

Is BEPS Good Policy?

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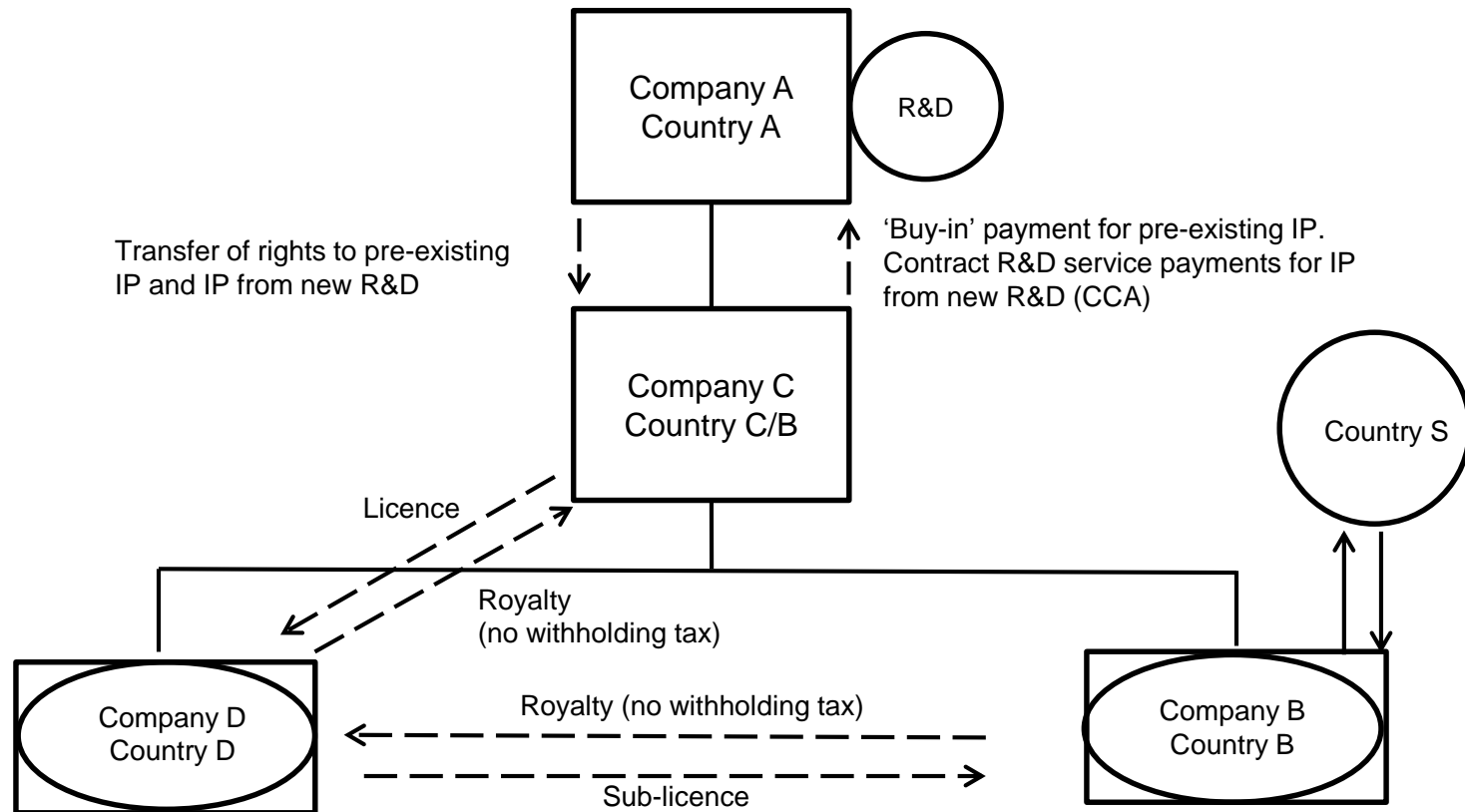
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- › Brief background to the Base Erosion and Profit Shifting (BEPS) project
- › Action 11 on data (and policy)
 - Seems to be going nowhere
- › The big policy picture: Can the corporate tax survive?
 - Questioning of arguments in the economic literature that it is doomed
- › The smaller (but still significant) policy picture ... does not exist in BEPS

- › The Google etc publicity 2010-2012
 - Commencement of work in OECD/G20 countries second half 2012
- › OECD Report February 2013
 - Some discussion of policy of corporate income tax, largely of the negative modern public finance kind (see later)
- › Action Plan July 2013
 - All action, little policy
 - Organised around three policies/themes
 - Coherence of the corporate income tax (Actions 2-5)
 - Taxing income where value adding activities occur (Actions 6-10)
 - Transparency (Actions 11-14)
 - With two cross-cutting issues
 - Digital economy (Action 1), multilateral treaty (Action 15)

Google (OECD+) A=US, B=IR, C=Bermuda, D=NL, S=sale/customer



BEPS Action Plan: Bold = DD/Report 2014 out Bold Italics = DD 2015 out, Plain = nothing out

Issue	Action	Output	Deadline
1 Digital economy	Address challenges	Report	9/14
2 Arbitrage	Neutralise	Treaty/domestic law	9/14
3 CFCs	Strengthen regimes	Domestic law	9/15
4 Interest deductions	Limit base erosion	Domestic law/TPG	9/15 12/15
5 Harmful tax practices	Counter more effectively	Identify OECD/non-OECD/revise criteria	9/14 9/15 12/15
6 Treaty abuse	Prevent	Treaty/domestic law	9/14 9/15
7 PE	Prevent avoidance	Treaty	9/15
8-10 TP Intangibles, risk, capital, abnormal contracts	Place of value	Treaty/Guidelines	9/14 9/15
11-13 Transparency TP Documentation	Disclosure, data & policy analysis	Recommendations/ Guidelines	9/14 9/15
14 Dispute resolution	Make effective	Treaty	9/15
15 <i>Multilateral instrument</i>	Identify issues, draft	Multilateral tax treaty	9/14 9/15

- › Brisbane G20 meeting endorsed deliverables published and endorsed in September by Finance Ministers
 - Digital economy
 - Hybrids
 - Harmful tax practices
 - Treaty abuse
 - Transfer pricing intangibles and documentation
 - Multilateral treaty
- › Virtually no discussion of policy except:

“No or low taxation is not *per se* a cause of concern but it becomes so when it is associated with practices that artificially segregate taxable income from the activities that generate it” – BEPS Action Plan

- › Action 11 is only real effort to address policy (though it reads as if it is all about data)

“Develop recommendations regarding indicators of the scale **and economic impact of BEPS** and ensure that tools are available to monitor and evaluate the effectiveness and **economic impact of the actions** taken to address BEPS on an ongoing basis. This will involve developing an economic analysis of the scale and impact of BEPS (**including spillover effects across countries**) and actions to address it. The work will also involve assessing a range of existing data sources, identifying new types of data that should be collected, and developing methodologies based on both aggregate (e.g. FDI and balance of payments data) and micro-level data (e.g. from financial statements and tax returns), taking into consideration the need to respect taxpayer confidentiality and the administrative costs for tax administrations and businesses.”

- Request for input August 2014, comments published October 2014
- DD January 2015 now delayed to end March 2015: what is happening?

Can the corporate tax survive?

- › Economic literature on mobile income
 - Views in OECD 2012 advice to Canada & Australia (eg increase GST, cut corporate tax rates) continues in 2014 Economic Surveys
 - Recent public reviews accepted literature (Australia 2009, Canada 2008, UK 2011, US 2005)
 - › BEPS by contrast proposes to reinvigorate the international corporate income tax
 - The arguments are still to be made – an attempt follows
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- › In a variety of ways the economic models and theories focus on capital income and ignore labour income
 - Widely agreed that taxation of labour income is distortive
 - Untaxed choices: Household production and leisure
 - Optimal tax theory suggests that if distortion in one part of system, it is likely not the optimal policy to remove distortions in another part of the system
 - Work of Aps and Rees
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- › Models often assume:
 - Perfect capital markets and mobility
 - Marginal investor non-resident tax exempt in home country
 - › Conclusion that source tax impossible
 - Investor will invest elsewhere and/or
 - Tax will be shifted to immobile factors
 - Policy recommendation is to reduce or do away with corporate income tax and taxation of income from capital generally
 - Taxes should be on immobile factors which are taken to be land, average employees, and consumption
 - › Capital market failures everywhere: global financial crisis or GFC
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- › Basic risk free rate of return can/should not be taxed
 - Unlimited borrowing/consumption tax style arguments
 - › Tax return to risk symmetrically > with no net revenue
 - Focus on tax system whereas optimal tax shows need to view tax and transfer systems as a whole; corporates receive large transfers
 - › Economic rents
 - Immobile can be taxed, mobile cannot be taxed (capital mobility again)
 - Impossible to observe line between risk and rents
 - Corporate returns are mixture of both varying over time (digital economy)
 - Rents are capitalised in prices and significant transitional issues for rent taxes
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Model of firm ignores real taxpayers and incidence

- › Company (modelled as black box with attributes of welfare maximising individual)
 - › Avoids questions of incidence of corporate tax
 - Is efficiency not affected by incidence
 - See above – incidence a consequence of shifting, not of efficiency
 - › Avoids issues of internal dynamics of firm
 - Rent-seeking executives
 - Moral hazard
 - Compare corporate literature
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- › Investors cannot achieve better than general market or risk-free rate of return
 - Efficient market theory for public markets in securities
 - › Hence tax on flat rate of imputed return or something similar
 - What happens to the rents?
 - Do shareholders matter or not?
 - Hard to connect with other theories/models
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The smaller (but still significant) policy picture

- › Digital economy and tax claims of country of the customer
 - Postponed to after BEPS by Digital Economy Report
- › Coherence of corporate income tax
 - Assumption that corporate income should be taxed somewhere (and not end up in havens where no activity occurs)
 - But where: Source (Actions 2, 4, 5) v Residence (Action 3)
- › What is the purpose of the PE threshold and does the current threshold fit the policy in the modern world?
- › What is the policy of the arm's length principle given the theory of the firm?
 - See also above regarding taxing the unobservable, risk and rents
- › No attempt to articulate the policy and seek to implement it (taking into account path dependence, tax sovereignty, political dynamics)