

Current & Quotable



OECD Funding: Setting the Record Straight

by Daniel J. Mitchell

Daniel J. Mitchell is the McKenna Senior Fellow in Political Economy at The Heritage Foundation.

The following was originally published in CF&P Talking Points — A Policy Analysis From the Center for Freedom and Prosperity Foundation (<http://www.freedomandprosperity.org>), October 2006.

Background

The Organisation for Economic Co-operation and Development (OECD) is an international bureaucracy based in Paris with an annual budget of about \$400 million, approximately one-fourth of which is financed by American taxpayers. Founded in the early 1960s and ostensibly representing the interests of 30 developed nations, for much of its history the OECD focused on collecting statistics and publishing innocuous studies.

In the mid-1990s, the OECD abandoned its traditional mission and launched a “harmful tax competition” project to make it easier for governments to impose high tax rates and to hinder the flow of capital from high-tax to low-tax nations. Elements of the project included a list of supposedly improper tax provisions in member nations and a blacklist of selected non-member nations — including a threat to subject these jurisdictions to financial protectionism. The project was designed — and still is pursued

— to advance the interests of high-tax nations. Indeed, the OECD openly stated that:

- Tax competition “may hamper the application of progressive tax rates and the achievement of redistributive goals.”¹
- Low-tax policies “unfairly erode the tax bases of other countries and distort the location of capital and services.”²

American policy makers have expressed dissatisfaction with the OECD’s project. Treasury Secretary Paul O’Neill in 2001 stated, “I share many of the serious concerns that have been expressed recently about the direction of the OECD initiative. I am troubled by the underlying premise that low tax rates are somehow suspect and by the notion that any country, or group of countries, should interfere in any other country’s decision about how to structure its own tax system. I also am concerned about the potentially unfair treatment of some non-OECD

¹Organisation for Economic Co-operation and Development, “Harmful Tax Competition: An Emerging Global Issue,” 1998. See also <http://www.oecd.org/dataoecd/33/0/1904176.pdf>.

²Organisation for Economic Co-operation and Development, “Towards Global Tax Co-operation: Progress in Identifying and Eliminating Harmful Tax Practices,” Report to the 2000 Ministerial Council Meeting and Recommendations by the Committee on Fiscal Affairs, 2000, at <http://www.oecd.org/dataoecd/9/61/2090192.pdf>.

countries. The United States does not support efforts to dictate to any country what its own tax rates or tax system should be, and will not participate in any initiative to harmonize world tax systems. The United States simply has no interest in stifling the competition that forces governments — like businesses — to create efficiencies.”³

Congress also has warned the OECD about its efforts to hinder tax competition, including the following language in the Conference Report for the FY2006 funding bill: “The conferees remain concerned with proposals by international organizations to interfere with the sovereign right of jurisdictions to pursue low-tax policies and direct the Department of State to consider such behavior when reporting whether continued participation in that international organization serves the interests of the United States.”⁴

The Case for Tax Competition

Labor and capital are increasingly mobile and this facilitates the flow of productive resources to more fiscally responsible jurisdictions. This has encouraged many nations to lower tax rates. Over the last 25 years, first triggered by the Reagan tax rate reductions, the top personal income tax rate in industrialized countries has fallen by an average of more than 22 percentage points since 1980. The corporate rate also has fallen dramatically — by almost 20 percentage points.

Politicians from uncompetitive, high-tax welfare states do not like the liberalizing impact of tax competition, but many U.S. officials are appropriately skeptical of “one-size-fits-all” harmonization schemes. John Bolton, currently serving as America’s Ambassador to the United Nations, wrote that this approach, “. . . represents a kind of worldwide cartelization of governments and interest groups. . . . The costs to the United States — reduced constitutional autonomy, impaired popular sovereignty, reduction of our international power, and limitations on our domestic and foreign policy options and solutions — are far too great, and the current understanding of these costs far too limited to be acceptable.”⁵

Several Nobel Prize winners have commented specifically on tax competition. James Buchanan points out that “. . . the intergovernmental competition that a genuinely federal structure offers may

be constitutionally ‘efficient’ . . .” and that “. . . tax competition among separate units . . . is an objective to be sought in its own right.”⁶ Milton Friedman, meanwhile, writes, “Competition among national governments in the public services they provide and in the taxes they impose is every bit as productive as competition among individuals or enterprises in the goods and services they offer for sale and the prices at which they offer them.”⁷ And Gary Becker observed that “. . . competition among nations tends to produce a race to the top rather than to the bottom by limiting the ability of powerful and voracious groups and politicians in each nation to impose their will at the expense of the interests of the vast majority of their populations.”⁸

Interestingly, even OECD economists admit that tax competition is desirable, writing that “[T]he ability to choose the location of economic activity offsets shortcomings in government budgeting processes, limiting a tendency to spend and tax excessively.” It does not try to scapegoat so-called tax havens. Instead, this bureaucracy says the real problem is bad tax policy. It explains that, “[I]llegal tax evasion can be contained by better enforcement of tax codes. But the root of the problem appears in many cases to be high tax rates.”⁹

Responding to OECD Talking Points

Talking points generated by the OECD, echoed by groups such as the United States Council for International Business, assert that the Paris-based bureaucracy somehow plays a crucial role in the enforcement of U.S. tax law. This is false, but irrelevant. The Senate-approved language does not restrict the OECD’s benign work on issues such as tax treaties and transfer pricing. The Senate language merely restricts the OECD from using American tax dollars to interfere with tax competition and national sovereignty. More specifically:

Q: Does the OECD’s tax work help U.S. interests by facilitating tax treaties?

A: Defenders of the OECD imply that America’s network of 57 tax treaties somehow is dependent on the OECD’s Model Tax Convention. This is false.

⁶Geoffrey Brennan and James Buchanan (1980), *The Power to Tax: Analytical Foundations of a Fiscal Constitution* (Cambridge University Press: Cambridge).

⁷Letter to Center for Freedom and Prosperity, 2001. Available at <http://www.freedomandprosperity.org/update/u05-15-01/u05-15-01.shtml#3>.

⁸Gary Becker, “What’s Wrong with a Centralized Europe? Plenty,” *Business Week*, June 29, 1998.

⁹Organisation for Economic Co-operation and Development, *Economic Outlook*, June 17, 1998. Available at <http://www.oecd.org/dataoecd/50/17/2088806.pdf>.

³Available at <http://www.treas.gov/press/releases/po366.htm>.

⁴Available at http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=109_cong_reports&docid=f:hr272.109.pdf.

⁵John R. Bolton, “Should We Take Global Governance Seriously?” *Chicago Journal of International Law*, 2000.

The U.S. Treasury has ample knowledge and ability to negotiate and monitor tax treaties without assistance from the OECD.¹⁰ Indeed, it is more accurate to state that the OECD relied on the U.S. when it developed its Model Tax Convention. In any event, the Senate-approved language merely restricts the use of funds for efforts to hinder tax competition.

Q: Does the OECD's anti-tax competition project help enforce U.S. tax law by facilitating the collection of information?

A: Defenders of the OECD imply that the American government somehow would be unable to enforce U.S. tax law without the OECD's anti-tax competition effort. This is false. Studies by experts show that the U.S. has the least amount of tax evasion of any nation.¹¹ Moreover, the United States has entered into Tax Information Exchange Agreements with many so-called tax havens without having to rely on or utilize the OECD.

Q: Does the OECD help enforce U.S. transfer pricing rules?

A: The IRS has transfer pricing rules to prevent companies from using cross-border sales to subsid-

iaries and/or branches to artificially boost profits in nations where tax rates are low and/or artificially boost costs in nations where tax rates are high. Defenders of the OECD imply that the IRS's transfer pricing work somehow depends on the OECD. This is false. The U.S. Treasury has ample knowledge and ability to implement and monitor transfer pricing rules without relying on the OECD.¹² In any event, the Senate-approved language merely restricts the use of funds for efforts to hinder tax competition.

Q: Does the OECD's anti-tax competition project reflect U.S. policy and include U.S. participation?

A: The OECD claims it has ongoing authority to fight tax competition based on decisions made in the 1990s when America has a different Administration with a different approach to tax matters. Treasury Department officials do participate in OECD meetings, and they periodically express support for tax harmonization schemes, but the views of these bureaucrats presumably do not trump the pro-tax competition views expressed by Treasury Secretary Paul O'Neill or the many pro-tax competition statements and actions by the White House. ◆

¹⁰<http://www.treas.gov/press/releases/js4001.htm>.

¹¹http://www.econ.jku.at/Schneider/ShadEconomyCorruption_2006_Pickhardt.pdf.

¹²<http://www.treas.gov/offices/tax-policy/library/ota61.pdf>.