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Committee on Financing for Development in the States Members of the Economic and Social Commission for Western Asia
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Item 6 (b) of the provisional agenda

Arab Financing for Development Scorecard

Domestic public resources

Summary

Taxation is a key ingredient for effective fiscal policy (given its redistributive role and influence on changing production and consumption patterns) and for domestic public resource mobilization (given its revenue creation potential and use in financing social public investments). Both policy strands shape a country's intertemporal budget constraints, and influences the design of medium-term revenue and expenditure strategies. Taxes are a key means of financing the 2030 Agenda for Sustainable Development, and play a major role in influencing growth, fiscal space, and structural transformation. How different tax instruments are designed, tax policies are enacted, tax codes are enforced, and taxes are collected define a country's fiscal space, the efficiency of its public financial management, and the credibility of its budget execution, all of which provide building blocks to forge integrated national financing frameworks that restore resilience and sustain the pursuit towards achieving national sustainable development priorities. Taxation is all the more crucial since other sources of financing have not been channelled to the Arab region at the scale or pace necessary to achieve the 2030 Agenda, based on the financing compact advanced in the Addis Ababa Action Agenda.

The present document provides an overview of trends, challenges and opportunities to raise domestic public resource mobilization in the Arab region. It assesses the region's untapped tax potentials, tax gaps and tax leakages, and puts forward a 25-point Arab tax reform agenda to fulfil the commitment of transposing Arab tax systems to become more fair, progressive, equitable and efficient in a manner that reduces lost financing opportunities associated with tax abuse.

The Committee on Financing for Development in the States Members of the Economic and Social Commission for Western Asia is invited to take note of the recommendations set out in the present document, and endorse the proposed reform actions.

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Introduction

1. The mobilization and use of public resources have long been the subject of both interest and contention. Interest in these two contrasting policy domains stems from their roles in framing Governments' intertemporal budget constraints. The contention lies in the important roles assigned to domestic public resources (considered the prime means of financing the 2030 Agenda for Sustainable Development) at a time when developing countries face severe limitations in raising domestic revenues, as a result of persistent fiscal deficits aggravated by debt repayment sapping over two thirds of their budgets, in some cases. In contrast, international finance, both public and private, has neither been channelled nor scaled up at the pace needed to bridge the "great finance divide" responsible for the major sustainable development setbacks in the Global South.

2. Governments generate domestic public resources (in terms of sources, instruments and regulations) and deploy them (through credible budgets, transparent procurement procedures, and pro-poor policies) to provide social protection and targeted subsidies, support the delivery of quality public goods, and achieve redistributive aims. These methods have been subject to increased scrutiny, especially given the fast-approaching midway point of the 2030 deadline with considerable shortfalls in realizing the transformative change set out in the 2030 Agenda, on the basis of the financing compact advanced in the Addis Ababa Action Agenda.

3. The fallout from the COVID-19 pandemic and the war in Ukraine, along with a global drive towards economic rationalization, fiscal consolidation, monetary tightening, and shortfalls in meeting development finance commitments (including financing climate adaptation and mitigation, and loss and damage) has severely strained the financing for development agenda, especially in the Global South that continues to face subdued growth, inflation, and debt overhangs. Consequently, there have been renewed calls for prudent public financial management; budget credibility; fair, efficient and equitable taxation; innovative and responsible public investment aligned with the Sustainable Development Goals (SDGs); improved public procurement; reconciled tax expenditures; and international collaboration to end public revenue leakages associated with the cross-border movement of illicit financial flows.

4. In this context, taxation emerges as a key component for fiscal policy design and budget execution. As the prime determinant of domestic public resource mobilization capacity, taxation defines a country's fiscal space and potential to finance its national sustainable development ambitions. Taxes serve as agents to deliver public goods; redistribute wealth; achieve societal equity; and create incentives to influence production, consumption and investment patterns, and act as automatic stabilizers for the economy. Today, the design of tax policies and their enforcement no longer follow the linear demarcations that once separated international from national policymaking. Equally, under conditions of increasing digitization and capital mobility, a country's tax sovereignty is no longer confined to its traditional geographic boundaries.

5. In 2015, the Arab region vowed to improve the fairness, efficiency and effectiveness of tax systems. Several tax reforms have been enacted since then but, for the most part, they have fallen short of improving tax equity and progressivity, and have not spurred the desired increase in public revenues, not least due to significant distortions that continue to undermine the integrity of Arab tax systems. Equally, the international tax architecture has been less than ideal in supporting domestic resource mobilization capacity, while the global financial system remains mired in short-termism, and is crisis-prone thus exacerbating inequalities both within and across countries, adding several financing rifts to the funding shortfalls faced by Arab economies.

6. The present document provides an updated assessment of the trends, challenges and potential opportunities to enhance domestic public resource mobilization. A special focus is given to the role of taxation in sustaining high and inclusive growth levels, structural transformation and fiscal discipline, and in forging credible budgets based on medium-term revenue and expenditure strategies. This is part of ESCWA efforts to advance evidence-based integrated national financing frameworks to weather the current polycrises and tackle the socioeconomic and environmental infractions confronting the Arab region as it approaches the midway point to 2030.

I. Global trends versus regional realities

A. Domestic public resources: a recipe for inclusive growth, structural change, fiscal discipline, and budget credibility

7. Growth and public revenues: The Addis Agenda recognizes that domestic public resources are primarily generated through economic growth, and that tax policies are crucial to ensure that gains from growth and public revenues are expensed equitably. This interplay between growth and taxes is based in economic theory, which suggests that as output expands, employment levels rise, and individuals and businesses generate more taxable income/profits. In practice, however, these links are obscured by sluggish transmission mechanisms, and their efficacy remains contingent on the ability to safeguard against the slippage of productive capacity into informality (which erodes the tax net), the ability to reduce tax abuse (which erodes the tax base), and the ability to raise tax buoyancy (the reaction of tax revenues to changes in national income and to discretionary changes in tax policies).

8. In that regard, the global context is characterized by the following:

- The global economy has been negatively affected by a series of mutually reinforcing polycrises, which could lead to the de-acceleration of growth by a forecasted 40 per cent in 2023.[1] In just two years, an estimated $2.9 trillion have been added to the global SDG-financing gap (twice the losses in global output). In tandem, both the pandemic and the war in Ukraine have thus far added 6 per cent, or an estimated $350 billion, to the Arab SDG-financing gap.
- With marked and persistent inflation (even prior to the triple food, fuel and climate crises), monetary tightening will continue until interest rate hikes dampen demand-side core inflation. In the meantime, counter-cyclical fiscal and tax policy measures to support growth and social aims require careful crafting to avoid offsetting the impact of monetary tightening (fiscal-monetary policy reaction).
- In the interim, countries seeking to stifle demand may see household incomes erode, borrowing costs increase, domestic private investment become risk averse, and real wage growth turn negative. These conditions risk triggering a vicious cycle of weak growth, low domestic public resource mobilization capacity, and unsustainable debt and austerity, with setbacks to critical public spending exacerbating SDG-financing gaps and turning the great finance divide into a lasting sustainable development divide and a crisis in global trust and solidarity. Consequently, the United Nations Secretary-General's SDG Stimulus to Deliver Agenda 2030 aims to strengthen development cooperation and SDG investments, reform the international financial architecture, and enact reforms to accelerate growth and raise public revenues for sustainable development.
- Moreover, while the growth forecasts of countries of the Organisation for Economic Co-operation and Development (OECD) have been revised upwards, they may swiftly see a rebound in public revenues as they maintain above parity tax buoyancy (implying that a 1 per cent increase in gross domestic product (GDP) leads to a more than commensurate rise in tax revenues). In contrast, many developing countries have lagged in realizing such parity due to several factors, including tax and institutional quality, low enforcement capacity, tax code complexity, and excessive tax expenditures enacted to make up for inherent structural deficiencies in attracting direct investments.

9. The Arab region is characterized by the following:

- Current levels of public revenues in the Arab region neither match the scale of SDG investments needed nor their long-term sustainability horizons. Revenues as a share of GDP have witnessed an overall decline since 2008, and this trend has been amplified by the pandemic, exacerbating pre-existing SDG-financing gaps in the region above the previously reported $6 trillion by 2030.

[1] United Nations, World Economic Situation and Prospects, 2023.

- Aggregate growth forecasts for the region are expected to hover at around 3.4 per cent in 2024, with inflationary pressures easing in following years. In the interim, oil abundant economies could benefit from an exceptional oil price rally to shore up reserves and recapitalize sovereign wealth funds, thereby offering opportunities to diversify their revenue streams through direct forms of taxation to limit vulnerabilities to future oil price fluctuations, and revisit their investment strategies going forward.
- Nonetheless, middle-income and least-developed oil and net food importing Arab economies would witness exacerbated socioeconomic challenges amid rising energy import bills, food supply shortages, and drops in tourism receipts and international private inflows, adding to the capital outflows that put pressure on their currencies in the first place. A delicate balance needs to be struck to rein in inflation and ensure fiscal sustainability under high debt burdens, while expanding public spending (but towards productive investments) and ensuring that both fiscal and monetary policies work in the same direction to influence aggregate demand and production patterns (transformation) in a manner that triggers a cycle of high sustained growth and tax revenues (tax buoyancy).
- Arab countries generally exhibit low tax buoyancy and suboptimal growth. While the latter is an indispensable condition, it remains insufficient on its own to realize domestic resource mobilization potentials. By altering the traditional drivers of GDP, structural transformation can yield higher growth levels. Equally, for growth gains to benefit different segments of the society, taxation needs to be progressive and efficient, exhibiting high tax buoyancy. Hence, the need to reduce incentives for informal productive capacity to slip into informality, to reconsider rentier dispositions, tax expenditures, multiple tax rates and exemptions (tax expenditures have equivalent incentive effects as direct subsidies or transfers to individuals, and the budgetary impact of these measures is similar to direct spending, as less public resources are available to fund other government priorities), and to ensure the taxation of high net-worth individuals and end corporate tax abuse.

10. Fiscal policy: The Addis Agenda highlights the international community's recognition of the importance of progressive tax systems, efficient tax collection, and prudent and targeted public social expenditures to maintain fiscal discipline and achieve growth, macroeconomic stability and other important social and distributional aims. Progressive taxes can spur consumption and increase the tax base by creating opportunities for redistributive fiscal policies to promote job creation, increase wages and reduce poverty. Efficient tax systems ensure that the cost of mobilizing domestic public resources exceeds the social and deadweight losses of tax collection (higher losses are incurred the more responsive the tax base is to effective tax rates), especially in contexts where tax revenues are leaked out of national systems as a result of tax evasion, profit shifting, and aggressive tax planning, to name a few.

11. In that regard, the global context is characterized by the following:

- Over two thirds of countries witnessed significant declines in public revenue as a share of GDP following the outbreak of the pandemic in 2020. Revenue losses amounting to $150 billion have been reported, as tax relief measures were enacted to support individuals and businesses. Tax revenues have since recovered asymmetrically, with many developing economies lagging owing to their reliance on consumption-based taxes whose quick revenue-generating potentials have been impaired by successive lockdowns and mobility restrictions, and more recently by synchronized increases in interest rates.
- The combination of subdued tax collection coupled with increased public spending on social protection, furlough (including informal and precarious workers), and food and energy subsidies caused fiscal deficits to soar. Loose fiscal policies have been largely consistent with quantitative easing policies that resulted in prolonged periods of negative interest rates, which stimulated borrowing (under increased conditions of capital mobility), and reduced intensive margins of direct investments (the decision to raise a firm's equity engagement in existing markets by increasing

investments, expanding production, or introducing new products) and consequently corporate taxable income.

- Tax collection tends to be higher in countries that have higher social expenditures/investments, implying better public service provisions on health and education. A focus on raising revenues (by merely raising statutory tax rates) may lead to resentment or higher tax non-compliance, unless it is accompanied by the provision of quality public services that reinforces trust in Governments and creates “buy in” among taxpayers. Failure to provide quality public goods and services owing to a lack of or inefficient public spending in social areas often leads to low tax morale, tax non-compliance and higher incidences of tax abuse, leading to tax-base erosion.

- Rationalizing inefficient subsidies that encourage wasteful consumption is another policy domain that requires action, in accordance with the Addis Agenda. According to the Inter-Agency Task Force (IATF) on Financing for Development, there is a need to rethink agricultural subsidies, by decoupling support from prices and production. Current agricultural subsidies distort food prices and degrade the environment. These subsidies amount to approximately $540 billion per year, or an estimated $1.8 trillion by 2030. Most agricultural support is concentrated on emission-intensive commodities or unhealthy products like sugar, and border entry price measures and subsidies are the primary forms of support. However, rationalizing or introducing subsidies remains bound by multilateral trade disciplines that have allowed various forms of agricultural support to be maintained in the first place.

- Taxes provide effective tools to change consumption and production patterns, notably in the case of fossil fuels. In the current global context, focus has shifted towards taxing windfall profits (profits that arise from unanticipated oil price hikes unaffected by investment decisions, considered a form of economic rent). Taxing windfall fossil-fuel profits was advanced by IATF through its 2023 flagship publication in reaction to a surge in hydrocarbon profits realized by corporates operating in extractive, refining and distribution industries. According to IATF, taxing these profits can help to offset the negative effects of high fuel prices on consumers (as taxation in this case targets economic rents rather than economic activity) and on the environment, while also providing Governments with additional revenue to support sustainable energy and other public goals.

- The efficient mobilization of public revenues is contingent on the ability to curb illicit financial flows, including tax-based revenue leakages. Different tax systems/instruments are prone to distinct forms of tax abuse. Indirect taxes such as trade taxes can quickly generate revenues, but may provoke counterfeit and carousel trade, effectively undercutting potential revenues accrued from these taxes. Tariffs or other fiscal charges with equivalent effects on trade may provoke tax fraud and trade misinvoicing. Excise taxes and other border taxes may score high on equity, but not when they are set higher than adjacent jurisdictions, as this creates incentives for smuggling and contraband. Exemptions on broad-based consumption taxes can provoke tax non-compliance, raise the cost of enforcement, and increase incentives for tax evasion. Highly progressive direct income taxes may score high on equity but are not necessarily efficient, as the high marginal tax rate may prompt top earners to shield or shift their wealth to avoid tax liability. Experience shows that even the most admirable tax structures on paper are of little value if inefficiently administered, or if enforcement is undermined by significant tax leakages.

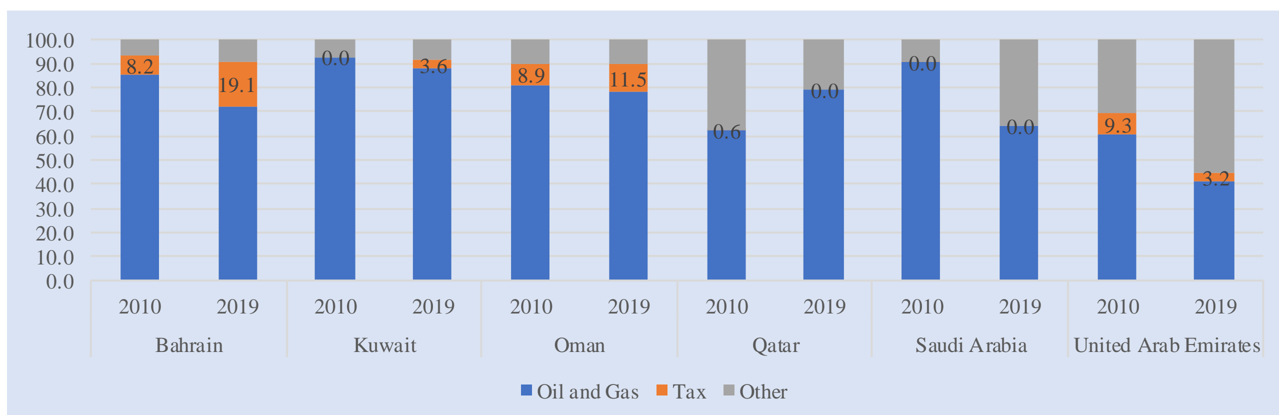
- Budget credibility (or Governments’ ability to accurately and consistently meet expenditure and revenue targets) is another important, and sometimes overlooked, factor in maintaining fiscal discipline, sustaining SDG-relevant fiscal space, and ensuring that both revenues and expenditures are aligned to achieve optimal SDG progress under intertemporal budget and tax revenue constraints.

12. The Arab region is characterized by the following:

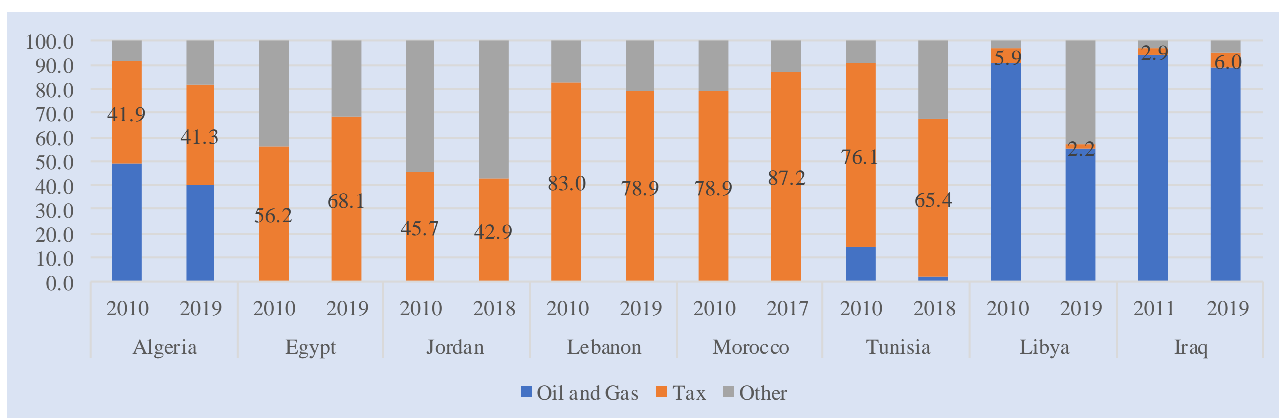
- The region has been grappling with recurring episodes of fiscal deficits, which can be traced back to unsustainable, volatile or subdued revenue streams, or a combination thereof. The situation has been aggravated by growing socioeconomic pressures, which necessitated higher public spending to advance human and physical social infrastructure. In response to the pandemic, Arab Governments implemented fiscal stimulus packages amounting to $100 billion, leading to a fiscal deficit of 9 per cent of GDP in 2020, and 19 of the 22 Arab countries increased or introduced subsidies on either/or both food and energy. Tax exemptions were enacted to support individuals and businesses, which further lowered the total revenues as a share of GDP by 3 percentage points to 27 per cent in 2020. However, the 2022 oil price hikes boosted the Gulf Cooperation Council's (GCC) primary balances. This surplus enabled GCC countries to reduce their debt-to-GDP ratio by 7 percentage points, from 37.4 per cent in 2021 to 30.2 per cent in 2022. Conversely, middle-income and low-income Arab countries experienced fiscal deficits, seeing their debt-to-GDP ratio increasing by 21 per cent to reach 90 per cent.
- Sources of public revenues widely differ among Arab countries owing to differences in natural resource endowment, economic structure, and asymmetries in income and development levels. For resource abundant economies, public revenues are predominantly accrued from the sale of oil and gas. Only after the 2014 oil price plunge have credible attempts been pursued by the GCC to diversify the tax base by introducing value added taxes (VAT) and excise taxes. Middle-income Arab countries (MICs) have generally relied on consumption-based taxes and excises, while least developed countries (LDCs) on taxes and grants (figure).

Sources of public revenues in the Arab region (Percentage of total revenues)

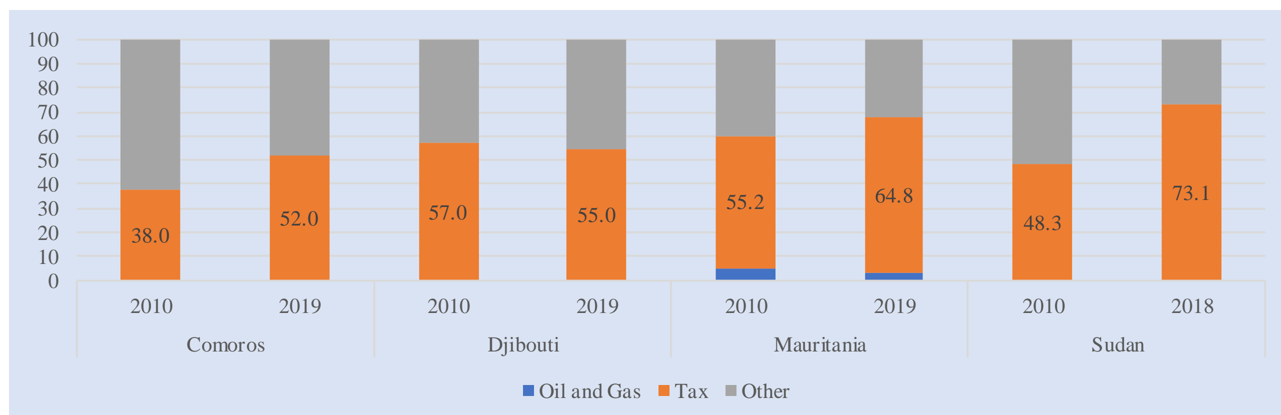
A. GCC



B. MICs



C. LDCs



Source: ESCWA based on national data, and IMF.

- Tax revenues make up 25 per cent of total revenues in developed economies, and 18 per cent in the world's middle-income and low-income economies. Tax revenues in Arab MICs constitute 19 per cent of GDP compared with a meagre 7 per cent for LDCs, and 1.5 per cent for conflict-affected countries. Overall, Arab MICs median taxes as a share of GDP reached 16 per cent compared with 25 per cent in developed economies worldwide. Arab dependence on indirect taxation points to the regressive nature of tax systems, while low tax collection points to multiple and overlapping tax exemptions, deductibles, tax evasion and non-compliance. Despite several reforms, personal income tax revenues remain low, and corporate tax revenues have not shown significant improvements, which may be attributable to weak enforcement and tax evasion. Wealth taxes remain negligible, despite the high concentration of wealth among the top decile of income earners.
- On the issue of windfall taxes, several challenges arise when considering the practicality of enacting windfall taxation as a permanent component in the tax mix. Policymakers need to consider a-priori whether windfall profits are a result of ordinary fluctuations in oil markets or otherwise; whether the tax would target upstream extraction or downstream products and services; whether production sharing and concession agreements in place with foreign extractive companies contain a "stabilization clause", which prevents the host State from changing the regulatory or tax environment, or otherwise risk being exposed to litigation; whether a windfall tax would exacerbate corporate profit shifting; and whether windfall taxes can be linked to the development of clean energy. In general, extractive industries involve a significant State-owned enterprise footprint. Hence, windfall profits would also accrue to the public sector, and the imposition of taxes may be less relevant.

B. Accounting for the unaccounted: tax revenue potentials and leakages

13. The following are the tax revenue potentials and leakages in the Arab region:

- Tax abuse: The region loses an estimated $8.9 billion in annual revenues owing to corporate tax abuse.[2]
- Tax competition: The region lost $50 billion in tax revenues[3] in the period 1980–2020 due to international tax competition, as statutory corporate income tax rates fell by almost half to match faltering global corporate taxes.

[2] Tax Justice Network, State of Tax Justice Report, 2021.

[3] ESCWA calculations based on IMF, Spillovers in international corporate taxation, 2014.

- Tax gap: The difference between actual and potential tax collection (tax gap) in the Arab region amounts on average to 15 per cent of non-oil GDP (for hydrocarbon-exporting Arab countries) and to 17.9 per cent of GDP (for hydrocarbon-importing countries).
- Tax incentives: Generous tax incentives awarded to attract foreign direct investments undercut the region's corporate tax revenue potentials by 60 per cent on average,[4] without rendering commensurate increases in multinational corporations' (MNC) activity in the region.
- Double non-taxation: On average, 69 cents on every dollar invested in the region[5] was repatriated untaxed as passive income on foreign direct investment (FDI) out of the region (2012–2019). This figure stands in contrast to the 46 cents that OECD countries gain on every dollar they invest abroad. Between 2011 and 2019, the Arab region returned $1.5 on every dollar gained in FDI inflows,[6] effectively turning the region into a net exporter of capital (globally, an estimated $15 trillion in phantom investments[7] have been channelled to shell companies, including in some of the region's financial centres).
- Tax preferences/efficiency: A third of MNCs operating in the Arab region are taxed below the proposed global minimum effective tax rate of 15 per cent.[8] Bahrain and Lebanon account for the highest share of undertaxed MNCs, reaching 50 per cent of MNCs operating in their jurisdictions.
- Tax revenue potentials: The region could have generated $2.3 billion in additional corporate tax revenues had the proposed global minimum effective tax rate been applied to under-taxed MNCs in 2019.[9]
- Rationalizing tax expenditures: Increasing average effective corporate tax rates (AETRs) to match the GloBe proposal could have generated up to $9 billion in additional tax revenues for the Arab region in 2020.[10] Higher AETRs can be realized by rationalizing tax exemptions, implementing dual tax treatment/economic zones, and curbing profit shifting.
- Trade-based illicit financial flows: Arab economies fall prey to at least $60–$77.5 billion per year in damages due to illicit financial flows associated with four types of trade misinvoicing and mis-declaration. In other words, for every $1 the Arab region gained in financing, it correspondingly lost $1.05 as illicit financial outflows. By 2020, illicit financial flows exceeded the combined aggregates of both official development assistance and FDI flowing into Arab countries (estimated at $50.5 billion in 2020).[11]
- Untaxed private wealth: Globally, $7.6 trillion of untaxed private wealth is hidden in tax havens,[12] but this figure may have risen following the pandemic, with a $5 trillion increase in the wealth of the world's richest in 2021. In the Arab region, the wealthiest 10 per cent now control 81 per cent of the region's net wealth (up from 75 per cent pre-pandemic). Moreover, the wealthiest 1 per cent in the region hold an estimated $2.6 trillion in personal wealth, where a 1 per cent annual tax on this wealth would raise enough funds to eradicate extreme poverty in the region.

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[4] ESCWA calculations based on the Orbis database; and Tax Foundation, Corporate Tax Rates around the World, 2022.

[5] ESCWA calculations based on data from IMF, Balance of payments and international investment position statistics.

[6] Ibid.

[7] IMF, What Is real and what is not in the global FDI network?, 2019.

[8] ESCWA calculations based on data from the Orbis database.

[9] Ibid.

[10] Ibid.

[11] ESCWA, Illicit financial flows in the Arab region, 2018.

[12] Gabriel Zucman, *The Hidden Wealth of Nations*, 2021.

II. Way forward: a 25-point Arab tax reform agenda

14. Arab Governments have implemented several tax reforms, some pointing in the right direction in terms of improving the fairness, efficiency and intactness of Arab tax systems. However, further qualitative reforms are needed to make tax systems more progressive, transparent and more diversified.

15. The following recommendations are presented at the national, regional and global levels, forming an integral tax reform agenda for the Arab region. The recommendations are not a "one size fits all" across countries, given the diversity in tax administration and enforcement capacities. Experience shows that even the most admirable tax structures on paper are of little value if the enforcement costs are higher than the yields from increased compliance. It is therefore critical to ensure that the marginal yields of compliance remain higher than the social cost of taxation and associated deadweight losses.

16. At the national level**,** the following salient reforms need to be considered:

(a) Redesign tax brackets to reduce the tax burden on low-income earners, avoid having more productive capacity slip into informality, and capture non-wage earnings and high net worth individual income streams to broaden the tax base and enhance the compliance and fairness of direct taxes;

(b) Rationalize overlapping or multiple tax exemptions, including direct income taxes and indirect taxes on goods and services, to improve tax compliance and value-added tax efficiency;

(c) Ensure that tax expenditures and holidays are consistently applied, quantified and made conditional on achieving defined development targets, with the possibility of replacing them by direct transfers to the extent admissible by multilateral and preferential arrangements. Rationalizing tax incentives and simplifying their codes may have a positive influence on raising tax buoyancy. However, aggregate tax buoyancy assessments need to be complemented with granular ones by type of tax. For example, the assessment of tax buoyancy in Egypt revealed that an increase in GDP does not result in a proportionate growth in tax revenue. However, distinct behavioural reactions of the different types of direct and indirect taxes provide further insight. Personal income tax revenues breached parity, outpacing growth. Consumption-based VAT buoyancy for goods and services increased by a higher pace than output. However, corporate income tax revenue buoyancy remained by far less responsive to growth, suggesting the existence of several distortions associated with corporate tax collection, enforcement and compliance;

(d) Tap niche financial market products and investors, as small tax changes on capital gains, dividends and interest income tax can generate significant revenues with minimal distortion to social imbalances;

(e) Re-evaluate the design and structure of tax systems, which may involve considering the introduction of property or wealth taxes. This should aim to enhance equity and social justice, while also emphasizing the importance of accurate asset valuation to support fiscal policy and appreciate the risk of capital flight;

(f) Strengthen tax administration, enforcement/collection and transparency by improving tax and customs administration, simplifying coding and regulation, and investing in digital technology to improve transparency in tax collection and reporting;

(g) Clamp down on cross-border tax evasion and tax avoidance, which requires a number of legislative and policy reforms following the review of tax and investment treaties to restore taxing rights and permanent establishment requirements, and redefine digital presence and taxation;

(h) Reassess how extractive industries are taxed, be it through royalties, windfall taxes on profits, withholding taxes, corporate income taxes, production sharing agreements, tariffs and licensing fees, and consider ways to effectively tax capital gains and reduce overlapping deductibles;

(i) Improve tax data and its availability for policy analysis towards better monitoring of the socioeconomic consequences of tax reforms. In each country, the Ministry of Finance must consider hosting a dedicated tax analysis unit that can support such research and analysis;

(j) Capitalize on the ESCWA Artificial Integrated Budget Intelligence Toolkit (i-BiT) to advance budget credibility and enhance the impact of public spending to achieve optimal SDG progress, including by forging evidence-based integrated national financing frameworks;

(k) Consider carbon taxes and import tariffs. Carbon taxes are recognized as a critical tool for discouraging investments that undermine climate action, although concerns have been raised about their potential impact on poor countries. Since low-income groups contribute relatively little to carbon emissions, it is important to devise mechanisms to support them in coping with any associated higher costs. Import tariffs may serve as a complementary measure to carbon taxes, discouraging production relocation to countries with more carbon-intensive practices. However, such tariffs risk penalizing producers from developing economies and may be perceived as protectionist measures, rather than as support for a global shift towards sustainability. Therefore, it is crucial to consider the international equity implications of these measures, especially given that some affected countries are not major carbon emitters overall.

17. At the regional level, enhancing tax cooperation should be considered on the following four fronts:

(a) Establish or mandate existing regional intergovernmental mechanisms to coordinate tax incentives, improve tax certainty and fast track tax dispute resolution, especially as tax expenditures can be construed as a form of harmful State-aid or subsidy that distorts conditions of competition. Moreover, as deeper forms of regional economic integration ensue within the Arab Customs Union (ACU), administering, collecting and distributing indirect taxes may become more cumbersome once goods and services are in free circulation within the union. Tax administrations will find it harder to tax corporates as they can operate in different jurisdictions without triggering tax residency rules. Arab countries could also consider developing regional digital tax directives to avert possible tax abuses within ACU;

(b) Develop a regional mechanism to tax digital services and preserve the corporate tax base. The Arab region may wish to consider the new amendment introduced to article 12.b of the United Nations Model Double Taxation Convention that gives source countries greater taxing rights over automated digital services. Arab countries could also consider developing regional digital tax directives to avert possible tax abuses until the necessary international tax reforms are in place;

(c) Enhance regional cooperation efforts to fight corruption and related tax abuses. Arab countries may need to launch an intergovernmental process to revisit the Arab Convention to Fight Corruption and the cooperation agreement on the collection of taxes, fees and curbing tax evasion, especially in view of the changing structure/digitization of supply and value chains in the region;

(d) Establish a regional Arab financing and tax justice forum. A multi-stakeholder forum that serves as a dedicated platform to coordinate Arab positions on international and regional tax matters is needed, noting that of the 15 specialized ministerial councils established by the League of Arab States, none is uniquely poised to address fiscal and tax policy cooperation, be it to combat tax evasion, address aggressive tax planning and competition, or re-work Arab tax treaties to factor several global tax reforms.

18. At the global level, the following measures should be considered:

(a) Reconsider national tax reforms. Under increasing conditions of digitization and capital mobility, there are limits to what national tax instruments or reforms may render in terms of revenue outcomes. Policymakers must consider that in reality, national tax reforms are not national, and that the Arab region no longer has the luxury of designing and enforcing its tax systems in isolation. Equally, digitization offers opportunities to expand the tax base beyond national borders, given that geographical borders no longer define a country’s potential tax base, or the impact of its tax policy decisions;

(b) Advance a fair and effective international tax system. There is a need to establish beneficial ownership registries, require multinational corporations to publish accounting and financial information on a country-by-country basis to ensure inclusive access, and ensure harmonized environmental, social and governance (ESG) reporting to avoid bluewashing and greenwashing. The issue of tax related illicit financial flows and a lack of a universal forum to address this issue systemically remain a key governance gap. Universal

forums such as the United Nations Convention against Corruption and the United Nations Convention against Transnational Organized Crime already exist for corruption and crime related illicit financial flows. While the existing United Nations Tax Committee is doing important work, it is only an expert body, not intergovernmental, with experts serving in their individual capacity;

(c) Reinvigorate cooperation on the part of Arab countries to reinforce tax transparency, including the automatic exchange of tax information, improve transparency on the location of assets and establish beneficial ownership registries, and call for access to country-by-country reporting registries;

(d) Engage effectively in advancing global tax negotiations, and forge a new international tax architecture. Arab countries are advised to actively engage and establish a dominant footprint, and plausibly defend their tax interests, in the global tax negotiations underway within the G20/OECD Inclusive Framework on Base Erosion and Profit Shifting. Arab Governments are advised to weigh their options with respect to what is being advanced under the two pillars of the Inclusive Framework, notably with respect to redistributing taxing rights and enforcing a new global minimum corporate effective tax rate. For this purpose, potential Arab subscribers may wish to consider advocating for the following:

- Lower thresholds to determine in-scope MNCs subject to Amount A: Potential Arab subscribers are advised to broaden the scope of MNCs to increase tax certainty, and ensure that Amount A is not rendered ineffective given its restricted application to MNCs with the most profits. Here, the carve-outs for MNC operating losses to be carried-over need to be factored.

- Lower country nexus threshold for market jurisdictions: To cover small economies and countries in conflict and ensure that no-one is left behind from receiving a taxing right under pillar one.

- Lower profitability ratio to determine MNCs routine-profits: Once a nexus is established, all profits, be they routine or residual, should in principle be allocated to market jurisdictions. The proposed unitary approach removes routine profits from allocation to market jurisdiction without a backing rationale. MNCs marketing and distribution functions can be conducted remotely from low-tax jurisdictions, and market jurisdictions should have a taxing right over remote marketing and distribution activities.

- Higher reallocation percentage of residual profits: Amount A must be set at a level that ensures a meaningful reallocation of MNCs profits across market jurisdictions, giving more weight to sales and employment factors in formula apportionment.

- Higher minimum corporate effective tax rate (than the proposed 15 per cent): The effective tax rate should factor revenue requirements under a prolonged COVID-19 scenario and post-pandemic effort to achieve the 2030 Agenda. The point of setting a minimum effective tax rate is to raise the bar not pull it down.

- Reconsider the binding nature of dispute settlement and the structure of its panels: Details of the mechanism and the implementation of the outcome of the panel review remain unclear. Yet, MNCs that do not agree with the outcome may withdraw and rely on domestic procedures in each affected jurisdiction to determine Amount A reallocation. Moreover, this provision may potentially undermine the status and purview of regional dispute settlement mechanisms that are currently in place, including the Arab Investment Court of the League of Arab States.

- Thorough consideration of the link by which *zakat* (almsgiving) is categorized as covered taxes under GloBE: Islamic law identifies eight eligible channels for the use of *zakat* funds. The question raised pertains to whether "corporate *zakat*", as advanced by the OECD, should be considered as an alternative to corporate income tax levied on a different basis, and accordingly included in the calculation of the minimum effective tax.