Funding the Future

Bring on the Common Consolidated Corporate Tax Base

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As the FT notes:

Ambitious plans for a pan-European corporate tax system that gained new momentum at a summit of European leaders on Friday could push up compliance costs for multinationals, according to a report by Irish business groups.

This is a plan for what is called the Common Consolidated Corporate Tax Base. What this means is that the entire profits that a group makes inside the EU will be calculated for tax purposes under common rules and then apportioned to states on the basis of a fomrula which determines the proportion of their real economy activity that takes place in each location.

It seems glaringly obvious as a result that the cost of compliance on the part of companies will, inevitably fall. They will only have to be involved in more than one country for the number of tax computations that they prepare and submit to at least half. This is why the largest business lobbying group in Europe has come out in favour of this proposal.

Ireland objects. The reason is obvious. They hired Ernst & Young to prepare their report, which says that the cost of compliance will increase. There is no logic to this. They also claim that jobs will be lost. This assumes that any increase in corporation tax does, of course, result in direct job losses. This is a myth, based on extraordinary assumptions, put forward by neoliberal economists, led by Prof Mike Devereux at the Oxford Centre for the Non-Taxation of Business. The simple real truth is, as they know, that they will lose out massively with regard to the amount of profit recorded in Ireland if this scheme is to be put in place. That is the beginning, and end, of their objection. They want to continue to abuse the tax laws of other countries. Thankfully, their objection is so transparent it is easily dismissed.

There are, however, unfortunately some who do, at least in part, side with Ireland. Almost inevitably David Gauke, the UK Treasury minister who is probably the best friend of tax havens to ever occupied that position, is one of them. The FT reports:

David Gauke, exchequer secretary to the UK Treasury, said in November that he did not want Britain to be a full participant, although it should engage in the debate.

He said: “The tax base should be decided by directly elected politicians.”

As usual, David Gauke fails completely to understand the real issues in question. as the UK tax academic, Thomas Rixen has shown, there are three variables in the equation that a state can set with regard to corporate taxation. The first is the tax base. The second is the tax rate and the third is the limit of their tax sovereignty. Unfortunately, of the three you can only control two at any one time. So a state can set the tax rate and the tax base if it wishes, but its tax sovereignty is then subject to challenge. And so on. This is, as Thomas Rixen argues, a process that is exacerbated by our existing arrangements on double tax agreements and the so-called arm's-length pricing model, which rarely serve their purposes, but which in combination ensure that the process of tax competition has mechanisms through which it can be pursued.

The Common Consolidated Corporate Tax Base explicitly recognises the problem to which Rixen refers. It acknowledges that tax sovereignty cannot be maintained unless there is international cooperation. But if tax sovereignty is compromised by agreeing to allow the tax base to be calculated cooperatively then the tax rate can be set nationally, and tax sovereignty can as a result be asserted to significant effect by allowing that rate be used as a mechanism in determining overall economic policy. In other words, if profits were allocated to a state then it might choose to offer a very low tax rate on the resulting allocated profits and use that as an incentive to encourage companies to bring inward investment into a state of the sort that triggers the allocation of profit which would then obtain beneficial tax treatment. Given that one of those inward allocations would inevitably relate to the number of people employed within the state, this could be used as a very effective mechanism in undertaking tax competition, and is the exact opposite of the outcome that Ireland predicts.

Now I don't suggest the tax competition is necessarily a good thing, but I do believe that tax should be paid where profit really arises. And I'm also quite confident, in the light of recent tax protest, the people are not going to put up with low corporate tax rates for long. These are now politically implausible. The result is, I think, that the CCCTB might actually deliver a great deal of benefit. Profits will be appropriately allocated. Business costs of compliance will be reduced. The waste of time of transfer pricing procedures inside Europe will be eliminated. And if profit really arises in a location then it will be taxed there, at the rate which is accepted as appropriate by the local democratic process. I can live with that. It's a shame that those who seek to undermine international taxation cannot.