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G20 – Group of Twenty
Measures to reduce aggressive tax avoidance by multinational corporations

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Introduction

Taxation is the method used by governments to raise funds for critical social infrastructure, such as healthcare and defense. All institutes in an economy are required to contribute. However one institute, the multinational corporations, are constantly finding legal ways around paying tax. In recent years the public has become more aware of issue of tax avoidance. In turn, this has propelled governments to act on tax avoidance, however it is clear to see, that multinational corporations are still not paying their fair share of tax, for example according to the guardian newspaper starbucks payed £8.6 million in tax in the UK, between the years 1998 and 2015, despite £3bn worth of sales in that same period, which is a tax rate of 0.5%. For reference wikipedia lists the official UK corporate tax rate is 21%.

Tax avoidance is a crucial issue, to which a solution has to be found. However it is incredibly challenging to find a solution, as there are many different views on tax avoidance. Tax havens profit hugely from tax avoiding multinational corporations and they stand to lose a significant portion of their income if it were to be eradicated, this compares to non-tax havens which are losing huge amounts of money in lost tax. As well as the complicated issue of finding a way to crack down on tax avoidance, as it is within the law.

Definition of Key Terms

Tax avoidance

Using legal methods to lower the amount of tax paid to the government. This should not be confused with tax evasion, which uses illegal methods to lower the amount of tax paid to the government.

Multinational corporations

A corporation is generally only considered a multinational corporation if it has large operations in multiple countries it operates in.

Tax Haven

The U.S. National Bureau of Economic Research have estimated 15% of the world's countries are tax havens. Sometimes referred to as secrecy jurisdictions, tax havens are countries that are usually both affluent and small, whose laws allow for money to be held there with high levels of secrecy, usually due to laws allowing for strong levels of bank secrecy or secrecy surrounding legal entities. Tax havens have a low, or even zero, tax rate for non-residents, making them even more desirable.

Arm's length trade

Trade where all parties do not have any connections with each other, this means that all parties are acting in their self-interest.

General overview

In 2012, the Global Financial Integrity estimated, the world economy loses $160bn dollars due to tax avoidance. This puts a huge stress on government to compensate for this huge amount of loss. There are three ways of compensating for this reduced income; increasing tax for another institute most likely the common people, this would come at a detrimental time for most people, with the global economy seeing a significant slowdown. The second option is to increase borrowing money and raising the deficit this in turn has a negative impact on future generations who already stand to inherit large quantities of debt. The final option, is to reduce government spending, with this comes the difficult question of where to cut spending, certain areas of the government are clearly exempt from any cuts, healthcare and defense are crucial to the stability of any country. Therefore cuts would go to important but not crucial parts of a country, education and disability benefits.

One of the many issues with tax avoidance is due to it being legal it is difficult to prosecute multinational corporations for avoiding tax, however tax avoidance has a bad image associated with it and media highlighting which multinational corporations avoid tax can severely damage their reputation. multinational corporations do not want their reputation damaged, as this reduces their sales. This can be used as an advantage when attempting to tackle the issue. It is also important to note that some multinational corporations avoid tax, because they have to do keep a competitive advantage.

Panama Papers

On 4th April 2016, the largest data leak occurred, revealing 2.6 terabytes of data from the fourth largest offshore law firm, Mossack Fonseca. The documents were obtained by an anonymous source by hacking into the email servers of Mossack Fonseca, who provided them to the International Consortium of Investigative Journalism (ICIJ). The data from the documents revealed people who profited from offshore tax havens. These people included 12 current nation leaders, most notably the prime minister of iceland, who resigned over the findings. The leak sparked a worldwide debate about offshore tax havens, and ways to crack down on them. This shows the importance that media plays in combatting tax avoidance, as the media storm created by the leak, brought the issue into light, which in turn made the public aware of the issue. The public then put pressure on their governments to crack down on this practise.

Profit shifting

Profit shifting is a strategy where multinational corporations shift their profit to different countries. multinational corporations pay tax in countries based on their income in those countries. Countries have different tax rates on income, so multinational corporations can send their profits to tax havens and not pay any tax on them. In our ever changing global climate, multinational corporations generate profit not from machinery or resources but from ideas and software, thus it is simple for countries to register an idea or software in a country with low tax rates. Thereafter all profit made from that idea or software is only allowed to be taxed in that country. This also works the other way, countries can shift costs for machinery and resources to countries with high tax rates, lowering their overall profits in those countries. As a general rule of thumb, More Economically Developed Countries (MEDCs) tend to have higher tax rates compared to Less Economically Developed Countries (LEDCs).

Transfer pricing

Intra-corporation trade, is trade, made up of goods and services, that multinational corporations do between different sectors and business that they own. An example of this is a car manufacture, making an engine in the United States and then shipping it to Mexico to assemble the entire car. Over half of international transactions are intra-corporation trade, all of this trade is not arm's length trade. Therefore multinational corporations can alter the prices they set for different goods and services, this is referred to as "abusive transfer pricing". Abusive transfer pricing can be used to shift profits to lower tax countries, as well as completely eliminating paying tax, as governments have trouble deciding what the tax should be on intra-corporation trade.

Timeline of Events

Date	Description of Event
3000 BC	Egyptians are first civilization to implement taxation
30th September 1961	OECD established to further economic growth
1964	Japan is first country outside EU and America to join OECD
23 May 1996	OECD Ministerial meeting, commitment to work against tax avoidance
2004	Steering Group is established to tackle tax avoidance
January 2015	UK chancellor implements naming and shaming policy
April, 2016	Panama Papers leak detailing tax avoidance of companies and individuals

Major Parties Involved and Their Views

United Kingdom

Many tax havens are British colonies, which means that the UK has the power to take control of them. It has been urged to harden their stance when telling their colonies to move away from being tax havens. The UK is strong opposer of tax avoidance, and has attempted many schemes to crack down on tax avoidance, which are detailed below.

Panama

Has only recently become a major party when discussing the issue of tax avoidance. This is due to the panama papers leak in 2015 already discussed. Panama is considered a tax haven, and thus it relies a lot on offshore investment to sustain itself. It is currently conducting a review into its financial and legal services.

Monssack Fonseca

Fourth largest offshore law firm, it was the firm hacked for the leak of the panama papers. Even though the papers reveal tax avoidance of many people, the law firm has consistently denied any wrongdoing, simply stating that they may have made some mistakes but were not to blame for other people's abuse of the system.

Organisation for Economic Co-operation and Development (OECD)

The OECD was formed on the 30th September, 1961 by european leaders. Currently there are 34 members of the OECD, but they also have close relationships with other countries. Altogether they represent 80% of the world economy. They work in a forum format where where governments can work share resolutions and work together to tackle common problems regarding the economy. This includes tax avoidance, in 2004 they set up a group named the Steering Group that focused on identifying tax avoidance schemes and finding ways of shutting them. It currently is made up 46 OECD and G20 countries.

UN Involvement, Relevant Resolution Treaties and Events

- Organisation for Economic Co-operation and Development (OECD) has helped find resolutions to issue of tax avoidance. Founded in 1960, consisting of 35 mainly developed states, with a common goal of economic development
- G20 endorses OECD measures to crack down on tax avoidance (16/11/2015)
- Committee of Experts on International Cooperation in Tax Matters, created by the Economic and Social Council (ECOSOC) to provide a framework for dialogue between countries on issues of tax

Previous attempts to resolve the situation

In 2015 The UK chancellor George Osborne implemented a system where Her Majesty's Revenue and Customs named and shamed all individuals that avoid tax. The idea behind this, was to make tax avoidance a moral issue, as tightening tax avoidance laws had so far proved fruitless. The government relied on the media to highlight multinational corporations that were paying less than their fair share of tax, and thus the public getting angry. Whilst bringing attention to tax avoidance is a very important step in cracking down on tax avoidance, it is not sufficient as it does not force multinational corporations to pay tax. The initial media attention multinational corporations might reduce a corporation's image for a short while, however the media will inevitably move on to other stories, rendering the idea that the public puts pressure on multinational corporations useless.

A second idea that the UK has implement is fining multinational corporations to repay tax that they have avoided, the amount of money that the multinational corporations are fined by the government has been negotiated. These negotiations are under intense public scrutiny, which is why the multinational corporations cooperate. Starbucks payed £8.1 million in 2015, which is the same amount of tax that it paid in the previous 14 years. Likewise google was fined £138 million pounds in 2015. Whilst these payments have been lauded as a step forward for tax avoidance, there are many critics who argue that the deals do not represent value for other tax avoiders. Richard Murphy, director of campaign group Tax Research said “We are claiming back a tiny extra proportion [of what Google has underpaid], way short of any reasonable amount of tax,” In 2013 the Organisation for Economic Co-operation and Development (OECD) and the G20, generated a report, in which they highlighted the issues of tax avoidance and ways of addressing them. This report has been criticised heavily, as many feel it does not go far enough to tackle the issue of tax avoidance. It is also not mandatory for countries to implement this resolution.

Possible solutions

An idea suggested by President Barack Obama of the Unites States of America was to implement a law stating that a country has to pay tax on all of its profits it makes in a country, even if the software, brand or idea is registered somewhere else. This tax would not be as high as the standard corporate tax, however still significantly more than what some multinational corporations currently pay. This idea sits well with most people, especially tax havens as they can still profit from multinational corporations wanting to reduce their tax bill. There have been objections to this idea from small business owners who have to pay the full corporate tax, because they do not have the resources to expand to a second country. They do not think it is fair, that a corporation whose profits dwarf theirs, have to pay less tax than they do.

As mentioned previously in this research report the media plays a powerful role when attempting to crack down on tax avoidance. Therefore continuing on from the UK idea of naming and shaming multinational corporations, this can be done on a global scale, to force corporations to act within the law when paying tax.

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