

World taxation Is a bad idea

The G7 Finance Ministers and Central Bankers claimed a breakthrough in moving to a world based system of company taxation. President Biden wanted to set a minimum tax rate of 21% worldwide, and find a way of preventing some global companies booking too much income to low tax countries. He settled for a 15% proposed minimum rate, and a complex outline over the allocation of profit. The Communique offers "market countries awarded taxing rights on at least 20% of profit exceeding a 10% margin for the largest and most profitable enterprises".

These so called twin pillars of policy were important to get all the G7 on board. The USA seeks the abolition of the recently imposed digital turnover taxes in the UK, France and elsewhere as a trade off for the promise of some transfer of profit to tax in countries where the digital giants trade substantially. Either way the USA will be one of the major beneficiaries. Many of the large global digital giants are US corporations who have in the past kept substantial business offshore in lower taxed jurisdictions. President Trump offered favourable terms to get some of the cash repatriated. The final agreement was a much watered down version of the original US proposal.

It needed to be watered down as countries understandably value independence in seeking to tax companies. There is no world government with democratic accountability or authority that can set a world tax rate for business and distribute the revenues between countries to a formula. The EU has been trying to get there by small steps, but has found it is much easier to invent a new specialist environmental EU tax that applies to all than to reform a tax like corporation tax so that it becomes a uniform levy. The EU has decided to allow Ireland to be a tax haven with a 12.5% corporation tax rate, even though many EU member states are unhappy about that status.

I think tax competition has a lot to recommend it so there is some countervailing force to the remorseless pressure to tax more based on the theory that higher rates produces more revenue. In the case of business taxes a lower rate often raises the amount of money collected, acting as an incentive to invest, raising the prospective returns and leaving more cash in the business to pay for it. Lower rates can produce more income for shareholders and governments.

This proposal looks difficult to enforce. The 15% minimum is not too damaging, and is still below the UK rate so it does not currently constrain us. There will need to be some good drafting to decide how turnover and profit allocation will work within a multinational profitable company. So far the general language allows various interpretations.

Assuming the G7 leaders endorse this recommendation, it then needs to be worked up further and sold to the G20. China and Russia may have other ideas. If they can be accommodated then it needs the support of the whole OECD. The proposal is vulnerable to some countries seeing an opportunity to set a low

corporation tax rate or to accept the minimum rate but offer lots of offsets and concessions to try to remain or gain status as a good tax location for substantial booking of business.