Funding the Future

The tax reforms needed if globalisation is to work

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IPPR produced a report on globalisation last week. With a forward by Lord Mandelson the report was written by Will Straw and Alex Glennie.

I admit I don't agree with either Mandelson or Straw; they have a political perspective I don't always share but this report has merit to it, as others have also noted since its publication. It represents a clear change of heart on Peter Mandelson's part, and that I welcome.

The report is especially strong on the need for corporate tax reform. Having noted that profits are rising as a trend t also notes that there is a steady fall in corporate tax receipts as a proportion of profits and realises this is an issue that has to be addressed. It dismisses the alternative to corporate tax proposed by Oxford University and Mirrlees, which is a form of Value Added Tax. As the report rightly notes there is no doubt this would be regressive and so unacceptable. Instead it suggests five reforms, as follows:

First, the European Union should implement the Common Consolidated Corporate Tax Base (CCCTB). Under the current tax regime, multinationals file separate accounts for each country in which they operate; under the CCCTB, each company would compute only its EU-wide consolidated profit, on a common definition of the tax base. This profit would be allocated to member states on the basis of an apportionment formula containing factors such as shares in employment, payroll, assets and sales. Each member state would retain autonomy to tax its allocated share of profits at its own tax rate. This approach would allow countries to retain their own tax rate and pursue healthy tax competition. But within the EU, companies would have to actually move their staff and physical capital to the lower-tax regimes, rather than relying on the accounting mechanisms outlined above. In time, other jurisdictions could be encouraged to join, paving the way for an eventual global consolidated tax base.

Second, the EU and its member states should begin discussions with the International Accounting Standards Board to introduce a requirement that all multinational corporations report sales, profits and taxes paid in all jurisdictions in their audited *annual reports and tax returns in what is known as country-by-country reporting. Country-by-country reporting discloses the profits that companies record in each jurisdiction in which they operate and the taxes that they pay on them. This means that they can be held accountable for what they do and do not pay. The requirement would complement the CCCTB by providing simple transparency on the activities of multinational companies in jurisdictions outside the EU.*

Third, other jurisdictions should be encouraged to adopt the EU Savings Taxation Directive as a means of creating an automatic exchange of taxation information. Since 2005, the directive has ensured that paying agents either report interest income received by taxpayers resident in other EU member states or levy a withholding tax on the interest income received. In Cannes, Indian prime minister Manmohan Singh called for the G20 to take a lead on the issue 'in the spirit of our [2009] London Summit that [said] "the era of bank secrecy is over"' . But the communiquÃ© only committed to 'consider exchanging information automatically on a voluntary basis as appropriate'. The EU should also adopt an amendment to the savings directive which would close existing loopholes and prevent tax evasion by stopping taxpayers from channelling interest payments through trusts and intermediate tax-exempted structures.

Fourth, as the Financial Action Task Force has already recommended, the beneficial ownership of companies, trusts and foundations should be on the public record. This would prevent multinational corporations from using networks of international subsidiaries to transfer profits and reduce their tax liability. This reform would also have the added benefit of making money laundering and the handling of illicit funds more difficult.

Fifth, bilateral and multilateral donors should support developing countries in building their tax collection and enforcement agencies.

Taken together, these measures will act to reduce the power of tax competition and lower the incentives on companies to execute tax arbitrage strategies.

There is much in here that is based on my work, that of the Tax Justice Network and colleagues in the Task Force on Financial Integrity and Economic Development. I welcome that.

I welcome Peter Mandelson and Will Straw seeing the merit of these ideas over those that were technically presented to them by economists as superior, but which ignored the political realities of taxation.

The tide is turning: the merit of international cooperation on tax is becoming apparent. It will help get us out of the mess we're in: that's now indisputable by all those except the governments of those states that promote tax evasion and those who benefit from it.