

DRAFT

unpan1.un.org/intradoc/groups/public/documents/un/unpan000881.pdf

<http://larrywillmore.net/Mendez.pdf>

**THE CASE FOR GLOBAL TAXES:
AN OVERVIEW**

**Paper presented to the
United Nations ad hoc Expert Group Meeting
on Innovations in Mobilizing Global Resources for Development
United Nations Headquarters, New York
25 – 26 June 2001**

**By Ruben P. Mendez
Erstwhile of UNDP
Adjunct Professor and Fellow
New York and Yale Universities
1 June 2001**

Abstract

The global public sector faces soaring financial needs, especially for international peace keeping and enforcement, development and poverty alleviation, and effective global governance. This, plus the dishearteningly flawed public financing framework used today, indicates an urgent need for fundamental and innovative reform. The *status quo* framework consists overwhelmingly of government contributions—which are mainly voluntary and in the case of obligatory payments flouted with impunity—augmented by some public borrowing and institutional income from operations and interest. The post-World War II record shows the arrant inadequacy, unpredictability, and unassuredness of the current form of international public financing and of the various attempts to improve it. What is needed is an international fiscal system based on automaticity and sound principles and lessons of public economics, and drawing from the experience of the tax systems of nation-states. This paper presents proposals for global taxation, charges for the use of the global commons, and related monetary measures which do not depend on voluntarism. Their aim is to mobilize sufficient financial resources to meet global needs, correct international market failures, and facilitate a more equitable distribution of income among and across nations. The proposed measures are technically, legally, economically, and administratively feasible within the existing international dispensation. The biggest obstacle is political. There is substantial progress, however, in the evolution of new and constructive attitudes, and with the probable introduction and trading in the near future of pollution permits—which the powerful nations favour and need—the dawn of a regime of global taxes and of unprecedented international progress appears to be at hand.

THE CASE FOR GLOBAL TAXES

I was starting to write this paper on the case for global taxes when I received Fred McMahon's disputatious diatribe explaining, in his opinion, why a global tax would be "unworkable, unnecessary and dangerous." My immediate reaction was to write my paper in the form of point-by-point responses to his alarmist arguments. On reflection, however, I decided that it would be best for me to stick to my original plan, which was to write an overview, in as straightforward a manner as possible, of why global taxes are necessary, workable, and not only safe but also reliable. I shall therefore proceed with my original plan, which I summarized in an outline I submitted previously and shall follow in this paper, while suffering the slings and arrows of Fred's outrageous tirade. My basic overview will be presented in Part One, where responses to them will be made only *en passant*. My detailed responses will be in Part Two.

PART ONE: OVERVIEW

I. Paying for peace, development, and effective global governance

Peace, development, and effective global governance are, in my view, the chief concerns of the international community. That the financing of these essential activities is sorely inadequate is obvious even from a brief recounting of the existing pattern of international public financing: The United Nations' regular budget and peacekeeping accounts, as is well known, are in a constant state of chronic crisis. As a result, actions to maintain, build or enforce the peace are usually curtailed or simply not pursued because of inadequate financing. Governance and even minimal international public administration similarly suffer. Although they are supposed to be financed from assessed, *i.e.*, obligatory, contributions, governments flout these conditions of their membership in the United Nations. This is one reason why we need a more *systematic* method of financing our global needs.

The current sources of funds for development are for the most part voluntary government contributions plus, in the case of the international and regional development banks, capital subscriptions, borrowing from capital markets, return flows from past loans, and some miscellaneous interest income. Voluntary contributions, in the words of the United Nations General Assembly, are "unpredictable, inadequate and unassured." This is reflected in the decline or, at best, stagnation of official development assistance (ODA) and the declining fortunes and volume of development assistance of our international public financing institutions, such as the United Nations Development Programme (UNDP), the International Development Association (IDA), and the soft-loan windows of the regional development banks. The development banks' share capital is limited, and borrowing from capital markets can fund only conventional loans with commercial rates of interest. This is to give the banks an adequate spread between their borrowing and lending rates to make a profit and to maintain, in the language of Wall

Street, their "financial integrity." ODA as a percentage of GNP currently runs at about 0.22 per cent, or less than one-third of the universally accepted norm of 0.7 per cent.

There is thus a crying need for a more effective financing system. The current method is an example *par excellence* of international Pareto improvement—a reallocation of resources that improves the welfare of at least one party without making any other party worse off. For ODA evidently increases the welfare of the recipient country without hurting the giver since if it did hurt, then the giver would normally not give the aid voluntarily¹. But as public sector economists point out, Pareto improvements are a minimal kind of action. And the historical record of ODA shows that this is the most we can expect from an international regime of voluntary contributions. The level of ODA as a percentage of GNP is infinitesimal compared to the public transfer of resources from rich to poor in nation-states, ranging from 22 to 28 per cent in the US and the UK.² The reason, of course, lies in the fact that nation-states have formal systems of taxation whereas the international community does not—which indicates the benefits global taxes can bring.

II. The need for financing to correct market failures

While the market mechanism is enjoying a surge in popularity as a cure-all, and public finance is often viewed solely as the collecting revenues and their expenditure, it serves another important purpose in both the national and global arenas: the correction of market failures. A principal kind of market failure is the inability of the private sector to provide public goods: goods and services that benefit the public at large and are a) non-rivalrous, *i.e.*, they can be consumed or enjoyed by two or more people without lessening each other's consumption or their consumption by others, *e.g.*, world peace; and b) non-exclusionary, *i.e.*, no one can be excluded in practical terms from enjoying the good, *e.g.*, the protection of the stratospheric ozone layer,. The private sector cannot be expected to provide public goods since it is difficult or impossible to make a profit from them, where there is no marginal cost in adding beneficiaries and you cannot exclude non-payers from enjoying the good. This is why we must depend on the international public sector for the provision of international public goods. In nation-states, it is the government, or national public sector, that provides national public goods, *e.g.*, national defence, public administration, weather forecasts, and the like, financing them from taxes rather than from charges or fees to individual consumers. The charges or fees would be impossible to administer or would involve such high transactional costs as to make them unrealistic.

Another area in which the market is grossly inefficient or simply inoperative is that of "externalities". A "negative" externality occurs when a private activity, *e.g.*, manufacturing automobiles, produces pollutants that hurt other parties, and society and the environment as a whole. These external costs are not reflected in the income-and-expenditure accounts of the manufacturer (or dealer and driver). To correct this inefficiency—to "internalize" it so that the polluter pays—national governments try to regulate the volume of pollutants emitted and impose fines, or corrective taxes, on the polluters. These act both as a disincentive to pollute and a means of raising the necessary

funds to clean up. A variation on this is the issuance, sale and trading of "permits" to pollute, which is a way of making the polluters pay. This is discussed in Claudia Kemfert's interesting paper, "Different global allocation schemes of emissions permits and its impacts on world economies," and to a lesser extent in Gabriela Chichilnisky's innovative presentation, "The case for an International Bank for Environmental Settlements". Permits to pollute, in fact, are a form of corrective, or "Pigovian", taxation and could presage the acceptance of global taxation *per se* in view of the interest of the big industrial polluting nations in this approach.

As in the case of negative externalities, private goods or actions can have positive external effects—benefits that accrue to outside parties, as in the oft-cited example of beekeeping, where the beekeeper's neighbouring orchard benefits from the pollination resulting from the bees' honey gathering. In nation-states, governments subsidise activities with extensive positive externalities—such as education, which benefits not only the individual student but also society at large—since without such intervention positive externalities tend to be underproduced. An example of an international positive externality is the world's tropical rainforests, which are believed to benefit other countries and the world as a whole by acting as carbon sinks, habitats of biodiversity, and sources of enjoyment from afar. If the countries in which the rainforests are located are to be persuaded to preserve or expand them, then a much more effective approach than the exhortations of environmental groups would be to compensate those countries for the opportunity costs of conserving their forests. As in the case of global public goods, financing is an essential ingredient. Schemes such as debt-for-nature swaps and voluntary contributions have proved ineffective, the financing achieved being paltry in view of the tendency of nations and people to be free-riders. Adequate financing is a problem that requires an automatic scheme, another argument in favour of taxation.

There are many other international market failures, which I deal with in some detail in my textbook on International Public Finance.³ An illustrative comparison of national and global market failures and policy responses at the national and international levels is shown in a table at the end of this paper. Suffice it to note in the present section that one requiring substantial financial resources is that of incomplete markets. If we are to rely completely on the market mechanism, there is bound to be a shortage of capital flowing to the poor and "poor risks". This is why the least developed countries of Africa are being bypassed. The public sector mechanisms dealing with incomplete capital and insurance markets—the World Bank group, International Monetary Fund (IMF), UNDP, the regional development banks and others—are sorely inadequate. They depend on voluntary contributions, capital subscriptions, and capital markets which, because of the profit motive, as was noted previously, favour the rich over the poor. In nation-states, the government often steps in to provide insurance and capital directly, spreading the risks widely and supporting the institutions with financial resources from taxation and in some cases supplemented by guaranteed private mechanisms.

III. The present financing method: Unpredictable, unassured, and inadequate

The unreliability of the present pattern of international public financing is due mainly to the fact that the funds are provided by national governments, which are both sovereign and undependable. In part, this is due to their budgeting process. It is typically slow, unwieldy, and dominated by domestic politics and priorities. In the industrialised countries, budgets are usually for one year—the salient exceptions being the Nordic countries and the Netherlands, which do approve multi-year budgets and pledges of ODA. Most budgets are subject to legislative scrutiny and approval, legislatures are characterised by intense politicking, and there is a saying that, in the final analysis, "all politics are local".

In addition to administrative constraints, there is a more serious problem in relying on national governments for international financial resources. This is the paramountcy of perceived "national interests". Just as individuals and private organisations—the private sector in national economies—act in their individual self-interest, so do national governments in the international economy. This is why bilateral assistance programmes are notorious for not being need-based but rather politically skewed in favour of assumed allies and countries where a government believes it has vested interests. Often, "national interests" combine with ethnic factors of looking after your "own kind". This partly accounts for the generous US aid to Western Europe under the Marshall Plan, which accounted for 2 per cent of GNP, for high level of the European Union's aid to its less developed member countries, and for the speedy establishment of the European Bank for Reconstruction and Development (EBRD) for Caucasian Central and Eastern Europe compared to the years it took for the industrialised countries to agree to the creation of the African and Asian Development Banks.⁴ The "selfish gene" and ethnocentricity have been a strong factor in the altruism of the West. But it is all humankind with which we must be concerned.

IV. The global commons: utilisation, regulation, and revenues

In accordance with classical economics, the factors of production are broadly classified as land, labour and capital (often also entrepreneurial skills), and the payment for their costs expressed as rent, wages and salaries, interest (and profits). This is certainly the case in national economies, where factor incomes are an essential element for economic efficiency. Thus, "rents" accrue to land, which includes natural resources. For if resources are "free", there will be *inter alia* inefficient (and unfair) pricing and a tendency to overuse them. In the international economy, however, the global commons are generally used free of charge. It is therefore only logical to have a system of global taxes, or user charges.

The global commons may be defined as those physical attributes of the universe that fall outside national jurisdiction or ownership. In addition to the traditional, tangible kinds of geographical space and features, *e.g.*, land, bodies of water, ocean depths, air, natural resources and ecosystems, they include impalpable but nevertheless important physical facts such as the different levels of outer space, the orbits of geostationary satellites, and the electromagnetic spectrum. In other writings,⁵ I have discussed those parts of the global commons that are being increasingly used by private firms and national governments and could be the subject of taxes or user charges, both as corrective measures and for raising revenues for international purposes. These are summarised in the discussions below.

V. Fiscal measures based on automaticity

To finance the provision of international goods—especially public goods and private goods with positive externalities⁶—and the combating of public bads, one must look beyond national governments to global, nongovernmental sources and apply the findings and lessons of public finance and the experience of national tax systems. A common thread in these is the principle of automaticity, as distinct from but complementary to voluntarism, although the concept is often taken for granted since voluntarism is a minor factor in national systems. The concept of automaticity in international public financing was first discussed in an official international forum in 1977, at the United Nations Conference on Desertification (UNCOD) in Nairobi. It was developed and incorporated in concrete proposals in subsequent studies and reports, in 1978 and 1980, by the United Nations Environmental Programme (UNEP) and the Secretary-General to the Economic and Social Council (ECOSOC) and the General Assembly on financing the UNCOD Plan of Action.⁷ These proposals were first analysed in an international public finance framework in my 1992 book on the subject and augmented in other writings. They are summarised in the following overview, which is broken down into three categories: international taxation, charges for the use of the global commons, and international monetary measures.

A. *International taxation*

A foreign exchange transactions tax. The world's largest and most liquid financial market is the market for foreign exchange. Over \$1.5 trillion (15¹², following the U.S. system, \$1.5 billion following the British) worth of foreign exchange transactions take place daily, a volume exceeding the M-1 money supply of the US or the combined foreign reserves of all the world's central banks. A recurring complaint is the market's volatility, speculative outbursts and financial crises such as those that have taken place in eastern Asia and Latin America..

Nobel Memorial Prize-winning economist James Tobin of Yale has proposed taxing foreign exchange transactions to dampen speculation and give governments and

central banks more independence in the formulation of domestic monetary policy. Although these are the professed goals of the tax, Professor Tobin has noted that it could also be a "terrific fund raiser" that "could cover everything"⁸—a potential that has not been lost on people concerned with international fund raising, who have now latched on to the "Tobin tax" bandwagon.⁹

Unfortunately, the proposal faces formidable obstacles: It would entail a massive and expensive administrative structure. A universal and watertight system seems improbable, and money changers could go to low- or zero-tax havens. Banks could develop derivatives or use treasury bills and other financial instruments to avoid the tax. And most policy-makers would oppose it, crying "interference" with the now-sacrosanct market mechanism.

A Foreign Currency Exchange (FXE). A more politically viable alternative, tapping the same extensive base as the Tobin tax, would be the creation of a Foreign Currency Exchange (FXE). The present market actually comprises two tiers: an inside, interbank dealers' market, where buyers and sellers do business directly or through brokers, competition is keen, and spreads between bid and asked are narrow (about 3 to 4 basis points); and the publicly quoted captive market of end users—industrial corporations, importers, exporters, portfolio managers and individuals—where spreads are much wider (typically 10 basis points)¹⁰ They cannot trade with each other and can buy and sell currencies only with the banks, which act as dealers. The market thus suffers from the market failures of incomplete information and competitive breakdowns.

FXE would serve the foreign currency market as national bourses serve the stock markets. Through an automated global computer network matching buy and sell orders electronically, it would lower the cost to consumers of changing foreign currencies by giving them competitive rates and access to other buyers and sellers, which they now lack. FXE would also bring order, transparency, and efficiency to the present market. If properly designed, managed and sponsored, it could generate considerable revenues from licensing and transaction fees from its member traders and customers, as is done in the stock exchanges. The revenues from the Exchange could be on the order of \$126 million daily, assuming a) user charges are 0.1%; b) only 12% of the total volume of transactions, or \$180 billion daily, are for end users; and c) FXE captures 70% of the total end-user market.¹¹ If the General Assembly appropriated the funds and authorised the UN to invest in a project, say in partnership with an existing automated broker, a start can be made to accomplish this programme.

International trade. Another large potential source of financing would be a tax on international trade, since it would also have a large base. The volume of trade, as measured by total imports, amounted to \$55,552 million in 1996. Thus, an *ad valorem* tax of 0.1% would yield over \$5.5 billion, and a tax of 1% over \$55.5 billion. Trade, furthermore, has been growing steadily, at an annual rate of over 8% since 1991. A trade tax is justifiable based on the benefit criterion: trade uses the global commons, and 95% consists of goods transported by ocean freight. It would be a form of user fee. An

alternative would be a tax on ocean freight. It would be based on the same benefit criterion, although the tax incidence, at least initially, would be different.

Specific traded commodities. Taxes could also be on specific traded commodities, for instance, internationally traded oil, other exhaustible materials such as the other hydrocarbons (coal, oil, and natural gas), mineral raw materials (aluminum, copper, iron, lead, nickel, manganese, tin, zinc, and other minerals), or manufactured goods. Taxes on raw materials could be justified on the grounds of conservation and Pigovian principles.

Corrective, or Pigovian, taxes. A precedent for corrective, or Pigovian, taxes exists in the Montreal Protocol on Substances that Deplete the Ozone Layer, the main culprit being chlorofluorocarbons (CFCs). It provides for assessed contributions to a multilateral fund based theoretically on each country's share of the production of CFCs.¹² The protocol thus serves the dual purpose of discouraging the production of CFCs and raising funds, which are used to help developing countries develop ozone-friendly technologies. Pigovian taxes could be applied with similar goals to polluters of the marine environment. The feasibility of combining the goals of discouraging certain activities through corrective taxation with resource mobilisation is illustrated by the measures carried out in the US to penalize cigarette making and smoking while at the same time raising funds from the tobacco companies to pay for (internalise) the social costs of the tobacco industry; in fact, certain municipal bonds are issued backed by expected revenues from the tobacco companies.

Military expenditures and arms transfers could also be taxed on the basis of Pigovian principles. Since their volume is tremendous and their public bads particularly severe, taxation could serve the double purpose of raising funds and reducing the volume of activities that produce global negative externalities. It would transfer resources from national military budgets to the UN's peace-keeping accounts. Unfortunately, this would be an incentive for governments to hide their military expenditures under other budget items. It would require an effective enforcement authority or strong political will, as in the case of the Montreal Protocol, to surmount this and other practical problems.

Leases and the sale and trading of permits to pollute. These are another potential source of revenues with the added benefit of charging the polluters for their pollution and other social costs. For example, long-term or quasi-perpetual leases could be given to private parties to exploit certain areas, *e.g.*, fishing nations could be assigned specific areas of the oceans in which only fish of a particular species, such as tuna, might be caught. Those fishing nations and organizations which were granted the leases would be motivated by their own self-interest to maintain sustainable yields in these fisheries.

Another means of internalizing the social and environmental costs of pollution is the sale and trading of permits to pollute. This is being dealt with in other papers, suffice it to note here that these permits are a form of taxation and may be the cusp that ushers in a new global tax regime.

Positive externalities. Taxes can also be levied to provide a source for encouraging positive externalities. For instance, the tropical rain forests, which are located mainly in developing countries, confer “utility” on other countries—mainly the industrialized—where they are studied in schools, shown on television and magazines, enjoyed by environmentalists and said to be the “lungs of the earth” and the last bastions of biodiversity. The developing countries are exhorted not to utilize their rain forests for economic purposes, but there are no serious attempts to compensate them for the opportunity costs of conservation or to promote the generation of positive externalities, whose returns these countries are unable to capture. Many developing countries also train physicians, nurses, scientists, engineers and other technical people who migrate to the developed countries, which benefit from their ready-made know-how. Yet, it is mainly the migrant laborers and household workers and not these trained expatriates who remit earnings to their relatives back home. The exporting countries thus do not capture the positive externalities enjoyed by the recipient countries.

B. Charges for the use of the global commons

Another way of generating international public funds is through charges for the use of the global commons, which we previously defined as those physical attributes of the universe lying outside national jurisdiction or ownership. The United Nations uses the term “common heritage of mankind,” which is more extensive in that it implies an obligation to preserve them for future generations. So far, the “common heritage” designations include the moon and other celestial bodies and the deep ocean bed and the subsoil thereof. A case can be made for including the high seas, international air space, Antarctica and the Southern Ocean, the geostationary orbit, and the electromagnetic spectrum under the concept of the global commons, or *res communis*.

Despite efforts by various countries to enclose parts of the international commons or to treat them as a free resource, there are extensive areas that remain unappropriated and can generate substantial revenues for international governance. A system of user rights, regulations and charges is necessary if these universal resources are not to be misused or degraded or to be overused and exhausted. Such a régime, together with international taxation, could also provide substantial revenues for a system of global governance.

The oceans. The oceans, as a means of transport, a carbon sink and a regulator of weather, are an international public good.¹³ The high seas, however, according to customary international law developed by the Western shipping countries since the time of Grotius, their most successful lawyer, have been considered free resources. It would be in accordance with their status as *res communis*, however, for the global community to charge user fees for the use of this part of the global commons, through the international trade tax mentioned above.¹⁴

Overflight. Like the high seas, international air space provides a passage for international transport. Since it lies outside national jurisdiction, is used by aircraft of various nations and is congestible, there is logic behind having the international public sector assert global ownership and charge user fees. One way this could be accomplished is through a surcharge on international air tickets, a proposal suggested by former Secretary-General Boutros Boutros-Ghali, but not repeated since an outcry by a group of US congressmen.

Antarctica and the Southern Ocean. During the "age of exploration," much of the territory outside Europe was considered *res nullius*, or belonging to no one, and claimed by the Western world. A number of countries have similarly laid claim to Antarctica and established a régime over the continent under the leadership of this exclusive club of mostly powerful industrialized countries, the Antarctic Treaty Organization (ATO).

The United Nations should assert its interest in Antarctica and aim eventually to declare it part of the common heritage of mankind. The future of Antarctica could then be considered with respect not only to the maintenance of peace on the continent but also to the welfare of the entire community of nations, rather than be decided by a small alliance of the developed world and a few claimants from the South. This would give the United Nations a basis to levy user charges and Pigovian taxes on industrialized nations which could decide, once they have acquired the technology, to develop the continent.

The Southern Ocean can similarly be considered part of the common heritage of mankind. It is questionable whether any claimants can declare exclusive economic zones in the region. Many nations fish the Southern Ocean for krill, whales and other fisheries resources, in which it is rich. There are grounds for charging user fees on this exhaustible resource.

Parking fees for geostationary satellites. The geostationary orbit is a unique band of outer space encircling the equator at an altitude of approximately 22,300 miles. It has already become congested and dangerous. Because of the speed and direction of the earth's rotation, a satellite moving in this orbit from west to east at a speed of 6,800 miles per hour is "parked" at a fixed position in relation to the earth's surface.

Governments, private firms, and mixed companies have placed satellites in such positions in the orbit, with substantial profits and other benefits to themselves. The equatorial countries have not been successful in asserting sovereignty over the orbit, which could be appropriated by the United Nations as part of the global commons. It would make economic sense to charge "parking fees" for the satellites. Estimates I have made indicate that revenues could be as high as \$14,000 million annually by the year 2010.¹⁵ The UN could also provide sorely needed rules and governance over the orbit.

The electromagnetic spectrum. Another special attribute of the physical universe that can be properly regarded as part of the international commons is the electromagnetic spectrum: the range of frequencies of electromagnetic waves from the

lowest frequencies, the radio waves, to the highest, the so-called cosmic rays. User rights are assigned by the International Telecommunications Union (ITU). Thus far, 90 per cent have been assigned to the richest countries. User rights could be accompanied by user fees, as is done in the US, in the form of small national surtaxes for international purposes.

C. Monetary and other measures

In addition to taxing and tapping foreign exchange transactions, discussed at the beginning of this section, there are two measures of a monetary nature, with considerable possibilities for fund raising, that are worth revisiting: Special drawing rights (SDRs) and IMF gold holdings.

Special drawing rights (SDRs) and development. Effective international monetary policy is an essential public good.¹⁶ Unfortunately, IMF policy is dictated by the central bankers and treasury officials of the Group of 10 (the world's most industrialised countries), and the world's needs are seen in terms of the Group of 10's needs. It is on this basis that the IMF decides whether or not the level of global liquidity is adequate. Although the amended IMF statutes creating SDRs stated that SDRs should become the world's principal reserve asset, the IMF has not issued any since 1981 except for a special one-time allocation in 1999 aimed mainly to accommodate the new members from the former Soviet bloc. The IMF's previous Managing Director was urging a new issue of SDRs, with increasing support from developed countries. The views of the new Managing Director are not yet clear, but the IMF should keep the matter under continuous review, taking into account the need for liquidity not only of the Group of 10 but also the developing countries. It should also consider anew the possibility of linking them with development, peace-keeping and the needs of future financial crises.

Gold-development link. The IMF still has 103 million ounces of gold in its coffers. Even at the current depressed price, in the neighbourhood of \$275 per ounce, this is worth over \$28 billion. The IMF could sell all or part of its gold holdings over a period of time and use the proceeds for development, peace-keeping and other governance purposes. The IMF did this in the late 1970s, when it sold 25 million ounces of gold and placed the proceeds in a trust fund for the provision of balance-of-payments assistance to developing countries at concessional rates from 1978 to 1981. A repetition of such action would be in line with the avowed purpose of the IMF to phase out the role of gold in the international monetary system. Plans for the sale of part of its gold holdings were recently killed by the gold-producing countries, which claimed that the sale would depress gold prices, but the IMF was able to revalue its gold holdings. The IMF should continue its efforts to convert its gold holdings into usable resources, and should use these resources for the developing countries.

VI. Distribution and alleviating poverty

World-wide poverty continues to be a chronic and seemingly intractable problem. This is reflected in the low income estimates, inadequate housing, sanitation and amenities, low literacy and longevity rates, and other measures. Comparisons of income distribution within and among nations using Gini coefficients shows the latter to be worse and deteriorating. And yet, national redistribution programmes are far more substantial, progressive, and effective at achieving their goals than the current pattern of international redistribution: intranational redistribution ranges from at least 22 to 28 per cent of national income in the US and the UK. The public flow of resources from rich to poor countries has at best stagnated over the years, and is currently about 0.22 per cent of GNP. This is also reflected in the recurrent introduction and failure of initiatives for Africa. The New International Economic Order, proposed by the General Assembly in the 1970s and calling for a share by the developing countries amounting to 20 per cent of world production, was quickly shot down by the industrialised countries. One of the main reasons for this disparity is the existence of progressive systems of taxation by national governments and their use to finance programmes of benefit mainly to the poorer segments of the population. Income redistribution is one of the main functions of fiscal policy and public finance in nations. But it is practically absent in the international sphere, as was noted previously, consisting entirely of ODA which currently amounts to 0.22 per cent of the GNP of the rich countries.

VII. Feasibility

One of the most strenuous criticisms of proposals for global taxation concerns its feasibility. An examination of the actions that must be taken if a system of global taxation is to be adopted and implemented indicates that it is feasible from a technical, legal, and administrative point of view. These are not immodest claims, excluding as they do any assertions of political acceptance.

Procedures for international taxes such as those described here could be put into effect *within* the existing international political system. For a global tax system, what is essentially required is a convention, or multinational treaty. At a minimum, it should deal with: (a) the definition of the tax base, (b) the establishment of the tax rate, (c) the method of collecting the tax, (d) the initial disposition of proceeds, (e) conditions for the treaty to enter into force, (f) sanctions against treaty violators, and (g) the procedures for withdrawal. Provision might also be made for review of the treaty after a specific period, or for its automatic termination at a fixed date, unless the parties reaffirmed their ratifications.

The treaty could include a ceiling on tax rates, so that the tax liability of corporations and citizens of each country would not be open-ended. It could provide a certain flexibility in rates. Differential tax rates could be used for distributing the tax

burden more equitably. The treaty need not deal with all of these subjects definitively. It could sketch the broad outlines of the proposed tax and leave the filling in of details to a standing body representing the parties to the treaty. This body could, for example, be given the authority to handle specified procedural and administrative problems and even to adjust tax rates within stated guidelines. The composition of the body and how it is constituted are political matters that would also have to be negotiated. But, as the historical record shows, there have been difficult but ultimately successful conferences and negotiations for the establishment of complex treaties and related institutions, such as the United Nations Charter, the United Nations Convention on the Law of the Sea (UNCLOS), the World Trade Organisation (WTO) and, on a regional scale, the European Union (EU), which has a system of international taxation through the allocation by member governments of specified portions of their Value Added Tax (VAT) revenues to the EU.

PART TWO: REJOINDER

Having presented my short overview of the case for global taxes, I shall now grasp my protective shield and hold it up to Professor Fred McMahon's slings and arrows. Although I have had the chance to read his paper, I do not believe that I should be writing from an unlevel "playing field" since he also had read some of my writings on what he calls a "menu of Mendez taxes", which he has treated as fodder for his tirade.

I should like to start by noting that we are on the same side *vis-à-vis* the Tobin tax—but for different reasons. I believe, contrary to his claims, that a tax on currency transactions, if it were successfully implemented, would be very effective in taming the present volatile currency markets. Currency traders typically make their profits from narrow spreads and huge volumes, but these profits would be easily eliminated by even a small transaction tax. For if you can make a profit of 1 per cent of the volume of currency traded by buying and selling that currency in a single day, then a tax of 0.5 per cent would wipe out that gain and thus make it unprofitable and unattractive for the traders. This would not be true for long-term investors, who are interested in a different dimension of finance.

My doubts about the Tobin tax concern the possibility of tax avoidance by money changers moving off-shore, by their trading in liquid financial instruments rather than currencies, and—most serious of all—the fact that all proposals made so far are for a *national* tax levied by the governments of the countries where the transactions take place. Except for Singapore and Hong Kong, the money centres are in the developed countries. But the need for increased revenues and volatility control is now greatest in the developing countries and countries in transition, which have become the favourite prey of the speculators, and are also victims of skittish portfolio managers and corporate treasurers. If the tax were a national tax collected by the handful of countries where trading is greatest it would take some doing to convince them to divert the revenues for

public international purposes, say as ODA. If these obstacles can be surmounted—for instance, through tighter and more effective global governance, and by the enforcement of an international treaty obligating all countries collecting the tax to allocate them for specified international purposes, and providing for sanctions against violators—then it could play a valuable dual role in bringing order to the present global monetary anarchy and raising unprecedented international public revenues.

The foreign currency exchange (FXE) I have proposed would probably be more politically acceptable than a Tobin tax and could raise similar quantities of revenues. Although not aimed *per se* at reducing volatility it could also facilitate, should its overseers so desire, the operation of a Tobin-type tax. In any case, FXE has a tremendous potential for generating revenues in view of their identical tax base. It would collect these revenues through transaction fees similar to those of bourses, or stock exchanges. By providing *brokerage* services to buyers and sellers of foreign currency it would widen the market to include the end-users and provide more favourable rates than the present dealer-driven two-tier market, thus becoming the end-users' market of choice.

McMahon's skepticism about the potential of FXE brings to mind the vignette of two theoretical economists taking a walk together; one economist spots a one-hundred-dollar bill on the ground, picks it up, and shows his good fortune to the other, who argues that this is impossible since if there were really a one-hundred-dollar bill lying on the ground, someone else would already have picked it up. In fact, there are many reasons why a foreign currency exchange has not yet been established. These include the power of the banks—which, I am sure, McMahon recognizes—which dominate and control the two-tier foreign currency market. In this market, it will be recalled, there is no brokerage mechanism to match buyers and sellers, as in the case, for instance, with the New York Stock Exchange. The end-users therefore have no option but to buy from or sell for the inventories of the banks, which do trade with each other while acting as dealers for the public in a similar way to the Nasdaq and bond markets. The technological revolution, furthermore, has spawned a new generation of fast and efficient electronically automated securities exchanges. The new technological advances could be used for an automated FXE.

McMahon's seemingly knee-jerk contrarian comments are too numerous to deal with point-by-point. He opens with a statement that "the establishment of a global tax faces intractable problems every step of the way, from implementation to collection to administration". The devil's advocate, we are warned, is in every detail, and I do not wish to write a seemingly endless paper. He states, furthermore, that "the most dangerous difficulties lie in the related issues of governance and distribution of tax receipts"—a warning that, had it been heeded, would have blocked the establishment of the World Bank, the IMF, all of the regional public financial institutions, and even the UN and all of its development subsidiaries. As I delve further into the text, furthermore, I find that he is an apparently complete free-market romantic, who equates the correction of market failures with central planning—a disciple of Peter Bauer, the Jerry Falwell of the Economics profession. Rather than pack up and go home, however, I shall try to cope with his attacks, limiting my response to the following:

a) There are many arguments in favour or against a trade tax, and many questions about it. It is tempting to write *in extenso* for one side or the other. I have discussed these in some detail in my book, *International Public Finance*, and other writings listed in the bibliography, which would be too long to repeat here. Suffice it to say for the moment that many of the arguments McMahon makes, *e.g.*, depressing effects on the world economy, impracticability of administration, complexity, unfairness, and the like, have been similarly levied against the US and other national tax systems.

b) Tax avoidance, administrative, and other problems characterise national systems of taxation. Should national taxes therefore not have been established and now be scrapped? Despite his protestations, it is doubtful that a global tax would be more complicated than say the US income tax laws.

c) McMahon claims a different set of difficulties for the global arena. There is, of course, a need for an infrastructure for tax collection, and such an infrastructure exists potentially in the customs offices, administrators, and experience that almost all countries have. As to whether and how the necessary international institutions could be run, the world community has had extensive experience in the establishment and operation of international institutions such as the United Nations, the traditional specialized agencies, the Bretton Woods institutions, the regional development banks, and others. The world community also has had ample experience in negotiating the relevant treaties and conventions. They are difficult to achieve, but there also have surprising successes, such as the UN itself, the Law of the Sea and its organs, GATT and WTO, the World Bank, IMF, and so on. They are not complete successes, but it is better to have a glass half full than an empty one.

d) I stand by my contention that all of the changes required can be carried out technically, administratively, and legally within the perimeters of the existing international political and juridical order, *e.g.*, that we do not have to establish a world federation beforehand (although I am not against it). In my discussion of the steps to be taken in the establishment of global taxes (see section on Feasibility of this paper and Mendez 1992 pp 218-219), I show how it can be done within existing international law, norms, and procedures. I do not claim smooth political sailing, but more on this later.

d) The "Bhagwati tax" is one of many which have an economic and ethical rationale but must be appraised in terms of political and national juridical considerations. Although not presented initially within a public economics framework, it can be seen as a way for the developed countries to compensate generators of positive externalities—the countries of origin of the highly trained emigrants, who benefit the receiving countries and do not produce returns that can be captured by their home countries.¹⁷ Such taxes have existed for some time, such as the exit taxes of the Russian Federation and the former USSR, although Bhagwati's point is that it is the beneficiaries, including the recipient countries, which should pay the taxes.

e) A tax on arms transfers looks dicey, but it would be easier to implement than a tax on national military expenditures (the point being that international trade activities are easier to monitor than the national activities, say of Iraq and Israel cited by McMahon). I see that Dr. Michael Brzoska is presenting a paper on this subject.

f) McMahon's objections based on questions of democracy, taxation without representation, and others hark back to fundamental issues of value systems. But are these the burning questions of international public finance? Does freedom precede prosperity (and repression precede poverty), or vice versa? Or are there more factors in the equation? Can Asian values exist, or does the West monopolise this field? Does China need Western style democracy? Is direct superior to representative democracy? Are the Bretton Woods institutions democratic or plutocratic? Which has more power: the democratic General Assembly or the oligarchic Security Council? In fact the present system favours the powerful.

g) Is the correction of market failures a throwback to central planning or a necessity for an efficient and well balance mixed economy?

CONCLUSION

This paper has attempted to provide an overview of the case for global taxes. This case reflects the financial requirements of the international community's soaring and urgent needs. These requirements can be met only through a fundamental and innovative reform of the international public financing methods used today, which are gravely flawed. The paper has summarised the main defects of the *status quo* framework: its excessive reliance on government contributions which are overwhelmingly voluntary, unpredictable, inadequate and unassured. The world's financial requirements need an element of automaticity, as is found in all national tax systems. Global taxation, reaching beyond governments to transnational corporations and other firms, as well as individuals, can no longer be avoided—as was the case when the United States in 1913 finally amended its constitution to establish the income tax, which had hitherto been unconstitutional. Global taxes can be created to finance the bulk of international public expenditures, supplementing voluntary contributions much as government supplements charitable contributions in nation-states. They can also serve the purpose of correcting international market failures and promoting distributional equity of income among and across nations.

I have cited and summarised a number of concrete kinds of taxes and charges for the use of the global commons, together with monetary measures that also could generate resources through an extra-governmental route. An analysis of the taxes, other measures and related factors shows that they are technically, legally, and administratively feasible within the present international dispensation. The most formidable obstacle is political. More open, far-sighted, and constructive attitudes, however, are evolving. The

industrialised countries are tending to favour the issuance of tradeable international pollution permits. Such pollution permits, which would have a price proportional to the social and environmental costs of the pollution activities, would be a kind of tax. Their adoption should thus ease the way for a system of international taxation.

In a 1993 review of my book, *International Public Finance: A New Perspective on Global Relations*, Professor Jeffrey A. Frieden of Harvard (then at UCLA), wrote

Ten years ago, the arguments Mendez presents might have appeared eccentric; today they seem only visionary, and they may indeed be prophetic.¹⁸

And today, with the start of a new century and millennium, the dawn of global taxation appears to be at hand.

TABLE

Illustrative table of national and international market failures and policy responses

FORM OF MARKET FAILURE	<i>NATIONAL (MAINLY THE U.S.)</i>		<i>INTERNATIONAL AND GLOBAL</i>	
	EXAMPLE	POLICY RESPONSE	EXAMPLE	POLICY RESPONSE
<i>Public goods</i>	Lighthouses Highways Maintaining law and order	Government provision, financed from taxes and user charges National guard, conscription	Protecting the ozone layer Information superhighway Peace-keeping	Montreal Protocol None UN peacekeeping, NATO
<i>Negative externalities</i>	Urban air pollution River pollution by paper mill	Clean air act Regulation	Emission of CFCs Marine oil pollution	Montreal Protocol None
<i>Positive externalities</i>	Education Polio vaccination Home ownership	Govt provision, subsidies, tax breaks Government provision Tax deductibility of interest costs	Education (“reverse brain drain”) Smallpox vaccination Maintaining rain forests	None WHO program Debt-for-nature swaps
<i>Competitive breakdowns</i>	Standard Oil Co. (US) Railroad monopsony Natural monopolies	Sherman Anti-trust Act Promotion of competition Regulated public utility	OPEC US and EU auto markets Agricultural subsidies	Petrodollar recycling None GATT/WTO
<i>Information failures</i>	Effects of tobacco Interest rates on loans Investment information	Surgeon-General’s warning Truth-in-lending Full disclosure at NYSE + SEC	Nuclear testing Two-tier forex market	None None
<i>Incomplete markets Merit goods</i>	Credit for small business Insurance for the elderly Music and the arts	SBIC Medicare, Medicaid Subsidies, tax breaks	Capital & credit for LDCs Balance-of-payments insurance Preserving historic treasures	World Bank/IDA IMF (in theory) UNESCO Abu Simbel program

ENDNOTES

¹ In fact, the donor government often also feels moral as well as commercial gains.

² Mendez 1992, pp 97-99; O'Higgins and Ruggles 1981; Ruggles and O'Higgins 1981.

³ Mendez 1992.

⁴ A partially analogous case is the Federal Republic of Germany's aid to the former German Democratic Republic upon unification—in the region of \$100 billion annually, or almost twice the total global ODA at the time.

⁵ Mendez 1992, 1995b, & 1997.

⁶ There is a nuance between public goods and private goods with externalities: the former is or can be enjoyed or consumed by everyone equally, whereas in the latter the private consumption or enjoyment of the good is different from the good's external effects.

⁷ UNCOD (1977) and UN documents (1978) and (1980). As economic adviser of the UNCOD and UNEP secretariats, I served as the rapporteur of the relevant expert groups and editor of these reports, which are listed in the bibliography. The proposals were first developed and published in an international public finance framework in Mendez 1992.

⁸ Personal remarks to the author during discussions in 1993 for the author's presentation of the proposal to the Commission on Global Governance.

⁹ For instance, see Haq *et al* (eds.), containing papers on the Tobin tax commissioned by UNDP's Office of Development Studies.

¹⁰ One basis point = 1 digit in the fourth decimal place of a foreign exchange price quotation.

¹¹ This proposal is explained in more detail in Mendez, 1995a, 1995c, 1995c, 1996a & 1996b.

¹² In practice, the assessment formula of the UN regular budget is used.

¹³ This is not true of the oceans as fisheries since fisheries resources are limited, and their consumption is rivalrous.

¹⁴ The questions of Antarctica and the oceans are discussed in greater detail in Independent World Commission on the Oceans 1998 & Mendez 1994.

¹⁵ Mendez 1992 pp253-8.

¹⁶ *E.g.*, see Kindleberger.

¹⁷ As noted previously, it is the unskilled emigrants who remit foreign exchange back home. Regarding my source. (*vide* McMahan p 15 fn) it is first hand knowledge and observations of various immigrant groups, as corroborated by my cohorts.

¹⁸ Book review by Jeffry A. Frieden in the *American Political Science Review*, Vol 87, No. 4. Dec 1993, pp. 1059-1060.

References

Frieden, Jeffry A. 1993. Book review in the *American Political Science Review*, Vol 87, No. 4. Dec. pp. 1059-1060.

Haq, Mahbub ul, Inge Kaul and Isabelle Grunberg (eds). 1996. *The Tobin Tax: Coping with Financial Volatility*. New York: Oxford University Press.

Independent World Commission on the Oceans, chaired by Mário Soares. 1998. *Report: The Ocean and Our Future*. Cambridge: Cambridge University Press.

Kindleberger, Charles P. 1986. "International Public Goods Without World Government". *American Economic Review*. Vol. 6, No. 1, March. (Inaugural address as President of the American Economic Association)

Mendez, Ruben P. 1992. *International Public Finance: A New Perspective on Global Relations*. New York: Oxford University Press.

_____. 1994. "Ocean Governance and Development: The Question of Financing," in *Ocean Governance; Sustainable Development of the Seas* (edited by P.B. Payoyo for the International Ocean Institute) Tokyo: United Nations University, 1994. pp. 309-329

_____. 1995a. "Harnessing the Global Foreign Currency Market: Proposal for a Foreign Currency Exchange (FXE)," in Commission on Global Governance, *Issues in Global Governance*, Amsterdam: Kluwer Law International, 1995. (A companion volume to the Commission's report, *Our Global Neighborhood*, Oxford University Press, 1995). pp. 425-441.

_____. 1995b. "The Provision and Financing of Universal Public Goods", in Desai, Mehgnad and Paul Redfern (eds.). *Global Governance: Ethics and Economics of the World Order*, London: Pinter Publishers, 1995. pp. 39-59. (Originally published by the London School of Economics, Centre for the Study of Global Governance. Discussion Paper 7 Dec 1993)

_____. 1995c. "Paying for Peace and Development", *Foreign Policy*. No 100 Fall 995. 19-31.

_____. 1996a. "Une Bourse mondiale des devises," *le Monde diplomatique*. February 1996; (reprinted in *Scénarios de la mondialization* (Nov. '96), a selection of 32 best articles published by *le Monde diplomatique* during the year. pp. 91-92)

_____. 1996b. An updated version of the above chapter was published by the *Review of International Political Economy* (Autumn 1996, vol. 3, no. 3) as the lead

article, pp. 498-512, in a “Debate” with comments by Stuart Corbridge and Alan Hudson of Cambridge University, “Plausibility, imaginative geographies and a global foreign currency exchange: comments on Mendez,” and Christian Chavagneux of the University of Paris (Dauphine), “FXE: a bad answer to good questions,” pp. 513-522, and my response, “Variation on a Theme by Tobin.” pp. 523-527.

_____. 1997. "Financing the United Nations and the International Public Sector: Problems and Reform". *Global Governance*. 3 (1997) 283-310 .

_____. 1999. "Peace as a Global Public Good," in Kaul, Ingeborg, Isabelle Grunberg and Marc A. Stern (eds). *Global Public Goods: International Co-operation in the 21st Century*. New York: Oxford University Press, 1999. pp. 382-416.

O'Higgins, M. and P. Ruggles. 1981. "The Distribution of Public Expenditures and Taxes Among Households in the United Kingdom". *The Review of Income and Wealth*, Series 27. no. 3.

Organisation for Economic Co-operation and Development. *Development Co-operation* (published annually) Paris: OECD.

Ruggles, P. and M. O'Higgins. 1981. "The Distribution of Public Expenditures and Taxes Among Households in the United States". *The Review of Income and Wealth*. Series 27, no. 2.

United Nations Documents

Study on Financing the United Nations Plan of Action to Combat Desertification (submitted by the Secretary-General as an Annex to his report to the General Assembly, doc. A/35/396, 17 Sept 1980).

Additional Measures and Means of Financing for the Implementation of the Plan of Action to Combat Desertification (UNEP document GC.6/9/Add.1, submitted by the Secretary-General to the General Assembly with doc. A/33/260, 6 October 1978). UNEP, 1978. [The first time proposals for new means of financing involving automaticity and the global commons were presented at an official international forum.]

Unpublished Material

United Nations Conference on Desertification (UNCOD). 1997. *Informal Note by the Secretary-General of the Conference to the Committee of the Whole*. DESCONF/CRP.3, 31 August 1977. (The first time the question of fiscal measures based on automaticity was presented officially to a UN conference. Issued as a Conference Room Paper, which does not form part of the official , or published, records of United Nations conferences.)