipient, some jurisdictions already showed concrete implementation actions (Colombia, Curaçao, Barbados, Brazil, Bahamas and Puerto Rico), and steps by other jurisdictions may probably not wait in 2025.

Third, from a very practical point of view the adoption by the EU of a Directive that is available in all EU official languages and whose rules are transposed to national law by some EU members in Spanish, French, Portuguese or Dutch, may help LAC jurisdictions to overcome the difficulty of translating hundreds of pages of official documents (model rules, commentaries, administrative guidance and other relevant texts) available almost exclusively in English. This is undoubtedly of great help for jurisdictions that face significant resource constraints and, in no case, can legislate by reference. Except for the "Minimum Tax Implementation Handbook (Pillar Two)" no other official document is in Spanish. Meanwhile, a few have been translated to French, Italian or German.

Fourth, while deciding how to react, LAC jurisdictions should also monitor the future EU reaction in respect of third jurisdictions that do not get on board with the GMT. While the GloBE rules are not mandatory for OECD/G20 IF members, but a so-called "common approach", it is relevant to bear in mind that OECD and EU standards have differed in the past. In this regard, there have been some signs that in the near future the adoption of the GloBE rules may be considered as a new component of the EU Standard of Tax Good Governance which may, therefore, be assessed for purposes of elaborating the EU list of non-cooperative jurisdictions.

Indeed, in July 2020 the European Commission, issued a Communication – which is in any case a non-binding instrument – to the European Parliament and the Council of the European Union on tax good governance in the EU and *beyond*, proposing the reform and modernisation of the Code of Conduct for Business Taxation and stating in relation to the timing of such reform that

[t]he timing of the Code reform must be carefully considered, to ensure that the result is as ambitious and effective as possible. The ongoing international discussions on the reform of corporate taxation, steered by the OECD, could have a major impact on the accepted limits of tax competition in the future. In particular, if minimum effective taxation becomes a global standard, there will be a new floor on how low countries can go in using their tax rates to attract foreign businesses and investment. This will clearly have to be integrated into the EU's actions on fair tax competition, within a reformed Code of Conduct. At the same time, if there is no consensus on minimum taxation at global level, this concept needs to be introduced in the Code as an EU standard, to modernize and clarify the concept of harmful tax competition and to ensure that all businesses pay their fair amount of tax when they generate profits in the Single Market.[7]

Furthermore, in respect of a review of the EU listing criteria,[11] the Communication stated that:

[d]iscussions at international level on taxation of the digital economy and global tax reform will also need to be taken into account in the EU listing criteria. This is particularly important if there is a global consensus on minimum effective taxation. This issue should be looked at in tandem with the future reform of the Code, once the outcome of the international tax reform discussions [is]... clearer.[8]

Later in time, the multiannual work package as agreed by the CoCG in October 2023, stated:

[a]s for minimum effective taxation, the Group could explore how to facilitate the proper functioning of the Pillar Two rules by making use of the EU listing process. This work will commence only after the Pillar Two rules start applying, in coordination with the OECD and possibly based on a future peer-review process.[9]

During 2024, in February, the work programme under the Belgian Presidency (of the Council of the European Union) as agreed by the CoCG established that "the Group will also work on... the interaction between the OECD/G20 BEPS Inclusive Framework GloBE rules under Pillar Two and the criterion 2.2 of the EU list on fair taxation"[10], criterion that concerns jurisdictions that have no or very low corporate income tax, while in October, the work program under the Hungarian Presidency established that:

"[t]he Group intends to continue the work at the technical level to evaluate possible impacts of the international agreement that was reached on a minimum effective taxation (OECD Pillar 2) on its work, *including on the EU listing criteria*".[11]

3. THE PUBLIC COUNTRY BY COUNTRY REPORTING DIRECTIVE

On 24 November 2021 the European Parliament and the Council of the European Union signed the Directive 2021/2101 – the "Public Country-By-Country Reporting (CBCR) Directive" – "amending Directive 2013/34/EU as regards disclosure of income tax information by certain undertakings and branches"[12]. As per this Directive, multinational groups significantly active in the EU and with global revenues exceeding EUR 750 million have to publish, starting in year 2026, how much corporate income tax they pay in each EU member jurisdiction as well as in non-cooperative jurisdictions for tax purposes.[13] The public reports will also include other information per jurisdiction such as the nature of activities, the list of subsidiaries, revenues, the number of employees, retained earnings, and profit before tax, as well as similar information on an aggregate basis for other third-country operations. The arguments put forward under this initiative are manifold: (i) to enhance the transparency on corporate income tax paid by large multinational groups; (ii) to encourage greater corporate accountability; (iii) to achieve better informed public debate; and (iv) to strengthen trust in the fairness of national tax systems.[14] How may this Directive impact LAC tax policy?

First, as mentioned in the preamble of the Directive itself "[b]y introducing public country-by-country reporting with this Directive, the Union becomes a global leader in the promotion of financial and corporate transparency". Increasing corporate transparency and enhancing public scrutiny may be a desirable outcome worldwide, including for LAC jurisdictions in respect of multinational groups significantly active in their territories. Furthermore, public country by country reporting has been supported for many years by non-governmental organisations such as Tax Justice Network.[15]

Second, these public reports may serve LAC jurisdictions that have no access to non-public country by country reports under BEPS Action 13. Indeed, some jurisdictions may not be able to receive information under the automatic exchange of information standard, due to confidentiality and data safeguard requirements. These jurisdictions may benefit from the EU initiative by accessing and making use of information from public reports that otherwise they would not have had access to. For example, such data may serve a jurisdiction's economic impact assessment of the GloBE rules.

4. CONCLUDING REMARKS

From referencing two of the latest EU initiatives adopted, this contribution intended to identify some potential effects on LAC tax policy, demonstrating that it is relevant for tax authorities and taxpayers in LAC jurisdictions to keep update with the work developed by the EU. What has been discussed and done so far? What is currently being debated for future action? Such an exercise enables to (i) identify in due course immediate effects; (ii) anticipate future demands under either the EU Standard on Tax Good Governance or other international initiatives (OECD/UN) that may be influenced by the EU, as well as (iii) be aware of practices from which the region can eventually take advantage of.

Andrea Laura Riccardi Sacchi

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[2]For further analysis please see: Riccardi Sacchi, A.L., Is Latin American and Caribbean Tax Policy in the Hands of the European Union? A Three-Country Case Study: The Source Principle under Attack, Bulletin for International Taxation, 2023 (Vol. 77), No.9, 2023, https://www.ibfd.org/shop/journal/latin-american-and-caribbean-tax-policy-hands-european-union-three-country-case-study (accessed 29.12.2024). After the article was elaborated, Costa Rica introduced a legislative reform mirroring in general the Uruguayan reform. Meanwhile, Panama -still blacklisted- may have decided to commit and to amend in the near future the application of the source principle.
[3]For further analysis please see: Casano, F. The EU tax list of non-cooperative jurisdictions: A Caribbean Experience, Caribbean Tax Law Journal, Edition 5, 2024, https://caribbeantaxlawjournal.com/wp-content/uploads/2024/02/CTL-5_Federica-Casano.pdf (accessed 29.12.2024).
[4]For instance, please see: Council of the European Union, Position on behalf of the European Union and its Member States on tax cooperation at the United Nations, 22 September 2023, https://data.consilium.europa.eu/doc/document/ST-12967-2023-INIT/en/pdf (accessed 19.12.2024); Promotion of international cooperation on tax matters: Position of the European Union and its Member States for the 79th session of the UN General Assembly, 27 September 2024, 13895/24, https://data.consilium.europa.eu/doc/document/ST-13895-2024-INIT/en/pdf (accessed 19.12.2024).
[5]Council Directive (EU) 2022/2523 of 14 December 2022 on ensuring a global minimum level of taxation for multinational enterprise groups and large-scale domestic groups in the Union, https://eur-lex.europa.eu/eli/dir/2022/2523/oj/eng (accessed 29.12.2024).
[6]Five of the 27 EU members (Estonia, Latvia, Lithuania, Malta, Slovakia) elected to delay the application of the GloBE rules under the article 50 of the Directive.
[7]The author's highlight; European Commission, Communication from the Commission to the European Parliament and the Council on Tax Good Governance in the EU, 15.7.2020, COM(2020) 313 final, p. 3-4, https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52020DC0313 (accessed 29.12.2024).
[8]Id., p. 7.
[9]The author's highlight; Council of the European Union, Outcome of proceedings, Brussels, 5 October 2023, 13649/23, p. 8, https://data.consilium.europa.eu/doc/document/ST-13649-2023-INIT/en/pdf (accessed 19.12.2024).
[10]The author's highlight; Council of the European Union, Code of Conduct Group (Business Taxation) - Work Programme under the Belgian Presidency, 13 February 2024, 6496/24, p. 7, https://data.consilium.europa.eu/doc/document/ST-6496-2024-INIT/en/pdf (accessed 29.12.2024).
[11]The author's highlight; Council of the European Union, Code of Conduct Group (Business Taxation) - Work Programme under the Hungarian Presidency, 1 October 2024, 13998/24, p. 6, https://data.consilium.europa.eu/doc/document/ST-13998-2024-INIT/en/pdf (accessed 29.12.2024).
[12]Directive (EU) 2021/2101 of the European Parliament and of the Council of 24 November 2021 amending Directive 2013/34/EU as regards disclosure of income tax information by certain undertakings and branches, https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32021L2101 (accessed 29.12.2024).
[13]The reference comprises tax jurisdictions included in both Annexes, I and II, to the Council conclusions on the revised EU list of non-cooperative jurisdictions for tax purposes.
[14]Nonetheless there are also opposing arguments. Please see: IBFD, Promotion of Inclusive and Effective Tax Cooperation at the United Nations, 1 June 2023, p. 402, https://financing.desa.un.org/input-paper-international-bureau-fiscal-documentation-ibfd (accessed 29.12.2024).
[15]Please see: https://policytracker.taxjustice.net/policy/country-by-country-reporting (accessed 29.12.2024).

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CHINA'S TAX INCENTIVES UNDER THE GLOBAL MINIMUM TAX: ASSESSMENT AND RESPONSES

By Dr. Yi Zheng, Assistant Professor at China University of Political Science and Law (CUPL).

1. INTRODUCTION

In December 2021, the OECD/G20 Inclusive Framework on Base Erosion and Profit-Shifting released the Global Anti Base Erosion (GloBE) Model Rules to ensure the 15% global minimum tax agreed under Pillar Two.[1] The GloBE rules will have profound influence on tax policies, especially tax incentives offered by countries. This article explores the interaction of China's various tax incentives and the GloBE rules, especially from the altruistic assumption that underlines Pillar Two,[2] but with a particular focus on the right for economic growth and the right to apply tax policy to balance and correct economic weakness. Based on the potential impact of the international taxation reform, the article categorizes China's tax incentives as low-risk and high-risk. To meet the challenges posed by the global minimum tax rules, China can adopt several responses, including making full use of the 'formula mechanism' (minimum effective tax rate–ETR), changing the high-risk incentives to low-risk ones, and improving tax certainty and the procedural efficiency.

The article is divided into five parts. Part two briefly explains the main features of the GloBE rules and illustrates the inevitable implementation of the new deal. Part three introduces and categorizes China's tax incentives. Part four raises the issue that the new deal oversteps economic growth sovereignty of countries. Part five sets out several possible responses from China.

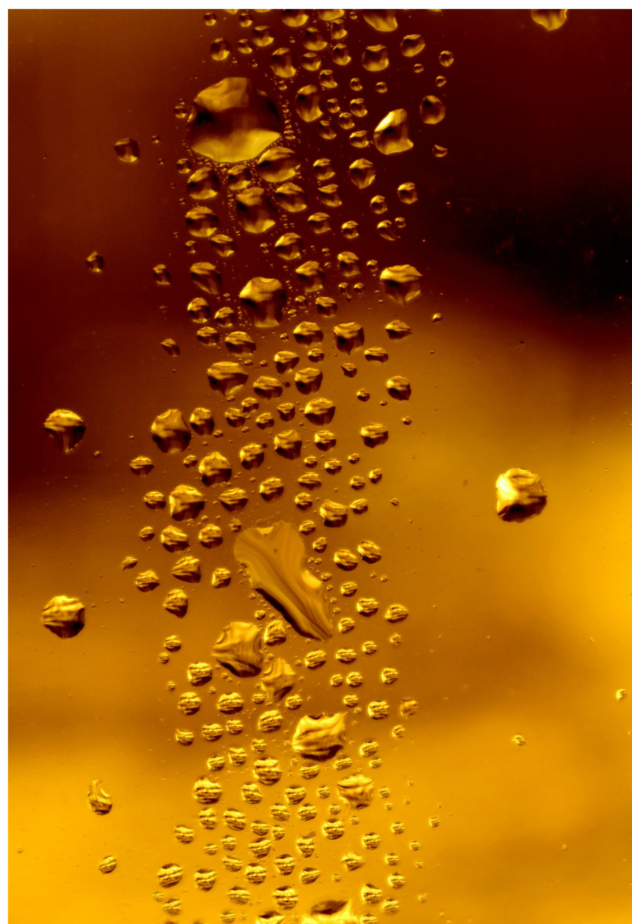
2. PILLAR TWO IN A NUTSHELL

Since 2018, the OECD/G20 Inclusive Framework, which comprises 145 jurisdictions now, has been working on a proposal for an international minimum corporate tax rate. Based on the Policy Note that OECD released in 2019, the GLoBE rules focus on setting a global minimum tax rate to solve the "remaining BEPS issues". Negotiations have culminated into a political agreement by 137 Inclusive Framework members on a common approach to implementing an internationally coordinated effective minimum tax of 15%, as laid down in the joint statement issued in 2021. Consequently, the profits of in-scope multinational enterprises (MNEs) will be taxed at a rate no lower than 15%. The core of the proposal relies on the taxation dependency that will be created between different tax jurisdictions worldwide, making profits taxable somewhere. If one jurisdiction does not exercise its right to tax to the minimum, then the power "slips" to others. This creates an idea of "take it or lose it".

To implement this idea, Pillar Two embeds a "top-up tax" approach that operates through two domestic rules: the income inclusion rule (IIR) and the undertaxed profits rule (UTPR). The IIR is triggered with priority in the country where the ultimate parent entity (UPE) of a MNE is located when income of the subsidiaries of an in-scope MNE group were not subject to a 15% ETR. Accordingly, the UTPR is triggered when the IIR fails to apply, allowing the country of other subsidiaries of the MNE group (taxing above 15%) either to deny a deduction or take the 'equivalent adjustment'. As a result of the application of these rules, countries that offer low tax rates will no longer be able to maintain their low tax competitiveness while forgoing fiscal revenue as well. In 2022, the OECD Model rules contemplated an alternative approach for those low tax countries, to neutralize unreasonable advantages granted to capital-exporting countries, especially due to the priority of the IIR. The low-tax countries are provided "another chance" to tax, which is through the so-called 'qualified domestic minimum top-up tax' (QDMTT). The QDMTT grants low-tax jurisdictions a primary right to collect their own domestic under-taxed subsidiaries' top-up tax. In other words, counties where low tax entities locate may jump the queue to collect taxes primarily through the QDMTT. However, this primary right has two caveats. First, the domestic top-up tax should be recognized as "qualified", which means meeting the standard set by the OECD Model Rules. Second, the "top-up" revenue collected by QDMTT cannot be used to refund or grant any "collateral benefits" to taxpayers.

3.CHINA'S TAX INCENTIVES UNDER PILLAR TWO

According to the Pillar Two rules, it is important to recognize that the minimum tax rule will not affect all tax incentives equally. The calculation of the ETR is based on a formula, and whether there will be and how much of the top-up tax depend on the ETR. Consequently, on one side, some tax incentives would reduce the ETR and trigger the top-up tax by either reducing the numerator or increasing the denominator, or both, when calculating the ETR. However, some tax incentives will be unaffected either because they will not be considered for the purpose of calculating the GloBE tax base, or simply because they will not reduce the ETR at all.



Currently, China has implemented a variety of corporate income tax incentives for promoting technological innovations, protecting environment and promoting regional development. This article categorizes China's tax incentives into high-risk and low-risk incentives, based on the possibility that the tax incentive incurs the top-up tax.

Low-risk incentives include immediate expensing and accelerated depreciation for investment in tangible assets, which have been widely adopted in China. For example, according to one Announcement issued by the Minister of Finance and the State Taxation Administration in China, the instruments or equipment newly purchased by an enterprise in any industry after 1 January 2019 and exclusively utilized in research and development may, if the unit value is not more than 1 million yuan, be included in the current costs and expenses at one time and deducted in the calculation of taxable income, instead of being depreciated annually. In addition, for the fixed assets newly purchased by an enterprise, they may be depreciated by shortening the depreciation period or by using the accelerated depreciation method. Where an enterprise uses the accelerated depreciation method, it may use the double-declining balance method or the sum-of-the-years-digits method. These two immediate expensing and accelerated depreciation incentives shall apply to all manufacturing industries.[3]

According to the OECD Model Rules (Article 4.4 "Mechanism to address temporary differences"), the "recapture exception accrual" includes cost recovery allowance, research and development expenses. As a result, China's accelerated depreciation incentives will not reduce the numerator of the ETR, allowing companies to benefit from this incentive. For dividends deriving from the oversea subsidiaries, China has adopted a worldwide taxation system, providing also for a foreign tax credit to eliminate double taxation.[4] From 2020, China also offers a participation exemption legislative pilot in Hainan Free Trade Port and Zhuhai Hengqin district to specific industries. As one official notice promulgated stated: "[t]he income obtained by enterprises in tourism, modern service industry, and high-tech industries established in Hainan Free Trade Port from their new overseas direct investments shall be exempt from enterprise income tax."[5] According to Article 3.2 of the OECD Model Rule, the dividends would be excluded for determining the GloBE income or loss. That is, Pillar Two requires countries neither to adopt worldwide taxation nor to treat the exemption of the overseas dividends as a tax incentive. Under this scenario, China's exemption of dividends from specific foreign investment would not be affected.

Nevertheless, China has announced a variety of tax incentives that directly reduce tax liabilities, such as tax rate reduction, tax exemptions, and tax holidays. For instance, Article 28 of the Enterprise Income Tax Law provides for a preferential tax rate of 15% for high technology enterprises. In an Announcement issued by Minister of Finance, the State Taxation Administration, the National Development and Reform Commission and the Minister of Ecology and Environment, it provided "[t]he enterprise income tax on eligible third-party enterprises engaging in pollution prevention and control shall be taxed at the reduced rate of 15%."[6] Besides, very generous tax exemptions have been granted to certain industries. For example, Article 87 of the Regulation on the Implementation of the EIT law provided, "[t]he income obtained by an enterprise from investing in or operating any of the public infrastructure projects under the support of the state shall be exempted from the EIT for the first three years as of the tax year when the first revenue arising from production or operation it is attributable to, and shall be taxed at the reduced half rate for the fourth to the sixth years." Similarly, an Announcement regarding the promotion of the development of the integrated circuit industry and the software industry stated: "[k]ey integrated circuit design enterprises and software enterprises encouraged by the state shall, from the first profit-making year, be exempt from enterprise income tax from the first to the fifth year, and be subject to enterprise income tax at the reduced rate of 10% in subsequent years."[7] These incentives are highly risk ones, as there is a strong possibility that when applied in combination, they could bring the ETR below 15%, resulting in a top-up tax somewhere else.

Another approach to grant tax benefits is allowing credits to offset final tax liabilities, that is, the so-called "Qualified Refundable Tax Credits (QRTC)". According to the QRTC shall be treated as income rather than the reduction of taxes in calculating GloBE Income or Loss. However, China rarely uses this type of incentives since the country does not recognize a "negative corporate tax". Indeed, the Chinese legislation contemplates several tax credits in the Corporate Income Tax. However, all of them are not refundable to enterprises. For example, in the Regulation of Implementation of the EIT law, Article 100 provided the tax credits as: "where an enterprise purchases and uses any of the special equipment dedicated to environmental protection, conservation of energy and water, safety of work, 10% of the investment in the special equipment may be credited to the enterprise's amount of taxes of the current year. If the amount of taxes is not sufficient for credit, the margin may be carried forward for credit in the following 5 tax years." As the regulation states, if taxes are less than credits, the remaining amounts would be carried forward to the next 5 years. Accordingly, if the credits are not used in the next 5 years, there will be no refund. At first sight, therefore, tax credits in China's tax incentive do not satisfy the QRTC definition. Therefore, they will only reduce the amount of "covered taxes" when applying and trigger the low ETR risk.

4. THE OVERSTEPPING OF SOVEREIGNTY OF PILLAR TWO

When the global minimum tax proposal was first revealed, it appeared as quite appealing. In fact, the global minimum tax grants rather than limits jurisdictions on those under-taxed profits for related countries, and it probably will finally solve the harmful tax competition problem, which has haunted countries for decades, saving them from the "race-to-the-bottom" dilemma.[8] However, despite the ostensible attractive results, there are concerns about the nation's sovereignty of economic development, especially for developing countries.

The IIR and UTPR rules attempt to curb harmful tax competition and aggressive tax planning. However, they overstep economic growth and country's sovereignty to choose the pattern that achieves economic growth, moving from one extreme to the other. The "leveling-the -playing-field" promise is at the price of nullifying certain domestic laws, especially tax incentives. Yet, based on tax sovereignty,[9] all nations have complete authority to determine taxable income, taxpayers, tax rates, tax incentives, etc. Countries may reduce taxes on specific income or even choose not to tax at all. This does not mean that the country has given up jurisdiction at all.

The above is indirectly recognized in the G20 New Delhi Leaders' Declaration, which states: "[w]e reaffirm that achieving strong, sustainable, balanced and inclusive growth (SSBIG) will require policymakers to stay agile and flexible in their policy response, as evidenced during the recent banking turbulence in a few advanced economies where expeditious action by relevant authorities helped to maintain financial stability

and manage spillovers".[10] However, the current ambitious global minimum taxation rules have ignored the fact that countries should have full sovereignty to determine their tax policies, which is commensurate with the stable and sustainable development of their economy. For some developing countries, especially those with poor political stability, insufficient skilled labor, and limited natural resources, there is few choices to be competitive for international mobile capital other than making their income tax system more attractive. For other developing countries with better infrastructure, the use tax incentives as economic regulations to promote development of specific areas and weak industries is also needed. It is precisely because of the actual inequalities in economic conditions that many countries provide tax incentives. In this regard, one would expect that emerging international tax rules should allow developing countries to provide appropriate balances and corrections of the potential risks and costs faced by investors due to those less developed economic realities. Nevertheless, the global minimum tax does precisely the opposite: severely limiting the possibilities for countries to choose how to attract investment. This has been —rightfully, perhaps— labeled by some commentators as 'paternalistic behavior' towards developing countries.[11]

An example of the above is the major shift in the OECD's perspective on international tax competition has been taking place under the new regime.[12] Over the past nearly thirty years, a clear distinction was made between harmful tax competition and others forms of competition. According to the previous documents of the OECD,[13] only those lack economic substance and attract mobile capital selectively are labeled as "harmful". Consequently, tax incentives designed to attract substantial investment and generate income cannot easily be shifted should be allowed, even if they will lead to an effective tax rate below 15%. However, all tax incentives leading to rates lower than 15% ETR will be counteracted under the GloBE proposal. Reviewing China's recent reform and market opening, tax incentives have been applied extensively to attract substantive investment, especially in the high-tech industry. Although the CIT liability was reduced, there was little risk of BEPS as the economic activities were performed where profits were generated. Therefore, even though Pillar Two was designed to solve only the "remaining BEPS issues", many tax incentives in China will be affected regardless of whether BEPS is ultimately present.

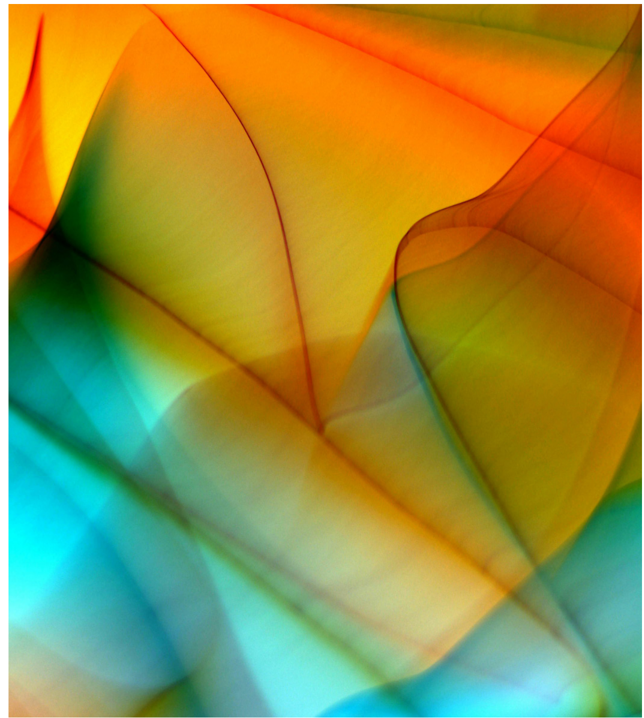
5.POSSIBLE RESPONSES THAT CHINA CAN TAKE

By the end of 2024, the implementation of Pillar Two has progressed in more than 140 jurisdictions, some countries already taken steps towards legislation with rules coming into effect in 2025.[14] In simple words, despite the potential interference with the economic sovereignty, the global minimum tax proposal likely prevails, forming the worldwide minimum corporate income tax regime. For China, a thorough review of the current incentives is suggested, as well as acting strategically to adjust incentive approaches to maintain the ETR.

Since the top-up tax is calculated according to a formula, it is natural to figure out responses based on that formula. Tax incentives that are applied to enterprises outside the scope of the GloBE can still provide benefits. In addition, the

ETR is calculated on a jurisdictional basis and based upon consolidated financial accounting rules. China is a vast country with a strong industrial system, for keeping tax incentives in certain areas, such as technology and innovation, incentives can be granted to one entity performing specific activities, while other entities in an MNE group are taxed at the normal rate, thereby increasing the average ETR and not triggering the extra tax liability. Consequently, tax incentives that are narrowly targeted are recommended, since they will leave room for blending with others. Moreover, Pillar Two contains a substance-based income exclusion (SBIE) rule, which may limit the impact of the minimum tax on entities with substantial tangible assets and payroll. In essence, SBIE is a carve-out rule, which works under the idea that profits arising from mobile income, especially intangibles, are more easily exploited for tax avoidance, and profits deriving from the "brick-and-mortar" economy should be excluded from the anti-BEPS rules. China can give full play of its substantial economy, matching entities deriving profits from intangibles with tangible assets and labor investment, reducing in this way the amount of 'excess profits' (which is on which the jurisdictional top-up tax is applied).

For general tax incentives, China can take the opportunity to re-evaluated them and improve the tax legislative quality. Tax holidays and rate reduction should be recognized as "red flag" incentives and determined whether they should be maintained or eliminated. In addition, expensing-based incentives would be more recommended when compared to income-based incentives. As mentioned previously, a qualified refundable tax credit (QRTC) is a tax incentive that the GloBE rules allow in a great extent. The



legal effect of this incentive is that the QRTC amount not actually borne by the entity is"deemed to have been borne" and is included in the covered tax. Although the net GloBE income increases accordingly, the effective tax rate of the entity will not be significantly reduced as the QRTC amount is still retained in the numerator. In other words, it is more of a financial subsidy than a tax incentive.

As noted already, China does not recognize the idea of a 'negative corporate income tax', and none of the credits provided in the current laws and regulations meet the "qualified" requirement provided by the OECD. However, when the existing credits and subsidies are applied together, they are very close to a QTRC. For example, Article 18 of the Notice of the Ministry of Finance, the Ministry of Environmental Protection, and the National Development and Reform Commission on Issuing the Measures for the Collection, Use and Administration of Funds for the Disposal of Discarded Electrical and Electronic Products, provided: "[e]nterprises that have obtained the qualification to process

waste electrical and electronic products may apply for a subsidy from the fund for processing waste electrical and electronic products listed in the Catalogue."[15] These enterprises can apply Article 100 of the Regulation of Implementation of the CIT law as well, acquiring 10% of the investment in their equipment which is used for environmental protection purpose (processing waste electronic products). China can adjust the subsidy and credits rules to switch the current tax credits into "qualified" ones, thereby mitigating the adverse effects of the GloBE rules.

Finally, promoting tax certainty could be an interesting incentive. China has not made a clear position regarding the global minimum tax, whether and which tax incentives would be effective is indeed highly uncertain. As one of the world's most attractive destination for FDI, and the world's second-largest capital exporting country,[16] China should consider the long-term development and the two-way capital flow. The IIR, UTPR and/or QDMTT need to be adopted into the Chinese domestic tax law, but they need to be well designed to connect with the existing tax system, including clear details, such as the scope of application, triggering conditions, and the procedural requirements.

Yi Zheng

[1]See OECD, Tax Challenges Arising from the Digitalisation of the Economy -- Global Anti-Base Erosion Model Rules (Pillar Two): Inclusive Framework on BEPS (2021) [OECD Model Rules]. See also, OECD, Challenges Arising from the Digitalisation of the Economy: Commentary to the Global Anti-Base Erosion Model Rules (Pillar Two) (2022)
[2]As many commentators have already argued, the altruistic assumption of the GloBE is unrealistic. For example, see Leopoldo Parada, 'Global Minimun Taxation: A Strategic Approach for Developing Countries. Columbia Journal of Tax Law' 15(2), 187–211 (2024); Afton Titus, 'Global Minimum Corporate Tax: A Death Knell for African Country Tax Policies?' Intertax 50 5 : 414-423 (2022); Pereira, R. Codorniz Leite, 'Pillar Two and Developing Countries: The Perils of Jurisdictional Blending' World Tax Journal 15 4 : 545-573 (2023).
[3]See Announcement of the Ministry of Finance and the State Taxation Administration on Expanding the Scope of Application of the Preferential Policies on the Accelerated Depreciation of Fixed Assets. (2019).
[4]See Article 3 and Article 23 of the Enterprise Income Tax Law of PRC.
[5]See Notice by the Ministry of Finance and the State Taxation Administration of Preferential Income Tax Policies for Enterprises in Hainan Free Trade Port (2020).
[6]See Announcement of the Ministry of Finance, the State Taxation Administration, the National Development and Reform Commission and the Ministry of Ecology and Environment on Issues Concerning Enterprise Income Tax Policies for Third-Party Enterprises Engaging in Pollution Prevention and Control (2023).
[7]See Announcement of the Ministry of Finance, the State Taxation Administration, the National Development and Reform Commission and the Ministry of Industry and Information Technology on Enterprise Income Tax Policies for Promoting the High-Quality Development of the Integrated Circuit Industry and the Software Industry (2020).
[8]"Race to the bottom" has been widely used to describe the worldwide tax competition could reduce countries fiscal revenue and their general welfare. See Rosanne Altshuler, Harry Grubert, 'The Three Parties in the Race to the Bottom: Host Governments, Home Governments and Multinational Companies' 7 Fla. Tax Rev. 153 (2005).
[9]Diane Ring, 'Democracy, Sovereignty and Tax Competition: The Role of Tax Sovereignty in Shaping Tax Cooperation' 9 Fla. Tax Rev. 555 (2009); Brian J. Arnold, 'The Evolution of Controlled Foreign Corporation rules and Beyond' Bulletin For International Taxation, 73(12): 631-648 (2019); Noam Noked, 'Defense of Primary Taxing Rights' 40 Va. Tax Rev. 341 (2021); Aitor Navarro, 'Jurisdiction Not to Tax, Tax Sparing Clauses, and the OECD Minimum Taxation (GloBE) Proposal' Nordic Tax Journal 2021: 6 - 19. (2021).
[10]See G20 New Delhi Learders' Declaration,9-10 September 2023, available here: https://www.mea.gov.in/Images/CPV/G20-New-Delhi-Leaders-Declaration.pdf
[11]Parada, supra note 2, 187–211.
[12]Ibid.
[13]See OECD, Harmful Tax Competition: An Emerging Global Issue (1998); and OECD, Base Erosion and Profit Shifting Action 5 Harmful Tax Practices (2013).
[14]OECD Pillar Two Country Tracker, available here: https://www.pwc.com/gx/en/services/tax/pillar-two-readiness/country-tracker.html
[15]Article 18 of the Notice of the Ministry of Finance, the Ministry of Environmental Protection, and the National Development and Reform Commission on Issuing the Measures for the Collection, Use and Administration of Funds for the Disposal of Discarded Electrical and Electronic Products.
[16]See Statistical Bulletin of FDI in China 2024, Department of Foreign Investment Administration of the Ministry of Commerce, available at here: https://wzs.mofcom.gov.cn/cms_files/filemanager/195082220/attach/20249/1534906939894198bbb5b6b86a752466.

IFA BRANCH CURAÇAO-ARUBA-SINT MAARTEN INVITES YOU TO A LECTURE ON **TAXING CROSS-BORDER BUSINESS INCOME IN A DIGITALIZED ECONOMY. WHERE DOES LATIN AMERICA AND THE CARIBBEAN STAND?**

PROGRAM

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Dr. Germaine Rekwest (President IFA Branch Curaçao-Aruba-Sint Maarten)

18.10 Taxing cross-border business income in a digitalized economy. Where does Latin America and the Caribbean stand?
Dr. Andrea Laura Riccardi Sacchi, Tax advisor to the General Directorate of Taxation within the Uruguayan Ministry of Economic and Finance.

Last December the UN General Assembly agreed to the Terms of Reference for the elaboration of a Tax Framework Convention, including an early protocol on the “taxation of income derived from the provision of cross-border services in an increasingly digitalized and globalized economy”. The presentation will share an overview of the current state in the field, briefly analyzing different alternatives and reflecting on the future by drafting a “wish list” for a proposal beyond the dichotomy "OECD Amount A – DSTs".

19.00 Closing

19.00-20.00 Network & drinks

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WHO IS AFRAID OF ARBITRATION TO SOLVE TAX DISPUTES? A LOOK INTO THE CARIBBEAN REGION FOR SPOTTING PROBLEMS AND PROPOSING SOLUTIONS

By Dr. Ricardo García Antón, Assistant Professor of International and European Tax Law, Fiscal Institute Tilburg, Tilburg School of Economics and Management, Tilburg University.

The recourse to arbitration as the last stage of the mutual agreement procedure ('MAP') to solve tax disputes is not universally accepted.[1] Arbitration is not listed as a minimum standard in Part VI of the Multilateral Convention to Implement Tax Treaty-Related Measures to Prevent Base Erosion and Profit Shifting ("MLI"). Looking into the Caribbean Region, this trend is confirmed. Jamaica and Belize have opted out of arbitration in Part VI of MLI. The double tax treaties ("DTCs") signed by Countries like the Dominican Republic and Cuba, which are not MLI signatories but concentrate important foreign direct investment in the Caribbean Region (i.e. tourism is a huge economic driver), do not contain the arbitration clause laid down in Article 25 (5) OECD and 25 (5) (B) UN Model Tax Convention. In regional organizations like the Caricom, Article 23 of the Caricom Double Taxation Treaty (1994) carved out arbitration. Barbados[2] and Curaçao[3] are perhaps the few exceptions in the Caribbean Region that opted in for Part VI of the MLI.

In the author's view, arbitration is crucial to be endorsed as a dispute resolution mechanism in double tax treaties ("DTCs"), provided the MAP ends without an agreement. Every tax dispute must be concluded with a final and binding decision as the only way to comply with the legal certainty principle. There are two reasons to support arbitration as an effective dispute resolution mechanism. First, investors aim to secure an effective solution to their disputes regarding tax treaties. The lack of arbitration clauses in DTCs may discourage the choice of a particular jurisdiction to structure a cross-border investment. Second, the fact that arbitration is not universally accepted in international taxation is a clear anomaly within international economic law. In the framework of international investment agreements ("IIAs"), all the agreements contain a referral to mandatory arbitration to solve disputes between the investor and the host state. Yet, there is an important caveat to add. The author's faith in arbitration as an effective dispute-resolution mechanism cannot be assimilated to support arbitrary or discretionary awards by the arbitrators. Arbitration must be always reconciled with the rule of law, and the award must contain proper legal reasoning.

This contribution aims first to examine the causes of why arbitration is traditionally discarded as a dispute resolution mechanism in international taxation, and second, propose several solutions that can be applied to the Caribbean Region to increase the acceptance of arbitration as an effective dispute resolution mechanism. The last section summarizes the principal findings.

THE RELUCTANCE TO ARBITRATION TO SOLVE TAX DISPUTES

The literature has underlined the most frequent concerns against arbitration conveyed by countries: risks of national sovereignty, constitutional limits, high costs, and the need for expertise.[4] Such concerns are decisive when developing countries are involved. Arbitration is perceived as a threat to national sovereignty since enables appointed arbitrators to potentially overcome national judicial decisions and give away tax collection. Arbitration challenges the power of the state to autonomously decide its tax matters. The arbitration costs (i.e. fees of arbitrators, lawyers, and independent experts) are indeed quite high, bearing in mind the lack of expertise associated with the tax administration of developing countries.

Aside from the previous concerns frequently handled by states, the OECD has not contributed much to supporting arbitration in Article 25 (5) OECD Model Tax Convention and Part VI of the MLI. First, Article 25 (5) OECD Model Tax Convention (2017) presents important limitations: (i) arbitration is only permitted in respect of actions of one or both states that “have resulted” in taxation not in accordance with the treaty (i.e. actions that “will result” are excluded); (ii) only unresolved issues in the MAP can be subject to arbitration (i.e. the arbitrators cannot solve the dispute as a whole if there was agreement on certain elements).[5] Second, Article 25 (5) OECD MC (2017) allows the states to exclude certain matters from arbitration (i.e. issues that are primarily factual in nature as Paragraph 66 of the Commentaries to OECD Model Convention (2017) point out).[6]

Part VI of the MLI neither benefits the widespread of arbitration since (i) it allows the states to introduce important reservations to arbitration and, (ii) makes a regrettable choice for baseball arbitration. The first block of reservations allowed under article 19(12) of the MLI ensures that domestic proceedings prevail over an arbitration procedure. Those reservations are the following: (i) an unresolved issue from a MAP cannot be referred to arbitration if a court or administrative body of any of the contracting states has previously ruled on the same matter; and (ii) if, at any time after the request for arbitration but before the arbitral commission has rendered its arbitration award, a decision is rendered by a court or administrative body of one of the contracting states, the arbitration procedure must be terminated. The latter reservation does not oblige the taxpayer to waive its domestic appeals in order to reach the arbitration stage. However, there is a risk that, if he does not do it, there could be a judicial solution prior to the arbitration award that would put an immediate end to the arbitration procedure.[7]

The second block of reservations is related to the scope of arbitration allowed under Article 28(2)(a) of the MLI. The Spanish position to the MLI offers an exhaustive catalogue of limitations to enter into arbitration: (i) cases involving the application of anti-abuse norms; (ii) cases in which a person directly affected by the case has been subject, by a final ruling resulting from legal or administrative proceedings of either contracting state, to a penalty for tax fraud, wilful default, and gross negligence; (iii) cases of transfer pricing involving items of income or wealth which are not subject to tax in a jurisdiction, either because they are excluded in the taxable base of that contracting jurisdiction, or because they are exempt or taxed at a reduced rate in that contracting jurisdiction; (iv) cases eligible for arbitration under the Arbitration Convention (90/436/EEC: Convention on the elimination of double taxation in connection with the adjustment of profits of associated enterprises); and (v) cases in which both contracting states agree that they are not suitable for arbitration (discretionary provision). These in-scope limitations jeopardize the effectiveness of arbitration. According to article 23(1) of the MLI, the so-called baseball arbitration (last best offer) is the default option instead of the reasoned opinion arbitration. Commentators have been critical of applying baseball arbitration to tax matters, particularly regarding (i) the limited role of the taxpayers; (ii) a decision being made without any reasoning, by a simple majority; and (iii) the lack of publication of the decision.[8] Despite the speed, low cost, and simplicity of baseball arbitration, this author agrees with the previous criticisms that pose serious breaches of legal certainty and fairness. If arbitration needs to align with the rule of law to be generally accepted by states as an effective dispute resolution mechanism, baseball arbitration is not the way forward.

In conclusion, the reluctance to accept arbitration as an effective dispute resolution mechanism for international tax disputes clashes with the states, which are concerned with the high costs and severe limitations to tax sovereignty. In addition, such unwillingness for arbitration pervades the OECD's work both in Article 25 (5) of the OECD Model Convention and Part VI of the MLI. On one hand, the OECD seems to encourage

MAP (i.e. BEPS Action 14 and Part V of the MLI are minimum standards) but blocks arbitration, on the other hand. Such a contradictory strategy will result in “fake MAPs”: the administration opens the MAP without any endeavor to solve it since access to arbitration will be precluded in a later stage (i.e. the state has introduced an in-scope reservation for arbitration for cases of applying anti-avoidance provisions).[9]

FOSTERING ARBITRATION IN THE CARIBBEAN REGION

The disappointing picture of arbitration as a dispute resolution mechanism needs to be reverted. Strikingly in the Caricom, the rejection of arbitration in the Caricom Double Taxation Treaty (1994) contrasts with the inclusion of arbitration as a dispute resolution mechanism to solve the disputes between the Member States of the CARICOM (Articles 204-206 of the Revised Treaty of Chaguaramas establishing the Caribbean Community, 2001 – ´Caricom Treaty´). In Addition, Article 223 of the Caricom encourages the Member States to facilitate arbitration to solve private commercial disputes among Community nationals as well as Community nationals and nationals of third states. Why tax disputes cannot be aligned with other international commercial disputes?

To increase the acceptance of arbitration, especially in the Caribbean Region, there are four potential areas of improvement: (i) elimination of restrictions to arbitration in tax matters; (ii) selection of arbitrators; (ii) the enforcement of uniform procedural rules for tax disputes in the Region with a substantial increase in taxpayers’ rights ; (iii) reduction of the arbitration costs. Concerning the first block of measures, there are important improvements to make. First, the OECD should amend Article 25 (5) OECD Model Convention (2017) to allow the arbitrators to review the whole of tax disputes, and not only the issues not solved in the MAP. Resolving the whole case is crucial since all issues of a case are interconnected. Limiting the scope of review to “unresolved issues” constraints arbitrators to issues already agreed by the states. Second, limiting arbitration to actions that “have resulted” and not “will result” in Article 25 (5) OECD Model Convention (2017) is not aligned with 25 (1) OECD Model Convention (2017) that relates to the opening of a MAP. While for requesting a MAP, action that “will result” in taxation not in accordance with the treaty is allowed, there is no justification to exclude it from the opening of arbitration in 25 (5). Third, the OECD should limit the scope of reservations that

states can make to arbitration in Part VI, as well as eliminate baseball arbitration as a default system for arbitration. These suggested modifications aim to reduce the dependency of tax arbitration in international taxation from the MAP procedure. Granting major autonomy to tax arbitration aims to get closer to arbitration in other areas of international law, like investment law.

About the second block of improvements, the appointment of arbitrators has been always controversial. Developing countries cast doubts on the impartiality of panel members coming from developed countries. To prevent this outcome, Article 20 of the MLI imposes an arbitration panel of 3 individuals with expertise in international tax matters. Each competent authority appoints one panel member and the two panel members appoint the third panel member, who will be the chair of the arbitration panel and cannot be a national/resident of either contracting state. In the author's view, regional organizations like Caricom, Andean Community, and Mercosur should play a major role in the appointment of the chair (the third member of the panel) for arbitration cases in the Caribbean and South America. Arbitrators listed by these regional organizations should have expertise in international taxation, as well as knowledge of the economic, legal, and political circumstances in the regions. Another improvement that can be made to assist the arbitrators without any previous background in international taxation is the creation of a permanent committee of tax experts that render non-binding opinions to arbitrators.[10] An impartial permanent tax committee, under the auspices of the UN, could increase the trust in arbitration by developing countries. If the final decision of the arbitrators deviates from the opinion of the permanent committee of tax experts, one should expect explicit and well-argued reasons to do so.

Regarding the third block, there is a need to uniformly regulate the binding procedural aspects of arbitration, the so-called Lex Arbitrii, for the whole Caribbean Region. Part VI of the MLI as well as the Commentaries to Article 25 UN/OECD Models contains detailed procedural rules on arbitration that states may agree upon (i.e. OECD/UN Sample Mutual Agreement on Arbitration). Some countries like Spain have entered into ad hoc Memorandum of Understanding with treaty partners (i.e. DTC between Spain and the UK, 2013) that provide detailed arbitration rules. The procedural rules cover issues related to the selection and requirement of the arbitrators, confidentiality, deadlines, interaction with domestic procedures, suspension, costs, implementation of the award, and participation of the taxpayer in the arbitration proceedings. In the author's view, countries in the Caribbean Region, via Caricom for example, should approve a Lex Arbitrii for tax disputes in the Region. In doing so, one of the crucial aspects will be to increase the participation of the taxpayer in comparison to the MAP. This has been already the trend in other jurisdictions like the EU. The EU Dispute Resolution Directive (Council Directive (EU) 2017/1852 of 10 October 2017 on tax dispute resolution mechanisms in the European Union) provides for more extensive rights for the taxpayer.

Finally, the fourth block, third-country funding could be used to alleviate the costs of arbitration. Third-party funding has been used in commercial arbitration since the 1990s to allow a third-party funder to provide financial resources to the party to the dispute without, or insufficient financial resources for a proceeding in exchange for shares of the case.[11] Some authors have already concluded that third-party funding does not present major legal barriers to be transplanted to international tax disputes.[12] The recourse to third-party funders can eliminate the high costs that developing countries may face. For third-party funders, financing tax arbitration could be attractive due to the economic magnitude of tax cases.

CONCLUSIONS

Arbitration in international tax matters has not yet been emancipated from the MAP narrative, an inter-state procedure that does not oblige the states to reach a solution. As such, arbitration in international tax matters cannot be leveraged to arbitration in commercial and investment disputes. The reluctance to arbitration in taxation is twofold. On one hand, the states are afraid of losing tax sovereignty and incurring substantial costs. And, on the other hand, it seems that the OECD/UN introduces serious obstacles to enable arbitration to be generally accepted (reservations, limited scope, baseball arbitration, etc.). Arbitration in tax matters is unfortunately a mere extension of an unsuccessful MAP.[13]

Contrary to this narrative, this author has emphasized that tax arbitration should be aligned with commercial and investment arbitration. Taxpayers have the right to obtain a binding resolution that puts an end to litigation on treaty disputes. In the Caribbean region, where foreign direct investment is crucial in sectors like tourism, investors request legal certainty.

There is no reason to keep the “tax exceptionalism” in the area of disputes, as this author has elsewhere written.[14] The convergence of tax arbitration with commercial and investment arbitration requires facing important challenges. First, tax arbitration should respond to the rule of law. Therein lies the need to replace baseball arbitration with reasoned opinion arbitration, and increase taxpayer’s rights. Second, regional integration organizations like Caricom, Andean Community, and Mercosur should play a major role in increasing trust in arbitration (i.e. appointment of the chair and enforcement of procedural rules). Third, the OECD, UN, and G20/OECD Inclusive Framework should work towards the elimination of restrictions that jeopardize the effectiveness of tax arbitration (i.e. reservations and procedural limitations). Fourth, third-party funding needs to be explored as an effective way to alleviate the costs derived from arbitration procedures.

Ricardo García Antón

[1]J. de Goede & Sam Maruca, Practical Approaches to International Tax Dispute Prevention and Resolution, IFA Cahiers, Vol. 108 (2024), p. 79
[2]Barbados chose to apply Part VI to its network of treaties subject to MLI (31 treaties). Available at https://www.oecd.org/content/dam/oecd/en/topics/policy-sub-issues/beps-mli/beps-mli-position-barbados-instrument-deposit.pdf (Access 15.12.2024)
[3]There was an arbitration provision in Article 24 (5) of the Netherlands in respect of Curaçao – Malta Income and Capital Tax Treaty (2015), IBFD treaty database; The arbitration provision in the MLI applies to the Netherlands in respect of Netherlands Antilles – Norway Income and Capital Tax Treaty (1989), IBFD treaty database
[4]J. de Goede & Sam Maruca, supra n. 1, p. 79
[5]See a detailed analysis in J. Schwarz, Scope of Arbitration under the OECD and UN Model Provision, in G. Maisto (ed), Dispute Resolution under Tax Treaties and Beyond, (IBFD, 2023)
[6]The matters excluded from arbitration are usually profit allocation, existence of permanent establishment, residence, and application of anti-abuse provisions. See J. Schwarz, supra n. 5, p. 232
[7]See A. Maldonado and R. García Antón, Spain, in G. Maisto (ed), Dispute Resolution under Tax Treaties and Beyond, (IBFD, 2023)
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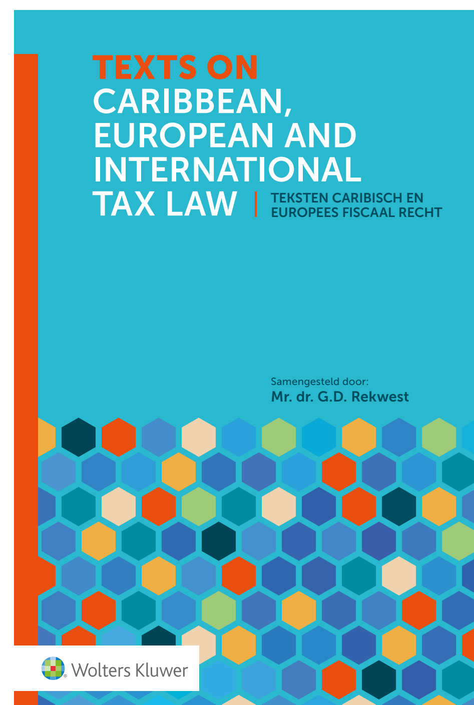


TAX COMPLIANCE METRICS IN EMERGING ECONOMIES: LESSONS FROM ECUADOR AND ITS REGIONAL NEIGHBORS

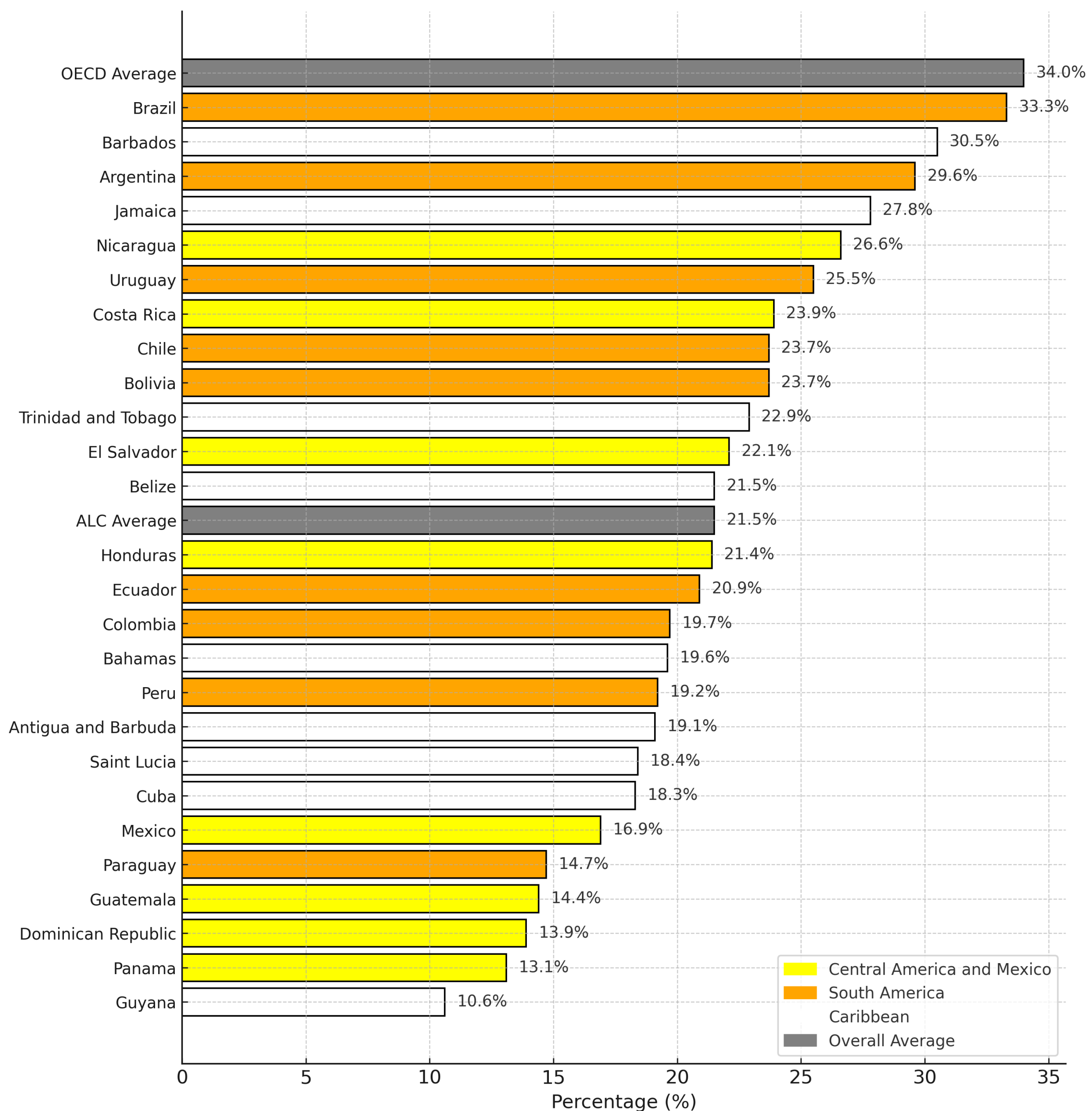
By John Arias Izquierdo, Master in Tax Law, MBA, Founding Partner and General Manager of Census Consultores.

INTRODUCTION

In emerging economies, tax compliance goes beyond technical aspects: it reflects citizens' trust in their governments and serves as a cornerstone for sustainable development. Latin America, a region marked by high levels of informality and inequality, faces significant challenges in building inclusive and efficient fiscal systems. Without a robust tax base, nations struggle to finance essential services such as education, healthcare, and infrastructure, perpetuating social and economic disparities.

This article explores the fiscal advances and challenges faced by Ecuador, highlighting how the adoption of digital technologies and structural reforms have boosted revenue collection and improved transparency. Simultaneously, it examines persistent barriers such as tax evasion and the informal economy—issues that affect Ecuador and its regional neighbors alike. Through comparative analysis, the article identifies key lessons that can be applied to other emerging economies, including those in the Caribbean, where similar contexts present opportunities for mutual learning.

Beyond the numbers, the article emphasizes the transformative impact of technology, transparency, and fiscal education on the relationship between the state and taxpayers. This approach not only underscores the importance of strengthening citizen trust but also offers practical insights for building equitable tax systems that promote sustainable and inclusive development, both in Latin America and globally.



THE TAX LANDSCAPE IN EMERGING ECONOMIES

Latin America presents a complex dynamic in fiscal terms. The region grapples with structural inequalities, high levels of informality, and a disproportionate tax burden on certain sectors. According to the 2024 Tax Statistics Report for Latin America and the Caribbean, the region's average tax revenue as a percentage of GDP was 21.5% in 2022, significantly below the OECD average of 34%.[1]

This disparity reflects historical challenges that have hindered countries' ability to mobilize domestic resources. These include a lack of diversification in tax bases, low progressivity in tax systems, and a heavy reliance on indirect taxes like VAT, which account for a significant share of fiscal revenues compared to direct taxes.

Region	VAT Collection Ratio	VAT Rate (%)
Central America and Mexico	**0.49**	**13.6**
Costa Rica	0.50	13.0
Dominican Republic	0.38	18.0
El Salvador	0.73	13.0
Guatemala	0.52	12.0
Honduras	0.52	15.0
Mexico	0.33	16.0
Nicaragua	0.52	15.0
Panama	0.41	7.0
South America	**0.60**	**16.8**
Argentina	0.47	21.0
Bolivia	0.71	13.0
Chile	0.42	19.0
Colombia	0.81	19.0
Ecuador	0.69	12.0
Paraguay	0.58	10.0
Peru	0.45	18.0
Uruguay	0.64	22.0
Caribbean	**0.71**	**13.6**
Antigua and Barbuda	1.26	15.0
Bahamas	0.62	10.0
Barbados	0.71	17.5
Belize	0.22	15.0
Guyana	0.73	14.0
Jamaica	0.59	12.5
Saint Lucia	0.81	15.0
Trinidad and Tobago	0.58	12.0
ALC Average	**0.56**	**14.7**
OECD Average (2020)	**0.56**	**19.1**

Ecuador, with a tax revenue equivalent to 20.9% of GDP in 2022, exemplifies the advances and challenges faced by emerging economies. One of the most notable measures implemented is the adoption of electronic invoicing, which has raised the VAT collection ratio to an impressive 0.81, significantly above the Latin American and Caribbean average of 0.58. This indicator reflects greater efficiency in revenue collection, driven by process digitization and institutional strengthening in tax administration.

Nevertheless, high economic informality, affecting 60% of workers in the region, remains a structural challenge that undermines fiscal equity. The inability to capture transactions outside the formal system not only complicates the expansion of the tax base but also perpetuates a fiscal model in which the tax burden disproportionately affects a small segment of the formalized population. Addressing this issue requires innovative policies that combine incentives for formalization with stronger enforcement measures.

Furthermore, the perception of fiscal justice and the efficiency of public resource allocation play a crucial role in tax compliance. When citizens perceive that their taxes do not translate into quality public services or that corruption levels are high, their willingness to fulfill tax obligations decreases dramatically. Ecuador, like other countries in the region, faces the challenge of strengthening citizen trust through greater transparency and accountability.

TAX COMPLIANCE METRICS: TOOLS FOR DIAGNOSIS AND IMPROVEMENT

Among the main metrics is the voluntary compliance rate, which reflects the percentage of taxpayers who declare and pay taxes within the established deadlines. This indicator not only measures the willingness of citizens to comply with their tax obligations, but is also a reflection of the perceived fairness of the tax system and the level of trust in tax institutions.

Another important indicator is the tax gap, which measures the difference between potential tax revenues and actual collections. This data highlights inefficiencies in tax administration, evasion problems and possible deficiencies in tax legislation. Bridging this gap is essential to ensure fiscal sustainability and foster tax justice, as uncollected revenues limit the government's ability to finance public policies.

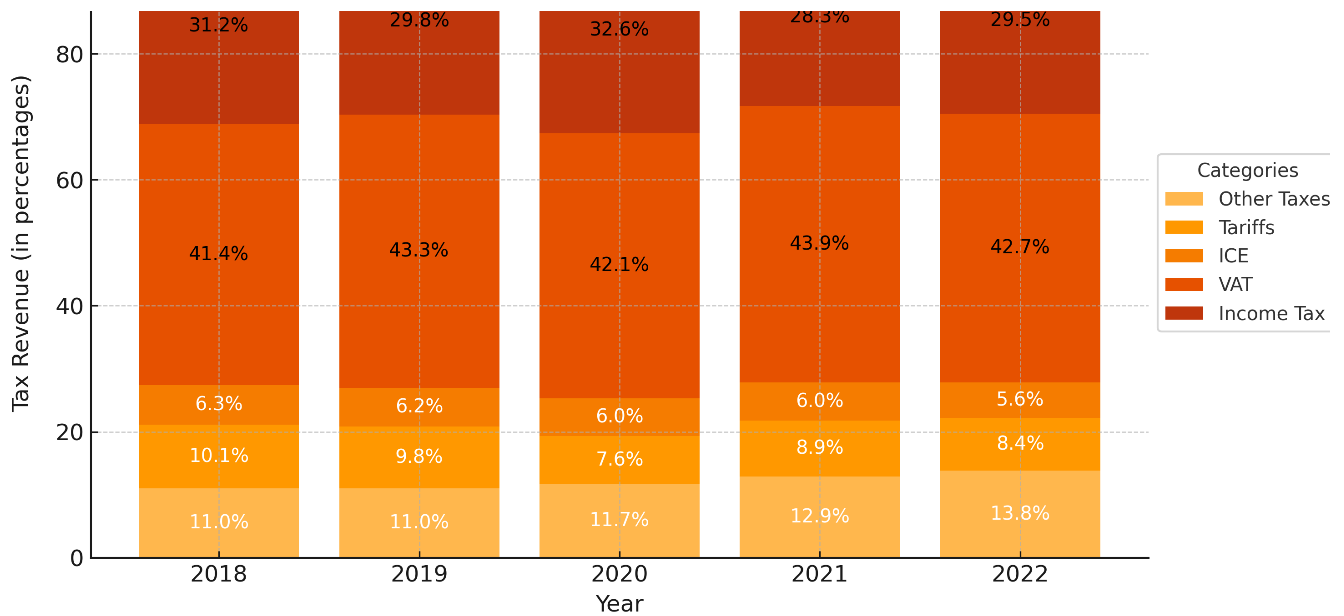
The cost of compliance is also a critical aspect. It measures the resources that taxpayers must allocate to comply with their tax obligations, including time, administrative costs and access to digital tools. A high cost of compliance can discourage compliance, especially among small taxpayers, micro-enterprises, and informal sectors.

Finally, it is important to consider indicators that evaluate taxpayers' perception of the quality of tax administration services. Aspects such as the ease of use of digital platforms, the speed of responses to queries and the clarity of regulations have a significant, albeit indirect, impact on voluntary compliance and the legitimacy of the tax system. All these elements allow for a more complete view of fiscal performance and contribute to the design of more effective and socially accepted public policies.

ECUADOR'S CASE: FACTORS BEHIND ITS HIGH VAT COLLECTION RATIO

In Ecuador, the high VAT collection ratio compared to the regional average reflects the effectiveness of several key measures. According to the 2024 Tax Statistics Report for Latin America and the Caribbean, the implementation of electronic invoicing has been a decisive factor, enabling more efficient control over commercial transactions and significantly reducing tax evasion. This technology has improved the traceability of operations and lowered compliance costs for taxpayers, facilitating their interaction with the tax system.[2]

On average, VAT accounted for 42.7% of Ecuador's total tax revenues between 2018 and 2022, making it the tax with the greatest weight in total revenue—12 percentage points higher than the second most important tax, income tax.[3] Moreover, its share has remained relatively stable during this period. In Latin America and the Caribbean, VAT accounted for 33.4% of total tax revenues in 2019 (the last pre-pandemic year), excluding social security contributions. In Ecuador, this share was 43.3% during the same year, according to the Ministry of Economy and Finance.[4]



Until 2024, Ecuador had one of the lowest VAT rates in Latin America. Until mid-2023, Ecuador and Guatemala shared the third-lowest rate in the region (12%), surpassed only by Panama (7%) and Paraguay (10%). The rate has now been permanently raised to 13% and will progressively increase to 15% by the 2025 fiscal period.

The progressive implementation of electronic invoicing has become a fundamental pillar for the success of VAT in Ecuador. This system has allowed the Internal Revenue Service to monitor commercial transactions in real time, promoting greater traceability and transparency in the country's economic operations.

Among the most prominent benefits is the reduction of tax evasion, since the digital registration of transactions makes it difficult to under-declare income, a recurring problem in the region. In addition, e-invoicing has significantly improved the control of value chains, allowing VAT compliance to be verified at each stage of the production process and thus reducing irregularities.

In addition to these aspects, the system offers greater convenience for taxpayers. Automating processes reduces errors and the time needed to declare and pay taxes, incentivizing voluntary compliance and strengthening the relationship between citizens and the tax administration. Overall, e-invoicing represents a crucial step towards a more efficient, fair, and modern tax system.

Ecuador has significantly increased tax revenues by diversifying its tax base, introducing temporary taxes, and digitizing fiscal processes. These measures have reduced compliance costs for taxpayers and improved administrative efficiency, facilitating voluntary adherence to the tax system.[5] Simplified procedures and integrated digital platforms have removed barriers to compliance, while data-driven targeted audits have strengthened the state’s capacity to mobilize resources sustainably.

INNOVATIONS IN TAX POLICIES IN THE REGION

Latin America has witnessed significant advances in the use of technologies to enhance the efficiency and transparency of tax administrations. One notable innovation has been Colombia's adoption of artificial intelligence (AI) in its tax processes. These tools have identified inconsistencies in tax returns by analyzing data patterns, improving the government's ability to conduct targeted audits and combat tax evasion.

Colombia stands out for its use of advanced technologies in audits and fiscal controls. According to Colombia's Ministry of Finance, the implementation of analytical tools to detect tax evasion has bolstered revenue collection, although challenges related to informality persist. A report by the DIAN highlights that "AI-based audits have increased tax revenues by 15%".[6]

In Peru, the introduction of electronic invoicing has transformed how economic transactions are tracked, establishing a reference model for other countries. This system has not only improved traceability and transparency but also reduced tax evasion by approximately 2% of GDP since its implementation in 2016.[7] These examples demonstrate how technological innovation can serve as a key catalyst for fiscal modernization in emerging economies.

Artificial intelligence has become an essential tool for improving tax collection, with applications that have demonstrated significant results in various areas. One of the most important is the detection and prevention of tax evasion. Through the analysis of large volumes of data and the use of predictive algorithms, AI makes it possible to identify irregular patterns in tax returns, making it easier to detect fraudulent companies and suspicious transactions. Likewise, its ability to cross-reference information has optimized the recovery of evaded taxes. In addition, the automation of tax processes through intelligent systems has simplified administrative tasks and improved interaction with taxpayers, making the system more efficient and accessible.

In Ecuador, tax administrations are moving towards transformation with the implementation of the Tax and Customs Administration Improvement Program, known as "Orion". This program aims to optimize the operational efficiency of the Internal Revenue Service (SRI) and the National Customs Service of Ecuador (SENAE), the main tax administrations of the country.

Through the incorporation of artificial intelligence, Orion seeks to increase voluntary compliance with tax obligations, combat tax evasion and strengthen the relationship between citizens and tax authorities. This is achieved by implementing more efficient and effective processes that promote transparency and improve interaction with taxpayers.

However, the integration of AI into tax administrations presents significant challenges from a legal point of view, particularly with regard to the modernization of regulations. The use of AI requires legal systems to adapt to regulate the use of personal data, ensure transparency in audit processes, and prevent abuses by tax authorities.

SOCIOECONOMIC FACTORS AND THEIR IMPACT ON TAX COMPLIANCE

Tax compliance in Latin America is influenced by socioeconomic and structural factors that directly affect fiscal dynamics. Variables such as per capita income, financial education, and the perception of fairness in the tax system play a crucial role in citizens' willingness to comply with their tax obligations. In emerging economies such as Ecuador and Bolivia, economic informality represents a major barrier to efficient collection, affecting approximately 60% of workers in the region, according to the ILO. This phenomenon significantly limits the tax base and perpetuates fiscal inequality.

Tax education emerges as a key tool to improve tax compliance. According to the World Bank, strengthening tax education can increase compliance levels by up to 20%.[8] Campaigns in this area not only inform taxpayers about their obligations, but also raise awareness about the positive impact of taxes on public services. In countries such as Ecuador, initiatives such as fiscal transparency portals and accountability campaigns have improved trust between taxpayers and institutions, increasing citizens' willingness to comply with their tax obligations.[9] A notable example is the Internal Revenue Service (SRI) where taxpayers can access information on the taxes assessed and paid by any individual or legal entity through the official mobile application "SRIMovil". This tool provides public access to such data without requiring login credentials, ensuring a transparent and accessible system. Additionally, the website provides public access to information on outstanding tax debts, promoting a system of accountability that encourages tax compliance.[10]

Similarly, all public institutions that manage state resources have fiscal transparency sections on their websites, as mandated by Ecuadorian law. These sections allow users to download detailed breakdowns of each entity's annual expenses, including information on salaries, contracts executed during the year, and specific details of each transaction. For instance, the Ministry of Finance Transparency[11], Ministry of Public Works[12] and Ecuadorian Institute of Social Security[13] portals enable that information.

On the other hand, tax evasion, which represents 6.1% of regional GDP according to ECLAC, generates losses estimated at more than 300,000 million dollars per year. This phenomenon, together with high informality, limits the ability of governments to finance essential services. In addition, the cost of tax compliance can be a significant barrier, especially in low-income countries, where regulatory complexity affects small taxpayers and informal sectors. To mitigate these problems, policies such as simplified regimes for microenterprises have been designed, which facilitates the transition to formality and reduces administrative burdens.

Insufficient administrative capacities also represent a significant challenge. The IDB estimates that adequate institutional strengthening could increase tax revenues by 15%. However, the implementation of more complex tax policies requires a comprehensive modernization of tax administrations. In addition, cultural and regional differences, such as limited access to tax education and digital connectivity in rural areas, make compliance difficult.

In response, administrations such as the Internal Revenue Service in Ecuador have implemented mobile and digital programs to bring tax services closer to remote communities.

Together, these factors underscore the urgent need for comprehensive strategies that combine tax education, regulatory simplification, combating evasion, and modernizing tax institutions, with the aim of building more effective, equitable, and sustainable systems in the region.[14]

CONCLUSION

Tax compliance is an essential component for ensuring fiscal sustainability and promoting inclusive development in emerging economies. Latin America has made significant progress in areas such as digitization and technological innovation, but structural challenges persist, particularly in informality, tax evasion, and the administrative capacities of tax institutions.

Ecuador and its neighbors have provided valuable examples of how to tackle these challenges. These strategies have not only increased the VAT collection ratio and improved transaction traceability but also fostered greater voluntary adherence to the tax system. To replicate these successes, countries in the region must focus their efforts on strengthening institutional capacities, investing in tax education, and fostering transparency to ensure that collected resources translate into tangible benefits for society. Ultimately, building strong tax systems will not only strengthen public finances but also enable nations in the region to advance toward greater equity, fiscal justice, and economic sustainability.

John Arias Izquierdo

[1]Tax Statistics in Latin America and the Caribbean, OECD 2024 - p. 14.
[2] Internal Revenue Service of Ecuador (SRI), Annual Report 2023, p. 45.
[3] United Nations Development Programmed 2023 for Latin America and the Caribbean, p. 10.
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[6] National Directorate of Taxes and Customs (DIAN), Results Report 2023, p. 27.
[7] National Superintendence of Customs and Tax Administration (SUNAT), Electronic Invoicing Report 2022, p. 30.
[8] World Bank, Tax Education Report 2022, p. 18.
[9] Transparency International, Public Expenditure Report 2023, p. 11.
[10] https://srienlinea.sri.gob.ec/sri-en-linea/SriPagosWeb/ConsultaDeudasFirmesImpugnadas/Consultas/consultaDeudasFirmesImpugnadas
[11] https://www.finanzas.gob.ec/transparencia/
[12] https://www.obraspublicas.gob.ec/transparencia/
[13] https://www.iess.gob.ec/transparencia/
[14] Inter-American Development Bank (IDB), Administrative Capacities Report 2023, p. 34.

AEOI STANDARD AND TAX TRANSPARENCY: A NEW POSITIVE SCENARIO FOR CURAÇAO

By Dr. Germaine Rekwest, Chair Taskforce International Tax Compliance, Ministry of Finance Curaçao.

As of February 2025, Curaçao has been removed from annex II of the 'EU list of Non-Cooperative Jurisdictions for Tax Purposes' or 'EU list'. The EU list has been established to address harmful tax competition by imposing tax standards on non-EU countries and jurisdictions. Mainly because of this initiative, the EU has managed to regain its influential role in international taxation. The list which is published to conclusions adopted by the Ecofin Council is composed of countries which have failed to fulfil their commitments to comply with tax good governance criteria within a specific timeframe, and countries which have refused to do so, the so-called 'annex I' or 'EU black list'.[1] Jurisdictions that do not yet comply with all international tax standards but have committed to implementing reforms are included in annex II: a state of play document ('EU gray list').

The three listing criteria are in short:

1. Tax transparency, which includes exchange of information with EU Member States by implementing OECD standards on Automatic Exchange of Information (AEOI) and Exchange of Information on Request (EOIR).

2. Fair taxation, which implies the idea that countries should not have harmful preferential corporate income tax measures according to the EU Code of Conduct.

3. Implementation of the OECD/G20 BEPS 'minimum standards'.

The first mentioned EU criterion ('tax transparency') is based on the OECD determination in relation to the AEOI. In the fall of 2024, the OECD published its annual update of the results of the conducted peer reviews of the legal frameworks putting into practice the AEOI Standard. The latter indicated – much to relief of Curaçao – that its legal framework implementing the AEOI Standard is in place, and it is consistent with the requirements of the AEOI Terms of Reference. For anyone closely following the AEOI developments and the annual reports, the recent removal of Curaçao from the EU list should not have come as a surprise.

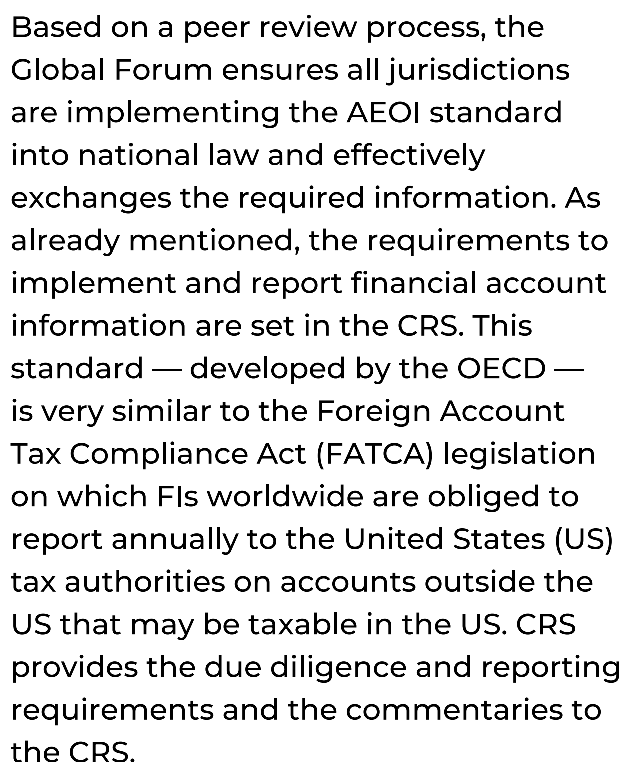
In this contribution, the author will elaborate on the recent progress Curaçao has made in advancing the implementation of CRS, both in terms of its legal framework and the effectiveness in practice. The author will highlight the strategy of Curaçao in implementing the AEOI Standards and bring forward the next steps for Curaçao. However, the essence of AEOI will be briefly flagged first.

THE STANDARD OF AUTOMATIC EXCHANGE OF FINANCIAL ACCOUNT INFORMATION

It has already been a decade since the AEOI Standard was developed by the OECD to effectively fight tax evasion worldwide. AEOI comprises of a framework for Reporting Financial Institutions (FIs) to identify reportable accounts, to collect certain information on accounts held by so-called 'reportable persons' and to report this information on an annual basis to the local tax authority. The local tax authority will then exchange the collected information with other tax authorities of participating countries of the Multilateral Competent Authority Agreement on Automatic Exchange of Information or 'MCAA', where the reportable persons are resident for tax purposes. The requirements to implement and report financial account information is provided by the so-called Common Reporting Standard (CRS).

OECD'S GLOBAL FORUM AND AEOI

The OECD's Global Forum oversees the monitoring and reviewing the implementation of the AEOI Standard. In 2014, the Global Forum members committed to implementing the AEOI Standard. By 2018, 100 countries started exchanging information and by now, 127 countries have formally committed to implement the standard.[2] By 2024, tax authorities from 111 jurisdictions have automatically exchanged information on financial accounts.[3] Information on over 134 million financial accounts was exchanged automatically in 2023, covering total assets of almost EUR 12 trillion.



Based on a peer review process, the Global Forum ensures all jurisdictions are implementing the AEOI standard into national law and effectively exchanges the required information. As already mentioned, the requirements to implement and report financial account information are set in the CRS. This standard — developed by the OECD — is very similar to the Foreign Account Tax Compliance Act (FATCA) legislation on which FIs worldwide are obliged to report annually to the United States (US) tax authorities on accounts outside the US that may be taxable in the US. CRS provides the due diligence and reporting requirements and the commentaries to the CRS.

IMPLEMENTATION OF CRS BY CURAÇAO

In 2017, Curaçao implemented the CRS in its national legislation (also known as "LB LIBB"). The LB LIBB includes the identification and reporting requirements of CRS. Based on the so-called wider approach, Curaçao is currently exchanging information with all participating countries of the MCAA.[4]
In short, the AEOI Standard is composed of four main components:

- A Model Competent Authority Agreement (Model CAA)
- The Common Reporting Standard (CRS)
- The Commentaries on the CAA and the CRS
- The CRS extensible mark-up language (SML) Schemas and related User Guides.

LEGAL FRAMEWORK

At the end of 2022, Curaçao had a negative conclusion from the OECD Global Forum's review due to issues of AEOI: the determination was "Not In Place" for CR1: Domestic legal framework. As Curaçao promptly committed to address this issue, Curaçao has been listed on a gray rather than black list since February 2023.

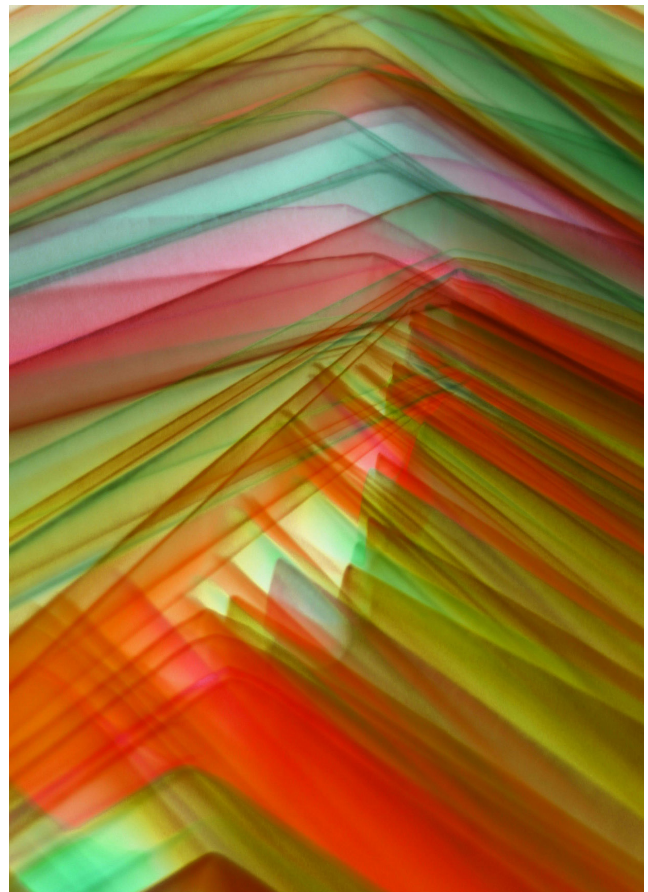
In general, any amendments made to legal frameworks by the end of June each year can be assessed by the OECD in that year with the results being published in that year's annual report of the OECD. Accordingly, Curaçao amended its legislative framework to address issues identified, the last of which was effective from 25 June 2024.

As already pointed out, the 2024 OECD report indicated that Curaçao's legal framework implementing the AEOI Standard is in place and is consistent with the requirements of the AEOI Terms of Reference. This includes Curaçao's domestic legislative framework requiring Reporting Financial Institutions to conduct the due diligence and reporting procedures (CR1) and its international legal framework to exchange the information with all of Curacao's Interested Appropriate Partners (CR2). No recommendations were made. As a result of the AEOI determination 'in place' by the OECD, Curaçao is now removed from the EU list of non-cooperative jurisdictions, Annex II or 'gray list'.

By amending its domestic legal and regulatory framework, strengthening compliance and enforcement mechanisms, including expanding relevant authorities' access powers, Curaçao is now on a very promising path. Curaçao introduced sanctions for non-compliance. Having the legal framework in place, Curaçao should now be focusing on the effectiveness in practice of this framework as it will be assessed by the OECD during the peer review process. In other words, Curaçao still needs to demonstrate to be "partially compliant or on track" during the peer review to maintain its status, that is, to be out of any list of non-cooperative jurisdiction.

IMPLEMENTATION AND EFFECTIVENESS OF THE AEOI STANDARD

The AEOI Standard requires every jurisdiction to implement an effective administrative compliance framework. To this end, Curaçao should develop a comprehensive compliance strategy, detailing the key actions officials must undertake to supervise the FIs compliance with due diligence, reporting and record-keeping obligations. Furthermore, Curaçao should ensure that all RFI's in Curaçao are correctly conducting the due diligence procedures and are reporting the relevant information. In practice, the Tax Inspectorate and the Stichting Belastingaccountantsbureau (SBAB) oversee the auditing of the FI's to verify if RFI's are compliant with the reporting and due diligence procedures. On top of that, the Tax Inspectorate is responsible for promoting voluntary compliance through, among other things, awareness-raising and educational activities.



Jurisdictions, like Curaçao, that have been rated as "non-compliant" during the initial "effectiveness peer review" will not receive an onsite visit as part of the peer review of their ongoing implementation of the AEOI Standard until they demonstrate, through an updated Administrative Compliance Framework Questionnaire (ACFQ) along with follow-up conversations as necessary, that they would be expected to be rated either as "partially compliant or on track" during the initial effectiveness peer review. The reason for this is that carrying out an onsite visit to a jurisdiction that either does not have complete policies and procedures in place or that is severely constrained by gaps in its legal frameworks, will not be worthwhile as they will most likely be unable to demonstrate the effectiveness of their implementation of "Core Requirement 1" in any case.

If a jurisdiction does not qualify for an onsite visit in time to meet the calendar of assessments under the second round AEOI effectiveness reviews (which ends in Q2 2025), it may still qualify for an onsite visit up until Q2 2026 at the latest. Therefore, jurisdictions have been granted another year extension to demonstrate the effectiveness of their implementation of "Core Requirement 1".[5]

Having a robust legal framework in place (phase I) as of 2024, Curaçao has now shifted its focus to the effectiveness of its compliance framework (phase II) by conducting compliance activities, onsite as well as desk-based audits to verify whether FIs are practically complying with their obligations under the CRS.

FINAL COMMENTS

It is fair to say that Curaçao has made some big leaps to comply with the AEOI standards. Surely, Curaçao has benefitted from the tailored bilateral technical assistance on CRS administrative compliance provided by the Secretariat of the OECD Global Forum. The administrative compliance framework and strategy of Curaçao are currently being updated and adjusted according to the AEOI standards and the CRS framework as set out by the Global Forum of the OECD.

Although the implementation strategy in Curaçao is ongoing, it will be challenging to demonstrate the full compliance with a stable and effective implementation. The capacity restraints are a critical aspect, and it will remain a significant challenge for small jurisdictions to keep up with compliance of the international AEOI standards. Even so, by addressing several recommendations made in the first-round review, it is expected that Curaçao will make some big steps in implementing its compliance strategy. In view of its efforts, it is likely that Curaçao receives a rating higher than "non-compliant". Yet, it is important to stress that receiving such a rating should not result in complacency and inactivity. For sure, it is essential that Curaçao also start using the information received under CRS to fight tax evasion and avoidance, as well as to promote domestic resource mobilization. More importantly, CRS should remain an integral and sustainable part of Curaçao's strategy to comply with the international tax standards, especially to maintain its status out of the EU list of non-cooperative jurisdictions for tax purposes. A promising future without any doubts.

Germaine Rekwest

[1] https://www.consilium.europa.eu/en/policies/eu-list-of-non-cooperative-jurisdictions/
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