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Finding the money to fix the world requires a rethink on tax, says Jayati Ghosh

The co-chair of an independent tax commission on why the focus should be on squeezing more from big business and billionaires

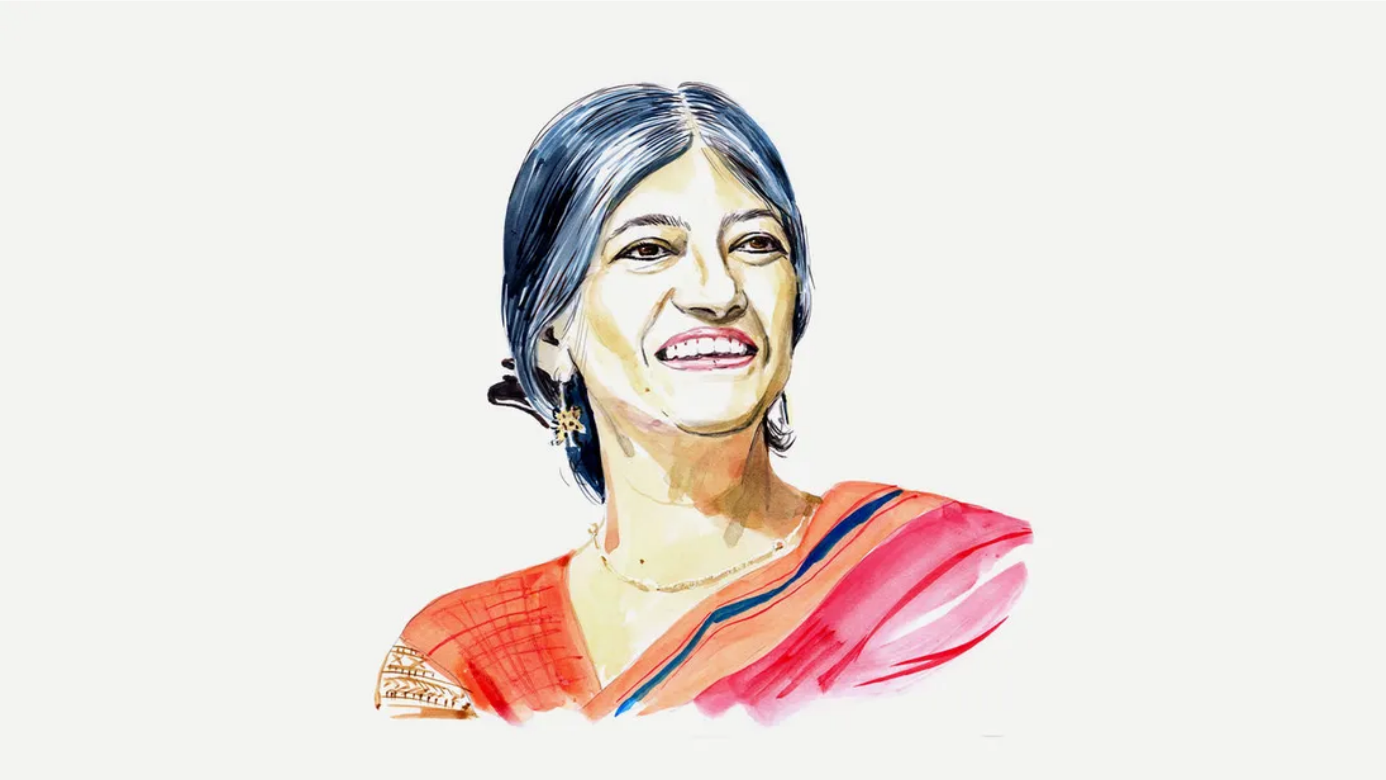

IMAGE: DAN WILLIAMS

Jun 13th 2023

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THE WORLD is facing numerous extreme, interlinked challenges, including a climate emergency and growing economic inequalities between and within countries. Tackling these problems requires funds to flow in the right direction, towards reducing carbon emissions, supporting education, health and other essential services and overhauling global infrastructure. All of this will, in turn, require massive increases in public spending.

But the current international economic and financial architecture—from the structure and goals of multilateral lenders to the regulation of financial flows—is inadequate and even obstructive. World leaders will meet in Paris next week

to discuss ways to fix this architecture. But already the level of ambition seems to be low; all that may result is yet another ineffective talking-shop. Yet two obvious strategies to increase public resources across the world are available: ending tax avoidance by multinational companies and taxing extreme wealth.

Currently multinationals avoid tax payments of at least $240bn per year, and probably more, because the current international taxation rules were developed a century ago, when there were fewer border-straddling companies and no digital ones. The rules allow multinationals to treat each national subsidiary as a separate "arm's-length" entity for tax purposes, and to move profits to low- or no-tax jurisdictions (a process dubbed BEPS, for Base Erosion and Profit Shifting). This can be prevented by recognising that multinationals are global unitary businesses, and by abandoning the arm's-length principle. Multinationals' profits could then be divided among countries according to a formula based on the location of revenues, employees and so on. A global minimum tax would further reduce the incentive to move profits to tax havens.

Since 2013 the OECD, a club of mostly rich countries, has been mandated by the G20 to work towards changing the rules to permit that. Years of fraught negotiations yielded an agreement between 136 countries in 2021. Billed as a sweeping overhaul, it did accept the principles of unitary taxation of multinationals and a global minimum tax rate. But it watered down the proposals so much that it will probably deliver very little additional revenue to developing countries, while requiring them to forgo independent sources of revenue, such as "digital-services" taxes on tech giants' local sales.

Done right, a global minimum tax would yield large revenues for governments. A rate of 25%, the median of corporate-tax rates around the world, has been proposed by the Independent Commission for the Reform of International Corporate Taxation, a group of experts which I co-chair. The Biden administration suggested 21%. But the final compromise of only 15% forged under the OECD-led process mainly pleases the tax havens. The potential revenue difference is significant: instead of more than $500bn of extra tax receipts with a 25% minimum tax rate, 15% provides only $220bn. And very little of that would accrue to the less-developed countries most in need of a boost to public coffers, even though some of them host large amounts of multinational business activity.

The commitment to divide taxing rights between countries has been eroded even more. It will apply only to large multinationals (with annual turnover of around $20bn) whose profits exceed 10% of revenues. And only a quarter of the "residual" profits above the 10% floor would be available for reallocation across countries for tax purposes. This would deliver as little as $12bn-25bn in additional revenues, with a small fraction of that going to lower-income countries. In any case, this measure may never see the light of day, since it requires a multilateral convention. Politics in many countries make this difficult. Republicans in America's Congress, for example, are clearly unwilling to share with the rest of the world rights to tax the profits of American multinationals.

One reason the OECD outcome has been underwhelming is that the process was not really inclusive: it ignored concrete proposals put forward during the negotiations by developing and emerging countries. Many countries are now tired of allowing America and Europe to decide for the rest of the world. In late 2022 lower-income countries won a diplomatic tussle with America and other OECD members, to give the United Nations a mandate to kickstart a new round of intergovernmental talks on taxation. These are scheduled to begin later this year.

Several countries—including Brazil, India, Indonesia and Nigeria—have already imposed or plan to impose digital-services taxes, despite fierce opposition from America. These are not a panacea for tax avoidance, but they are simpler to administer than the proposed new rules to divide taxing rights and can provide much-needed revenue until a better solution is negotiated.

Similarly, wealth taxes can be levied nationally. Even modest taxes on extreme wealth, which has grown dramatically in recent years, can reduce financial inequality and provide more revenue. Most countries have taxes on property but do not levy them on other wealth. Financial assets account for a growing share of the wealth of the richest individuals and the revenue potential is significant.

Raising more revenue through wealth taxes requires identifying the true beneficial owners of all assets, financial and physical. This information can be collected in national registries and shared across jurisdictions to prevent people from dodging taxes by shifting their wealth offshore. Moving towards a global asset registry should be the ultimate aim, but like-minded countries can co-operate even without a global agreement. This is already happening. In July Colombia, Brazil and Chile will convene a meeting of Latin American and Caribbean countries to look for a common approach to taxing multinationals and fighting tax havens—the first regional ministerial summit of its kind. Other regions could follow their example.

An international tax architecture that works for the benefit of all countries is in the best interests of people everywhere. Let's see whether leaders at the Paris summit take note. ■

Jayati Ghosh is co-chair of the Independent Commission for the Reform of International Corporate Taxation.

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