How corporate tax incentives undermine climate justice

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Why corporate tax incentives undermine climate justice

1. Tax justice is climate justice

The tax justice movement and the climate justice movements are natural allies. Both aim to redress deeply discriminatory practices and inequalities upheld by a minority at the expense of everyone else. These practices and inequalities often stem for them same roots, which makes for common targets and goals between the two movements.

The Tax Justice Network recently began a series of works aimed at clarifying and strengthening the links between the tax justice and climate justice movements. Our position paper from 2023 laid out our thinking on how the two movements intersect, and how tax justice policies help address climate justice challenges.[1]

Corporate taxation and climate justice

This brief builds on the framework established in our position paper by focusing on how fair corporate tax policy – a cornerstone of tax justice, intersects with the 'polluter pays' principle – a cornerstone of climate justice.

Fair corporate tax policy enshrines the polluter pays principle. And conversely, harmful corporate tax policy negates the principle, at times flipping it on its head. **We zero in on how a specific area of corporate tax policy – tax incentives – allows two environmentally harmful sectors – shipping and extractives – to operate in polar contradiction to the polluter pays principle**. The destructive, though largely hidden subsidising of corporations operating in these sectors by many governments make them central stakeholders in the burning and degradation of the planet.

Based on data from the Tax Justice Network's Corporate Tax Haven Index[2] – a ranking of countries most complicit in helping multinational corporates abuse tax – we demonstrate the prevalence and diversity of

[1] Franziska Mager and Sergio Chaparro, Delivering Climate Justice Using the Principles of Tax Justice: A Guide for Climate Justice Advocates <https://taxjustice.net/wp-content/uploads/2023/06/Policy-brief-climate-justice_2206.pdf>.
[2] Corporate Tax Haven Index 2021 Methodology <https://cthi.taxjustice.net/cthi2021/methodology.pdf> [accessed 11 June 2024].

such incentives, and thus how they reward polluting sectors for their activities while depriving governments of urgently needed public revenue.

When it comes to tax and climate policy, much attention has been given to the role tax can play to reprice and thus disincentivise, chiefly through raising the price of carbon, including through carbon taxes. Subsidies by governments, including those for fossil fuel extraction[3], have also attracted considerable consideration. But relatively less bandwidth has been given to the role of tax incentives. This is a critical gap. **As we laid out in our position paper, the role of taxation in the fight for climate justice must go far beyond the narrow scope of using tax chiefly as a repricing tool, which we argue risks leaving deep structural inequalities intact or deepening them further.** Tackling harmful tax incentives, on the other hand, can offer an additional route to making the polluter pays principle come to bear, reap urgently needed revenue to address loss and damage, adaptation and mitigation, and in the process redress the deeply unequal power dynamics in global tax governance.

Recent years have seen unprecedented demand for action from countries around the world to claw back urgently needed tax revenue from tax abusing multinational corporations and tax havens. Economically and morally unjustified incentives and exemptions to existing tax rules granted to multinational corporations are key in this fight.

In the next chapter, we discuss how tax and the polluter pays principle are directly linked. But first, we set the stage with a summary of the thinking laid out in our 2023 position paper on how climate justice advocates can leverage tax justice towards their goals.

The 5Rs of tax for climate justice

When it comes to both tax abuse and the impact of rapidly rising global temperatures, it is the communities that do the least damage that suffer the worst consequences. **Cross-border corporate tax abuse by multinational corporations hits poorer countries hardest, as they suffer revenue losses equivalent to a larger share of their current tax revenues.[4] The same communities also experience the unequal impacts of the climate crisis, such as higher exposure and vulnerability to extreme weather events and rising sea levels**.[5] In both cases, the margin of action

3 ‘Fossil Fuel Subsidies Surged to Record $7 Trillion’, IMF, 2023 <https://www.imf.org/en/Blogs/Articles/2023/08/24/fossil-fuel-subsidies-surged-to-record-7-trillion> [accessed 14 February 2024].

4 The State of Tax Justice 2023 <https://taxjustice.net/wp-content/uploads/SOTJ/SOTJ23/English/State%20of%20Tax%20Justice%202023%20-%20Tax%20Justice%20Network%20-%20English.pdf> [accessed 11 June 2024].

5 Lucas Chancel, Philipp Bothe and Tancrède Voituriez, Climate Inequality Report 2023 (January 2023) <https://wid.world/news-article/climate-inequality-report-2023-fair-taxes-for-a-sustainable-future-in-the-global-south/> [accessed 19 June 2023].

lies with stakeholders holding economic and political power in the global north.

When we say that tax policy can be a powerful tool for climate justice, we argue for using it in a way that prioritises human and planetary wellbeing, instead of playing to the interests of the biggest and wealthiest polluters and extractors.

The most obvious way is by normalising taxes' revenue potential.[6] Huge sums of public revenue are needed to fill the enormous climate finance gap – the trillions of dollars to pay for loss and damage, and for adaptation and mitigation measures. This revenue function of tax is perhaps the most well-known benefit of effective tax policy.

But tax policy has the potential to go far beyond revenue, in what the Tax Justice Network has coined as the "5Rs" of tax justice: revenue, redistribution, repricing, representation and reparations. Beyond raising revenue, our policy platform offers a reform framework with multiple levers that the climate justice movement can build on – from fighting tax abuse to increasing financial transparency, to curbing the influence of the polluter elite on democratic processes and dismantling colonial legacies and power imbalances in the global financial architecture.

In our position paper, we identify four key challenges facing the climate justice movement that the "5Rs" can support: (1) the climate finance funding gap, (2) legacies of historic injustice, (3) extreme inequalities in emissions and wealth, and (4) international cooperation. The polluter pays principle cuts across these four challenges, which means good tax policy that enshrines it can help towards tackling all four challenges. +

The impact of harmful tax incentives, which this paper focuses on, and conversely the benefits to be gained from reforming harmful tax incentives, are most visible under the first and fourth challenges, those of the climate finance funding gap and international cooperation.

2. Tax justice and the Polluter Pays Principle

Many in the climate justice movement are familiar with taxes linked to biodiversity loss, ecosystem destruction and fossil fuel consumption. This includes duties on plastic bags and incandescent lightbulbs, the gradual increase on the price of polluting fuels, to potential taxes on luxury consumption goods like private planes or yachts.

Tax is intimately linked to the polluter pays principle. Historically applied in environmental law, it requires polluters to bear the environmental and

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6 Finding the Finance: Tax Justice and the Climate Crisis (June 2024) <https://actionaid.org/sites/default/files/publications/Finding%20the%20Finance%20Report%20-%20FINAL.pdf> [accessed 13 June 2024].

social costs of their actions. It can be applied to different environmental challenges, both ongoing – such as air and water pollution, and mitigating the release of greenhouse gases – as well as in a preventative manner, such as to avert oil spills.

The polluter pays principle is implemented through various policies and measures. The specific common denominator is that those who pollute more in the production or consumption of goods and services should pay more.

Existing taxes at the individual level, for example, can indirectly mirror the logic of the polluter pays principle. Take for example a progressive income tax. This kind of tax applies higher rates to high income groups than low-income groups, the former typically disproportionately responsible for a large share of a country's carbon emissions.[7] It follows then that a higher income tax on higher earners in practice applies a higher levy on those who capture a higher share of total emissions.

In other cases, regressive or indirect taxes undermine or contradict the polluter pays principle. Flat taxes like VAT or sales tax, for example on cooking fuels – an essential good especially in low-income countries – apply the same rate regardless of economic circumstances.[8] The common assumption that progressive transfers or inclusive public spending will offset the regressive effects of such taxes is often not met in practice.

But it is in the nature of the international tax architecture itself to reverse the logic of the polluter pays principle. Mechanisms like tax incentives excuse corporations or other legal entities from paying taxes that others must pay. This web of laws and loopholes is often only offered to, or only accessible to, the wealthiest multinational corporations and individuals – those with the resources and know-how from professional enablers to artificially minimise their tax bill. Moreover, when these laws and loopholes are utilised by, or even exclusively applicable to polluting sectors, the polluter pays principle isn't just flipped in principle but in concrete, costly practice. This means these laws and loopholes by design are antithetical to the polluter pays principle: those who emit more can and do pay much less.

In this paper we focus on the tax incentives that affect the income tax that companies pay: corporate income tax. We provide evidence of the widespread prevalence of incentives and provide examples of how their design and opacity create avenues for companies to abuse tax even as they operate in some of the most highly polluting sectors. These incentives severely limit countries' abilities to collect public revenue and

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[7] Lucas Chancel, 'Global Carbon Inequality over 1990–2019', Nature Sustainability, 5/11 (2022), 931–38.
8 Giovanni Ochialli, 'Just Environmental Taxation in Africa: How Tax Policy Can Curb Environmental Damage, Far beyond Just Carbon Taxes', Tax Justice Network, 2023 <https://taxjustice.net/2023/12/05/just-environmental-taxation-in-africa-how-tax-policy-can-curb-environmental-damage-far-beyond-just-carbon-taxes/> [accessed 14 May 2024].

are emblematic of the deep structural inequalities in global tax governance.

BOX: Corporate tax havens love polluting multinationals

Some countries intentionally set out to poach the profits of other nations by offering multinational corporations ways to escape or undermine the tax rules where they operate, reducing tax payments in those countries. These countries are called corporate tax havens. The spillover effects of one country's policy decisions means corporations can artificially shift profits away from where they make them and avoid paying the taxes they would otherwise be liable for. It also triggers a race to the bottom, where countries misguidedly compete for investment by reducing tax rates.[9]

Corporate tax havens are heavily implicated in undermining the polluter pays principle. Take the case of an Australian mining giant that can sell the coal it has extracted in Australia to its own offshore subsidiaries in corporate tax havens at very low prices.[10] By selling the coal at an artificially low value, it can drive down the taxes due on the sale of its coal. It is thus able to "move" the ownership of its Australian coal out of Australia into corporate tax havens while paying little to no tax on it to the Australian government. From the corporate tax havens, where corporate tax rates are very low to non-existent, it can now sell the coal to real customers at its true, profitable value.

And adding insult to injury, this multinational can reduce the taxes it owes to Australia even further by transferring corporate debts it has incurred elsewhere in the world onto the shoulders of its Australian subsidiary. This makes it look like the company is making losses in Australia, even though its operations are in fact highly profitable.

Finally, the use of corporate tax havens and increase in profitability is likely to have led this and a number or multinationals in similar positions to produce and sell more planet-damaging coal than if it had paid tax properly. Thus, tax havens can effectively engineer subsidies for carbon intensive or polluting economic activities.

9 International Monetary Fund, Spillovers in International Corporate Taxation, Policy Paper, September 2014, 1 <https://elibrary.imf.org/openurl?genre=journal&issn=2663-3493&volume=2014&issue=071> [accessed 11 June 2024].
10 Introducing the Dirty Dozen: Australia's Filthiest Fossil Fuel Polluters <https://www.climatecouncil.org.au/wp-content/uploads/2023/02/CC_MVSA0344-CC-Report-Introducing-the-Dirty-Dozen_Evergreen-Version_V12-FA-Screen-Single.pdf> [accessed 3 June 2024].

3. How corporate tax incentives undermine the polluter pays principle

Tax incentives are changes to the tax rules that reduce the taxes that individuals or companies are liable for, thus reducing tax obligations and providing an economic benefit. Tax incentives are sometimes made available only to specific groups of people or sectors. As our analysis will show, many countries offer tax incentives specifically to two of the world's most polluting sectors: shipping and extractives.

In theory, tax incentives can be a useful tool for governments to pursue important policy objectives, such as incentivising investments, for example in renewable energy. However, the importance of tax rates in a given location is generally overemphasized in relation to investment allocation: tax is not the first-order or only location factor for companies looking at investment decisions. At least as important are human capital, market access, infrastructure, rule of law and political stability. Once such conditions are met, many companies tend to compare different tax regimes and consider paying less tax for a given number of benefits.[11]

Overall, our Corporate Tax Haven Index finds that more often than not, tax incentives prove to be harmful.[12]

Why corporate tax incentives don't work

Through tax incentives, governments relinquish a sum of money they would otherwise have received in the form of corporate income tax. So, why do it? The reasoning for government giving up tax revenue is that society gains a bigger and broader benefit in return. Like a restaurant might offer a lunch discount to get more customers in, a government might offer a tax incentive to get more businesses growing, raising productivity, generating more jobs and more tax revenue, and so on.

In practice, however, tax incentives hardly ever work this way when it comes to corporations.

Take the stark contrast in how the Spanish government taxes bakeries and investment funds. Bakeries must pay a statutory 25 per cent tax rate on their income, while investment funds only pay 1 per cent on theirs due to a tax incentive. Does this incentive encourage more investment in Spain? An assessment by the Independent Authority for Spanish Fiscal

11 Markus Meinzer and others, 'Comparing Tax Incentives across Jurisdictions: A Pilot Study', SSRN Electronic Journal, 2019 <https://www.ssrn.com/abstract=3483437> [accessed 3 June 2024].
12 Michael Masiya and others, 'Tax Expenditures and Progress to the Sustainable Development Goals', Sustainable Development, n/a/n/a <https://onlinelibrary.wiley.com/doi/abs/10.1002/sd.3016> [accessed 3 June 2024].

Responsibility found the impact of the incentive was “inconclusive”.[13] An inconclusive result for an incentive that gives up €550 million in tax revenue a year is hardly a resounding policy success.

So why don’t tax incentives work for corporations?

Unlike a lunch deal at restaurant where a customer can only get a discount on their receipt after they have eaten at the restaurant, **corporations can benefit from tax incentives without having to substantiate that they conducted business activity in the country**. In fact, unlike restaurant customers, it’s the corporations who print and send in their receipts to governments for a discount under a tax incentive. One only has to imagine a restaurant that lets customers print their own receipts to see how things can go wrong.

For example, it is perfectly feasible for a Spanish investment fund to pretend on paper that the profits it made from investing in Luxembourg were made investing in Spain, allowing it to benefit from Spain’s tax incentive while generating no new investments in the country.

But it gets worse. **Because tax incentives are often not tied to real business activity, corporations may benefit from a country’s tax incentive from wherever they are in the world.** Imagine the print-your-own-receipt restaurant now letting customers order from anywhere in the world. It’s easy to see how a country’s tax incentive can spiral out of hand and enable corporations to accumulate extreme levels of wealth. This is wealth that often does not enter the economy of the country from which it reaps a tax incentive or does enter the country’s economy but in harmful ways that exacerbate inequalities, like by skyrocketing local real estate prices beyond what residents can afford.

If tax incentives don’t work, why are they so widespread? Tax incentives are often driven by lobbying, rather than a long-term industrial strategy, and are often designed without clear policy objectives. Governments seldom subject tax incentives to cost and benefit evaluations or to robust public oversight.[14]

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13 Evaluación Del Gasto Público 2019 <https://www.airef.es/wp-content/uploads/2020/10/Docus_Varios_SR/Estudio_Beneficios_Fiscales_Spending_Review.pdf> [accessed 12 June 2024].
14 Hania Kronfol and Victor Steenbergen, Evaluating the Costs and Benefits of Corporate Tax Incentives: Methodological Approaches and Policy Considerations, In Focus <https://documents1.worldbank.org/curated/en/180341583476704729/pdf/Evaluating-the-Costs-and-Benefits-of-Corporate-Tax-Incentives-Methodological-Approaches-and-Policy-Considerations.pdf> [accessed 11 June 2024].

BOX: Two broad types of tax incentives

There are generally two types of tax incentives: ones that are profit-based and ones that are cost-based.

Profit-based tax incentives are the most harmful because the potential revenue losses for governments are unlimited, and because they rarely change the investment decisions of companies. These profit-based incentives can be fully disconnected from economic activity on the ground, making it possible for multinationals to exploit them through the way they structure their business even without being physically present in a country. As a result, these incentives are often disconnected from a company investing in real terms more than it would have without incentives.

By contrast, **cost-based tax incentives** offer reductions for additional company expenditure in respect of staff, fixed assets or research and development. As a result, the resulting revenue losses are limited by the real expenditure costs of a company (albeit these can be inflated). They are not considered in this briefing.

Profit-based tax incentives can come in different forms and shapes. They include targeted or special rules for specific industries or entire economic sectors or contracts with individual companies. These incentives reduce government revenue and create an unequal playing field for businesses within a country's borders. A country that has lower tax rates and loopholes in corporate tax rules causes harm to other nations as well (see BOX on corporate tax havens).

In theory, tax incentives can be seen as complementary to the logic of the polluter pays principle: those who provide a social good pay less. In return for an economic reward, corporations provide a greater, broader, social good. In practice however, tax incentives often provide corporations with an economic reward for little in return, and at the cost of foregone public money that could have contributed towards social goods. In practice, tax incentives can therefore contradict the polluter pays principle.

That conceptual contradiction becomes especially concerning when we look at the prevalence of tax incentives that countries give to two of the world's most polluting industries: the shipping and extractives sectors.

4. Incentives’ mass subsidising of emissions in the shipping and extractive sectors

Tax incentives are widespread in the shipping and extractives sectors. These industries are two of the world’s biggest and most emissions intensive and environmentally damaging. **Governments subsidise their catastrophic impact through incentives.**

Transport is hugely emissions intensive – the EU’s transport sector alone accounts for almost 25 per cent of total global carbon emissions.[15] The OECD estimates that in 2022, there were 858 million tonnes of CO_2 emissions globally from the shipping industry, compared with 739 million tonnes of CO_2 emissions from air transport; and 63% of emissions from global shipping came from vessels operated by companies based in OECD countries.[16] Resource extraction is responsible for half of the world’s carbon emissions[17], in addition to polluting air, water and land and contributing to biodiversity losses. Despite efforts to decarbonize, it is expected that both sectors will continue to be sizable for years to come, including for extracting minerals needed for the energy transition.

Despite these industries’ huge environmental footprint, they enjoy some of the world's most outrageous tax incentives. Proportionally speaking, this makes them simultaneously some of the world's biggest emitters and lowest taxpayers. Corporations operating in the shipping and extractives sectors are key actors in the opaque albeit hugely consequential decision of many governments to further subsidise global warming. **The tax incentives provided by many countries enable them to leave the rest of the world to foot the bill of the negative environmental externalities arising from their sparsely taxed profit-making.**

In the shipping sector, tax incentives are primarily exercised in the form of “tonnage tax regimes”. In the extractives sector, tax incentives are primarily exercised in the form of special rules, contracts and “special economic zones”.

Pandering to emissions intensive shipping corporations: tonnage taxes

A "tonnage tax" is a special set of tax laws that applies to the shipping industry. Under this tax regime, large shipping companies do not pay tax

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15 Trends and Projections in Europe 2023, EEA Report 07/2023 <https://www.eea.europa.eu/publications/trends-and-projections-in-europe-2023> [accessed 13 June 2024].
16 OECD Statistics, ‘New Estimates Provide Insights on CO2 Emissions from Global Shipping’, 2023 <https://oecdstatistics.blog/2023/06/15/new-estimates-provide-insights-on-co2-emissions-from-global-shipping/> [accessed 3 June 2024].
17 ‘Why Does Extractives Matter?’, 2017 <http://www.unep.org/explore-topics/extractives/why-does-extractives-matter> [accessed 3 June 2024].

on the profits they make from shipping goods, but instead pay a “flat fee” on the tonnage capacity of their ships. In other words, they pay tax on how much weight they can carry instead of how much profit they make. According to the Corporate Tax Haven Index, more than half of the 70 countries reviewed were exercising a tonnage tax regime.

Tonnage tax regimes result in shipping companies paying a tax rate on their profit far below a country's official corporate tax rate. Usually structured in tax bands, these rates can in effect be as low as 0.5 per cent to 2 per cent.[18] Countries' official corporate tax rates, in comparison, average around 19 per cent. One 2017 study captures the state of taxation in the global shipping sector: “[...] the race to the bottom has reached the bottom[...]”.[19]

How tonnage tax regimes result in extremely low tax rates is easy to see. If the profit a shipping company makes is many times bigger than the fixed flat fee it pays on its ships, than that fee will account for a tiny fraction of the shipping company's profit. **This inevitably means the more profit a shipping company can make, the smaller the company’s obligation to pay tax becomes.** By design, tonnage tax regimes inverse the polluter pays principle.

The injustice of the tonnage tax regime doesn't just shortchange society out of a fair share of tax, it results in one the world's most carbon intensive industries contributing a sliver of tax compared to others towards addressing the negative externalities they are responsible for. Take two ships anchoring in the same port – one belonging to a local fishing enterprise and the other to an international shipping company. They use the same amount of fuel to generate their profits, but the local enterprise’s ship does not fall under a tonnage tax regime and so the company pays a 35% corporate tax rate on the profits made selling freshly caught fish. The high sea vessel is registered in a country far away that offers a convenient tonnage tax regime resulting in tax rates below 5%. They have comparable environmental impacts, but only the local shipping enterprise contributes to government revenue needed to adapt and mitigate.

This dysfunctionality is amplified in countries that include activities like gambling on ships or natural resource exploration expeditions in their tonnage tax regimes. These ships pay a flat fee based on the weight they can carry even though weight has little relevance in determining how much income their primary business activity – which is not cargo transport based – can generate.

18 George Steer, ‘Container Shipping’s Tonnage Tax Trick’, *Financial Times*, 16 August 2022 <https://www.ft.com/content/002e4a91-a4b5-4ef8-bf53-f61374f7fda3> [accessed 13 June 2024].
19 Guglielmo Maisto, ed., Taxation of Shipping and Air Transport in Domestic Law, EU Law and Tax Treaties, EC and International Tax Law, vol. 15 (Amsterdam, 2017).

Two aspects of tonnage tax regimes specifically run counter to the polluter pays principle.

Firstly, tonnage tax regimes result in overall much lower tax rates for transportation activities that generate large amounts of carbon emissions. Secondly, some tonnage regimes additionally apply to other environmentally harmful activities, such as oil, gas and minerals exploration and offshore extraction. While the income models of oil drilling or deep-sea mineral mining exploration has little to do with the tonnage of ships or the shipping industry, these activities are nonetheless covered by, and subsidised through, some tonnage tax regimes.

Tonnage tax regimes are pervasive, especially in the European Union. All nine tonnage regimes that apply to extractive activities identified by the Corporate Tax Haven Index are found in the European Union. Another eight countries provide full tax exemptions – meaning no tax obligation – for the shipping industry through tonnage taxes.

Table 1. Countries with corporate income tax incentives for the shipping industry out of 70 countries covered by the Corporate Tax Haven Index 2021 (see Appendix 1)

Partial tax exemptions apply for shipping companies (incl. tonnage tax regimes*, where calculation of corporate tax is not linked to profits)	Belgium*, Bulgaria*, Croatia*, Cyprus*, Denmark*, Finland*, France*, Germany*, Gibraltar*, Greece*, Ireland*, Latvia*, Liberia*, Lithuania*, Malta*, Netherlands,* Poland*, Spain*, and Taiwan*. Cost-based tonnage regimes available (disregarded): United Kingdom and Italy
Full exemption for shipping business: operators pay no corporate tax whatsoever	Curacao, Hong Kong, Lebanon, Mauritius, Montserrat, Panama, Singapore, and South Africa.
Foreign profits incl. by shipping operators (and businesses in general) are exempt from income tax	Costa Rica, Curaçao, Gibraltar, Hong Kong, Lebanon, Liberia, Panama, Seychelles, and Singapore.
Zero tax is payable by shipping operators (by law or de facto through complex rules)	No income tax is payable: Anguilla, Bahamas, Bermuda, British Virgin Islands, Cayman Islands, Guernsey, Isle of Man, Jersey, Turks and Caicos Islands, and the United Arab Emirates. Special tax computation rules result in a tax rate of zero per cent: Estonia, Latvia, Monaco.

Incentives as handouts to extractive industries

Many countries also offer incentives for companies operating in the extractive industries (see Appendix 2).

Countries that are home to fisheries, forests and mineral reserves may introduce sector specific tax rules on corporate profits. This can have deeply destructive outcomes. Ocean fishery in China, for example, is taxed at zero per cent.[20] Given the negative environmental and human rights impacts associated with ocean fishery, such as through trawling and modern slavery on vessels[21], the exemption of corporate income taxes further reduces the accountability of this industry.

For example, Dutch-controlled Aruba and Curaçao exempts income from the extractives sector (see appendix). While the former provides a 10 per cent reduced rate for oil refineries, the latter fully exempts such activities, as well as petroleum extraction and sale activities. These tax incentives, like the tonnage tax system, flip the polluter pays principle on its head. Moreover, in absence of substantial taxes paid, increased profitably only makes continued further extraction more likely.

But it’s not just countries with abundant natural resources – where the extraction happens – offering tax incentives. **Callously, some of the most extreme tax incentives enjoyed by the extractive industries are offered by countries miles away, which possess none of the natural resources.** These “remote” tax incentives often drastically reduce or even eliminate the tax dues that extractive industries must pay on the resources they extract in other countries. By design, this deliberate targeting of other countries’ natural resources deprives them of public money.

These remote tax incentives often work by having special sets of laws in place, known as regimes, which allow a multinational corporation to setup a local company or legal structure in the country offering the tax incentive. The multinational corporation can then shift the profit it makes from extracting resources elsewhere in the world to this remote legal structure, which is granted a large or full tax exemption under the special rules.

Singapore, for instance, has very few natural resources. Nonetheless, it gives companies incorporated within in its borders a large tax exemption on profits they make from selling the types of resources and commodities that are not found within its borders. These local companies are setup by multinational corporations who extract these resources found elsewhere in the world. Despite not having any significant metal resources, Singapore is today a major global exporter of metals, virtually none of which are extracted locally, and thanks to Singapore’s special tax rules, go largely undertaxed[22] and in blatant contradiction with the polluter pays principle.

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20 Ma Shiqi, China - Corporate Taxation, BFD Country Tax Guides.
21 Ian Urbina, ‘Superpuissance de La Pêche, La Chine Exploite Les Hommes et Pille Les Océans’, *Mediapart*, The Outlaw Ocean Project edition <https://www.mediapart.fr/journal/international/011123/superpuissance-de-la-peche-la-chine-exploite-les-hommes-et-pille-les-oceans> [accessed 13 June 2024].
22 A. Lingbawan, Singapore - Corporate Taxation, Country Tax Guides IBFD.

Other corporate tax havens like the Cayman Islands, Mauritius and Jersey levy zero per cent income tax. By integrating tax incentives as a core feature of their tax systems, countries like Estonia, Monaco and Hong Kong make it easy for many companies to eliminate their tax obligations entirely. For example, an offshore drilling company or a copper mining company can be established in Mauritius, Monaco or Estonia without having to pay any tax on income accrued from these activities – which take place elsewhere in the world.

The pervasive use of tax incentives goes against even their theoretical good intent. Rather than offering a tax incentive to boost local economic activity, countries offer tax incentives to disconnected economic activity going on elsewhere in the world.

Table 2. Countries with corporate income tax incentives for the extractives industry out of 70 countries covered by the Corporate Tax Haven Index 2021 (see Appendix 2)	
Partial tax exemptions apply for extractives companies (incl. overbroad tonnage tax regimes*, where calculation of corporate tax is not linked to profits)	Argentina, Aruba, Belgium*, Croatia*, Cyprus*, Denmark*, Germany*, Greece*, Latvia*, Malta*, Netherlands*
Full exemption for extractives businesses: some operators pay no corporate tax whatsoever	China, Curacao, Mauritius, Montserrat, Singapore
Foreign profits incl. for extractives activities (and businesses in general) are exempt from income tax	Costa Rica, Curaçao, Gibraltar, Hong Kong, Lebanon, Liberia, Panama, Seychelles, Singapore.
Zero tax is payable by extractives companies (by law or de facto through complex rules)	No income tax is payable: Anguilla, Bahamas, Bermuda, British Virgin Islands, Cayman Islands, Guernsey, Isle of Man, Jersey, Turks and Caicos Islands, United Arab Emirates. Special tax computation rules result in a tax rate of 0 per cent: Estonia, Latvia, Monaco.

Many tax incentives targeting the extraction of resources are not agreed through parliament nor codified in a country's laws. Rather, companies often seek to negotiate individual contracts with governments directly – too often outside of legislative process and in the absence of public scrutiny. The taxation of many mining, oil and gas projects is governed by such individually negotiated contracts, rather than by the general tax code. In Africa in particular, negotiated tax incentives are almost as common as those granted in primary legislation.[23] The public disclosure of

23 Insights on Incentives: Tax Competition in Mining <https://www.iisd.org/system/files/publications/insights-incentives-tax-competition-mining.pdf>.

these contracts is essential, as contract secrecy worsens tax abuse and obscures destructive environmental impacts.

BOX: Special Economic Zones

Specials rules and contracts are not the only way countries offer tax incentives. Some countries establish “special economic zones”, which are geographical areas that exempt existing regulations to commodities, manufacturing or trade that occur or move through the zone. Special economic zones are often called “freeports” or “free trade zones”.[24] Despite the promise of economic activity these names imply, special economic zones often function as tax-free warehouses where high-value assets can be stored or can exchange hands with little to no transparency and without having to pay the tax obligations that would normally apply. Plenty of evidence shows special economic zones generally do not boost economies.[25] [26]

There may be as many as 5,000 special economic zones in the world across more than 130 countries offering a wide range of tax incentives.[27]

Tax incentives offered in special economic zones heighten the risk of money laundering and tax evasion. These zones are characterised by deregulation and secrecy, even if their original intent was to remove the need for payment of taxes on goods simply in transit through a country. This plays into the hands of nefarious actors seeking to circumvent sanctions or engage in environmental crimes, including illegal mining and logging and waste trafficking.[28]
The customary secrecy of these zones, where beneficial owners (the true owners of companies and assets) can remain hidden[29] and where virtually no customs oversight is applied, combined with the absence of taxation, makes them powerful tools for fully exploiting economic returns from environmental crimes. For example, the Suifenhe free trade zone in China has been linked to illegal logging in Russia, and Las Palmas-Gran Canaria free trade zone in Spain, to illegal fishing.[30]

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24 ‘Freeports: PM Johnson’s “Free Self Storage” for the Rich and Powerful’, Tax Justice Network, 2019 <https://taxjustice.net/2019/09/10/freeports-pm-johnsons-free-self-storage-for-the-rich-and-powerful/> [accessed 3 June 2024].
25 Chris Holden, ‘Graduated Sovereignty and Global Governance Gaps: Special Economic Zones and the Illicit Trade in Tobacco Products’, Political Geography, 59 (2017), 72–81.
26 Alexandra Hall and others, ‘Duty Free: Turning the Criminological Spotlight on Special Economic Zones’, The British Journal of Criminology, 63/2 (2023), 265–82.
27 *OECD Recommendation on Countering Illicit Trade: Enhancing Transparency in Free Trade Zones*, OECD Legal Instruments <https://www.oecd.org/gov/risk/recommendation-enhancing-transparency-free-trade-zones.htm> [accessed 13 June 2024].
28 Money Laundering from Environmental Crime (Paris, July 2021) <https://www.fatf-gafi.org/content/dam/fatf-gafi/reports/Money-Laundering-from-Environmental-Crime.pdf.coredownload.pdf> [accessed 13 June 2024].
29 Matti Kohonen, ‘Beneficial Ownership and Climate Crimes: A Fishy Business’, Tax Justice Network, 2023 <https://taxjustice.net/2023/09/06/beneficial-ownership-and-climate-crimes-a-fishy-business/> [accessed 11 June 2024].
30 Natalia Muñoz Cassolis, ‘Open Secrets: Corruption in Free Trade and Special Economic Zones as an Enabler for Illegal Wildlife Trade’ (2022) <https://files.worldwildlife.org/wwfcmsprod/files/Publication/file/6pghxs9zpy_Corruption_in_FTZ_SEZ_as_an_enabler_for_IWT.pdf>.

5. Addressing climate justice challenges with the momentum for tax justice reform

Incentivising multinational companies in the shipping and extractives sectors in the ways described so far has dire consequences on key environmental and climate metrics. They include a high volume of greenhouse gas emissions, but extend to air and maritime pollution, loss of biodiversity and related harmful effects on the natural environment, alongside a rise in global temperatures.

These tax incentives also undermine the efforts of climate justice advocates and exacerbate two of the challenges facing the climate justice movement to which the 5Rs of tax can be applied. As we identified in our position paper, these two challenges are the climate finance funding gap and international cooperation.

In this section, we draw out the consequences of harmful incentives as they overlap with these two challenges and discuss how tax justice offers concrete policy solutions.

Tackling the climate finance gap with an alternative global minimum corporate tax

The most urgent challenge for the climate justice movement lies in securing the funding required compensate affected communities with the necessary funds to adapt to and mitigate the adverse effects of the climate crisis, and to implement broad-scale systemic change[31]. Climate finance pledges are currently pooled in a variety of multilateral climate funds, yet they fall short of the needed scale. In addition, rather than public grants, much of climate finance still comes in the form of loans, further indebting affected countries.[32]

Yet at a minimum, the cost of protecting the most vulnerable communities from the unavoidable consequences of climate change, like rising sea levels, is estimated at over US$500 billion a year.[33]

Tax incentives – and corporate tax abuse in general – undermine the ability of countries to mobilise large sums of public revenue that could fill the climate finance gap. The loss of corporate taxes is also a loss of

31 *Finding the Finance: Tax Justice and the Climate Crisis*.
32 Leia Achampong and Iolanda Fresnillo, 'Irresponsible Lending Prevents the Global South from Escaping the Debt-Climate Trap', Eurodad, 2024 <https://www.eurodad.org/irresponsible_lending_prevents_the_global_south_from_escaping_the_debt_climate_trap> [accessed 4 June 2024].
33 'Finance & Justice' <https://www.un.org/en/climatechange/raising-ambition/climate-finance> [accessed 3 June 2024].

an integral part of the 'mosaic of funding' that will be required.[34] This loss is experienced both in the global north and south but especially detrimental in the global south, as poorer countries rely on a relatively higher share of tax revenue to fund public expenditure of all kinds. Simultaneously, the global south is where the effects of rising global temperatures are the most destructive.

But there is momentum: There are also proposals specifically for profits derived from resource extraction and rents (including from fossil fuels, minerals mining, fisheries, agriculture, forestry and more).[35] Excess profit taxes were reintroduced in the European Union in the wake of the war in Ukraine, and the International Tax Taskforce launched at COP28[36] explicitly mentions various types of corporate taxes and sectoral levies as sources of future climate finance. Nobel laureate Esther Duflo is only one of a series of high-profile economists to argue that mobilizing corporate taxes to fill the climate finance gap is a moral obligation for historic polluters.[37]

And indeed, the biggest site of change on corporate tax right now is the new global minimum tax rate. **First announced and championed by the Biden administration in 2021, the proposal sought to bring an end to the race to the bottom between countries by enshrining a minimum global corporate tax rate.** Many were optimistic about the opening of a unique window of opportunity for structural change, given the influence of the US government. A truly effective and just minimum rate – an idea that had long been relegated to the fringes of the tax justice movement – could in fact make corporate tax havenry a thing of the past and make tax incentives ineffective.

Initial estimates on how much tax revenue a global minimum rate could recover from corporate tax havens ranged from $540 billion to $640 billion per year.[38]

However, the proposal became progressively watered down to the point of being anything but just. It sought to distribute the taxes it clawed back from tax havens not to the original countries where the multinational corporation should have paid taxes, but to the countries where it has its headquarters. Since these are mostly located in global north countries,

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34 Franziska Mager, 'Fight Tax Abuse for a Fighting Chance on Climate: Reflections on COP28 - Tax Justice Network', 2023 <https://taxjustice.net/2023/12/14/fight-tax-abuse-for-a-fighting-chance-on-climate-reflections-on-cop28/> [accessed 3 June 2024].
35 Markus Trillig, Make Polluters Pay: How to Tax Excessive Ecological Footprints <https://assets.nationbuilder.com/eurodad/pages/3351/attachments/original/1711008822/green-taxation-briefing-feb29.pdf?1711008822>.
36 'ITTF | International Tax Task Force' <https://internationaltaxtaskforce.org/> [accessed 22 May 2024].
37 Joe Lo, 'Global Billionaire Tax for Fighting Inequality Rises up Political Agenda', Climate Home News, 2024 <https://www.climatechangenews.com/2024/04/19/global-billionaires-tax-to-fight-climate-change-and-hunger-rises-up-political-agenda/> [accessed 3 June 2024].
38 Bou Mansour, 'Biden Tax Plan Can Recover $640bn but OECD Proposal Would Shrink Gains and Reward Worst Perpetrators' <https://taxjustice.net/press/biden-tax-plan-can-recover-640bn-but-oecd-proposal-would-shrink-gains-and-reward-worst-perpetrators/> [accessed 11 June 2024].

the proposal would have ended the race to the bottom for the global north but not the global south, allowing the syphoning of corporate tax revenue from the global south to continue.

It was amended further under pressure from European tax havens like Ireland. **The new minimum rate will now keep the race to the bottom mostly intact in the global north too, just alive enough to enable European corporate tax havens to continue to conduct their tax haven ways but reap even greater rewards than before**. This has led some tax experts to label the global minimum tax rate as a "rewards programme" for tax havens.[39] High-income countries and investment hubs would be the big winners under Pillar Two, with over 80 percent of revenue gains accruing to these two groupings. Low-income countries, meanwhile, would receive just 0.03 percent of additional revenue, which is significantly lower than their share of corporate income tax in 2019 (0.3 percent). Similarly, most of the revenue gained by developing countries under Pillar Two would accrue to China.[40]

Obviously, a global minimum tax rate that does not make a significant dent in the race to the bottom and continues to permit the global north's syphoning of tax revenue from the global south will do little to address the climate finance gap, or to reverse the power imbalance that the global tax governance system encapsulates. And if that wasn't bad enough, the shipping industry has already been granted an exemption from the new global minimum tax rate. Deliberate action has been taking to ensure the new global minimum tax rate does not rock the 'polluter gets away' climate long fostered by tax incentives.

Fortunately, however, the promising route of a more comprehensive global minimum tax is increasingly becoming a feasible proposition. An ambitious proposal by the South Centre[41] sets out how countries can pursue an alternative, effective global tax rate by acting in regional groupings and unilaterally, including revisiting tonnage tax regimes and finally covering the shipping industry.

Democratising global tax cooperation to advance climate finance

The initial ambition behind the global minimum tax rate made clear a strong political desire among many governments to clamp down on the race to the bottom, facilitated by policies like tax incentives. But the

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39 'The Global Tax Rate Is Now a Tax Haven Rewards Programme, and Switzerland Wants in First', Tax Justice Network, 2023 <https://taxjustice.net/2023/04/06/the-global-tax-rate-is-now-a-tax-haven-rewards-programme-and-switzerland-wants-in-first/> [accessed 3 June 2024].
40 Felix Reitz, Revenue Effects of the OECD Corporate Tax Reform - An Updated Impact Assessment of Pillar Two <https://ile.unisg.ch/wp-content/uploads/2023/07/17-WP-Reitz.pdf>.
41 Sol Picciotto and others, 'Beyond the Two Pillar Proposals A Simplified Approach for Taxing Multinationals'.

struggles to realise and enforce this ambition point to a bigger challenge faced by the climate justice movement: international cooperation.

The global minimum tax rate is a stark example that the existing system of global tax governance with its entrenched inequalities is utterly unfit to effectively deal with the challenges posed by the climate crisis. This system was established and is dominated by the OECD, a small club of rich countries which has determined – opaquely, behind closed doors - global tax rules for the past sixty years.

The OECD's exclusionary governance structure fuels existing historic inequalities in taxing rights and decision making. It oversees the setting of harmful tax standards and practices like the new global minimum tax rate, to benefit rich countries in the global north, at the expense of those in the global south.

But fair, transparent global cooperation on an equal footing is essential to introduce, mainstream and ultimately pass policies to reduce emissions, as well as to reform international tax governance in service of these aims. So far as decision making on global tax policy remains exclusively in the hands of OECD members deliberating behind closed doors, attempts to take on the aggressive use of tax incentives by countries to undermine others' tax revenues will face daunting challenges at the international level.

The vast majority – 78 per cent[42] – of all tax losses countries suffer every year are facilitated by OECD member countries and their dependencies. This costs countries US$374 billion in lost tax every year. US$219 billion of this sum is lost due to OECD members and their dependencies enabling multinational corporations to underpay tax elsewhere in the world, including using tax incentives. At the same time, OECD member countries are where most of the polluting multinational companies and their creditor banks have their headquarters.

The global minimum tax rate is not just an example of how the OECD's non-inclusive governance process produces bad deals for the global south. It also demonstrates how this 60-year-old governance system imposes its unfavourable rules on non-OECD members. Many non-OECD member countries have complained of having their arm twisted into supporting the new minimum tax rate, despite the OECD failing to produce the statistics it promised on what impact the minimum tax rate would have on countries' tax revenues.[43] In 2023, the IMF was exposed attempting to coerce Sri Lanka during debt renegotiations to accept the

42 The State of Tax Justice 2023.
43 ATAF, The Place of Africa in the Shift towards Global Tax Governance: Can the Taxation of the Digitalised Economy Be an Opportunity for More Inclusiveness <https://events.ataftax.org/index.php?page=documents&func=view&document_id=35> [accessed 4 June 2024].

OECD’s new minimum rate even though the IMF’s own research the new rate would constrain the country's ability to raise tax revenue.

The OECD and many of its members are clear that they believe tax abuse by multinational corporations is an urgent, costly global problem that needs to be fixed. But the OECD has been unable, after more than a decade of attempts, to reform its own global tax rules to curb tax abuse. Many countries, particularly from the global south, and leading experts from around the world argue the OECD’s failure to make progress is due to the OECD being an unfit and non-legitimate body for deciding global tax rules.

But a democratic revolution to unseat the OECD’s reign over global tax policy is unfolding. In 2023, countries at the United Nations, led by the African Group, took historic action and voted by a landslide majority to begin negotiations on establishing a UN tax convention, which would move rule-making on global tax rules from the OECD to the UN and finally open the door to democratic, inclusive and transparent decision making on global tax policy.[44]

Inclusive tax governance means all countries can freely deliberate the rules of international taxation. For most countries and their populations, a UN tax convention would give them sovereignty over their taxing rights for the first time since their independence, and the best opportunity in decades to end the influence of corporate lobbyists and tax havens over global tax rules and thus the first real fighting chance to significantly curb tax abuse. Ongoing negotiations show a desire to deliberate a simpler and more comprehensive global minimum tax rate that would stop the pandering to polluting sectors through frameworks and exemptions.

But some countries have gone even further and expressed their desires to incorporate into the UN tax convention explicit commitments on using tax policy to address environmental issues. For example, Colombia has listed among the five substantive issues it believes require urgent commitments, ‘tax measures to finance climate action, such as a global corporate income tax.’ Indeed, the draft Terms of Reference for the convention state the explicit objective of ‘ensuring that tax measures contribute to addressing environmental challenges’.[45]

The UN tax convention process is a vital opportunity for climate justice advocates to shape the global tax policy landscape now to enshrine climate justice goals, including the setting of the New Collective Quantified Goal on Climate Finance (NCQG). Advocates should seize the opportunities coming with this process and aim to ensure the UN Tax

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44 ‘UN Adopts Plans for Historic Tax Reform’, Tax Justice Network <https://taxjustice.net/press/un-adopts-plans-for-historic-tax-reform/> [accessed 3 June 2024].
45 ‘Introductory Note to the Bureau’s Proposal for Zero Draft Terms of Reference for a United Nations Framework Convention on International Tax Cooperation’, 070624 <https://financing.desa.un.org/sites/default/files/2024-06/Zero%20draft%20ToR%207%20June%202024.pdf> [accessed 11 June 2024].

Convention turns the polluter pays principle into a reality, including by putting an end to the mass subsidising of polluting corporations through harmful corporate incentives.

6. Conclusion

Global corporate income tax rules are riddled with harmful incentives that systematically spur the race to the bottom. Based on data from our Corporate Tax Haven Index, this brief has shown the prevalence of harmful tax incentives in the shipping and extractives industries – two particularly polluting sectors.

The brief illustrates with examples such as tax rates of effectively zero for shipping operators, and pervasive tonnage tax regimes, some of which extend to activities like deep sea drilling. Many countries also offer exemptions for companies operating in the extractive industries, including when they themselves aren't resource rich. Illegal fishing, logging and mining are plunged into further secrecy through different levels of exemptions of corporate income, sometimes shrouded behind Special Economic Zones, thus further reducing the accountability of these sectors.

Climate justice activists largely operate separately from tax negotiations. Yet the movement needs to embrace how central corporate taxation rules are to undermining the polluter pays principle, to limiting the revenue raising function of tax and effective international cooperation.

For a hope of success, and along with harmful fossil fuel subsidies and large scale decarbonization efforts, the tax justice and the climate justice movements need to call for ending morally bankrupt tax incentives that fuel the climate crisis. If countries managed to eliminate the incentives for the shipping and extractives sectors discussed in this paper through a fair deliberation process based at the UN, decades of tax abuse by some of the worst polluters could be stopped. Additional corporate tax revenue in the billions of dollars could be collected from highly profitable, emissions intensive and environmentally destructive industries. This process would work alongside the implementation of additional taxation measures to collect public revenue from polluting corporations, including fossil fuel companies.

With countries across the globe recently taking historic actions to bring an end to the race to the bottom on taxes through UN tax reform negotiations, there are several opportunities to enable redistributive policies that accurately reflect the polluter pays principle.

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Appendices

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