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Corporate Power – Corporate Capture

How transnational corporations avoid paying taxes



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**TAX JUSTICE SEMINAR:
TRANSNATIONAL CORPORATIONS
MUST PAY THEIR FAIR SHARE**

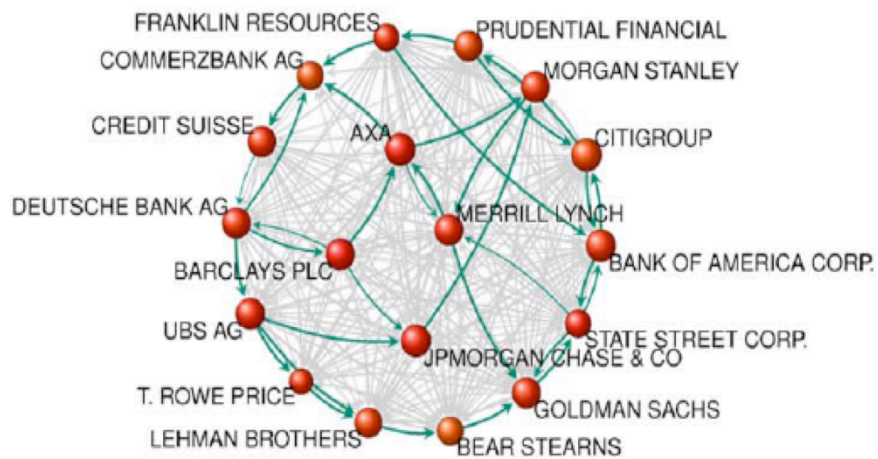
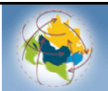
Buenos Aires, Argentina. 9-10 November 2015

Recasting the Die, what does that mean? TNCs have molded or constructed their global institutional and legal environment, the "die", or casting, in which they operate. We need to break that casting, that die, and recast it.



Global Corporate Power and Control

- TNC-led Global Value Chains/Networks account for **60%** of global trade (**80%** if financial transactions are included)
- 737 company groups (top holders) control 80% of all TNCs.
- smaller nucleus of 147 companies controls about 40% of TNCs.
- Three-quarters of these companies are in the financial sector.
- RESULT: a large portion of control flows to a small tightly-knit core of financial institutions



Vitali, S., Glattfelder, J. & Battiston, S. (2011) 'The Network of Global Corporate Control', *PLoS ONE*, 6 (10), e25995.



Country Rankings: Competitiveness, Workers' Rights, Democracy

Country	FDI Ranking 2014	Global Competitiveness Index 2014-2015 (144 Countries)
China	1	28
USA	3	3
United Kingdom	4	9
Singapore	5	2
Brazil	6	57
India	9	71
Chile	11	33
Mexico	13	61
Indonesia	14	34
Russia	16	53

Corporations may be "global players", but they still have to produce and sell or provide services to real people in real places. So let's take a look at some of the characteristics of countries with the largest amount of foreign investments. In this chart we see 10 of the top 20 countries as ranked by investments. In the next column is the global competitiveness index, devised by business interests using such indicators as flexibility in wage determination, hiring and firing practices cooperation in labor relations and redundancy costs. RESULTS

But how do these countries rank in terms of their standards of democracy and in terms of trade union rights?



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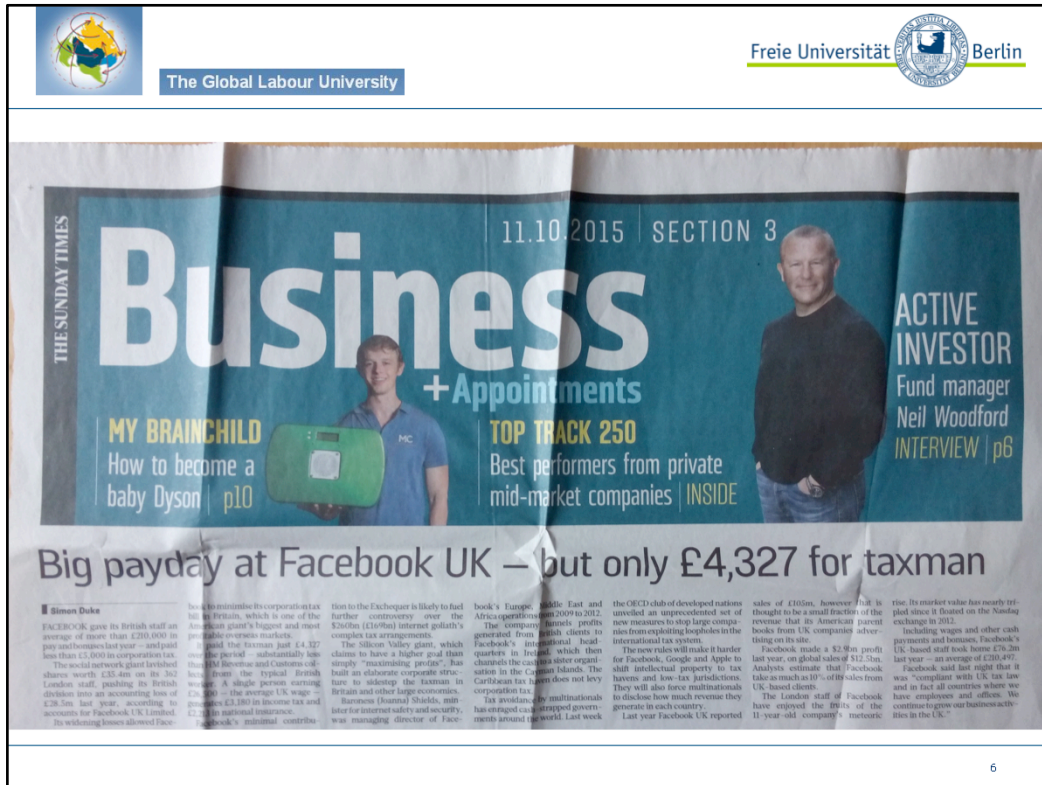
- **Tax Avoidance:**

Undermining the legitimacy of public service



TAX AVOIDANCE

Most of America's largest corporations maintain subsidiaries in offshore tax havens. At least 358 companies, nearly 72 percent of the Fortune 500, operate subsidiaries in tax haven jurisdictions as of the end of 2014.



Facebook 2015 (The Sunday Times, Oct. 11, 2015, Section 3), funnels income from UK customers to its international hq. in Ireland, which transfers the money to a sister unit on the Cayman Islands where there is no corporation tax!

Facebook generates ca. 10% of its yearly revenues of 12.5 billion pounds in the UK. That's about 1.2 billion pounds.

Facebook gave its UK staff of 362 bonuses totaling 35.4 million Pounds leading to an accounting loss of 28 million pounds.

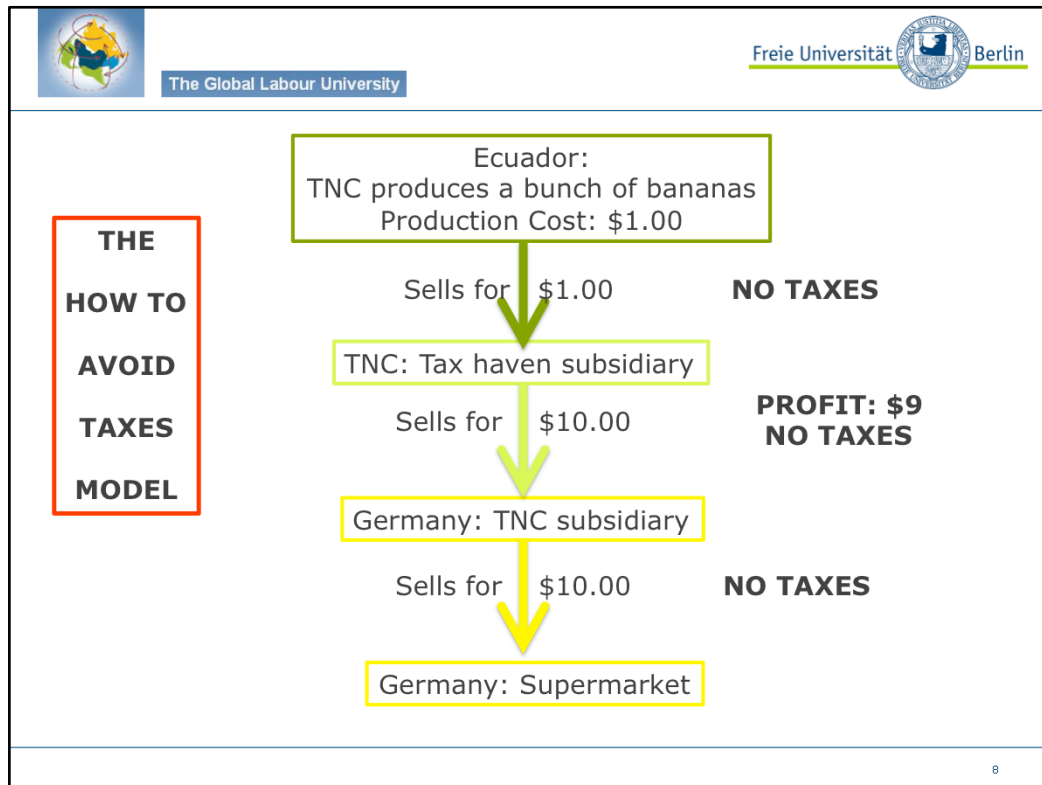
Facebook paid 4,327 pounds in taxes 2014
 Average British wage earner (26,000 pounds) paid 3,180 pounds income tax and 2,213 in national insurance.



The FTSE 100's top 10 tax havens

8,492 FTSE 100 subsidiaries in tax havens





Moving on to the question of taxation, I want to present to you a very simplified model of how corporations avoid paying taxes.

Let's say it costs a TNC \$1 to produce a bunch of bananas in Ecuador. It can sell it for \$10 in Germany. Here's how the TNC cuts its tax bill. The Ecuador affiliate sells the bunch to an affiliate of the TNC in a tax haven for \$1. The tax haven affiliate sells it to the TNC's German affiliate for \$10. The German affiliate sells it to a German supermarket shop for \$10, the true market price in Germany.

So what happened here?

The Ecuador subsidiary had costs of \$1 and sold at \$1, so its profits – and therefore its tax bill – are zero. The German subsidiary bought at \$10 and sold at \$10, again for zero profits and zero taxes. But the tax haven subsidiary bought it \$1 and sold at \$10, for \$9 profit. But the tax haven doesn't tax profits, so the tax bill is zero there too! There are many different ways to achieve the same effect.

ANOTHER METHOD: Contracting services from another unit of a TNC in another country. Amazon in Europe separates the functions of sales and website operation (attributed to Amazon SARL Luxembourg) from customer support, warehousing, and order fulfillment, which are done in each country close to its customers.

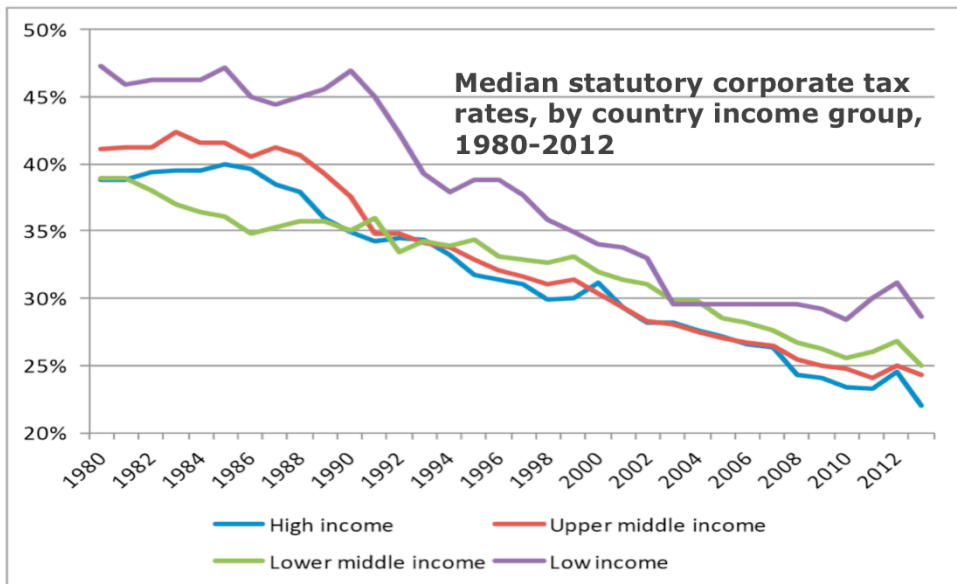


Supply Chain Planning – First Principles

- ▶ Allocation of profits:
 - Operating entities entitled for normal profits
 - Hub entity entitled for residual (entrepreneurial) profits
- ▶ Hub entity
 - Located in Low Tax Jurisdiction (“LTJ”)
 - Centralization of management, control & business risks
 - Entitled for residual (entrepreneurial) profits
- ▶ Operating entities
 - Location based on business & tax considerations
 - Perform routine functions and bear subordinate risks
 - Receive a stable and relatively low profit level
 - Profit level can be controlled



Who wants to win the race-to-the-bottom?



Source: IMF 2015



IMF ESTIMATES OF REVENUE LOSSES ARISING FROM PROFITS SHIFTING BY TNCs

	USD Billion	% of GDP
OECD countries	509.2	0.57
Developing countries	212.7	1.70

Source: IMF Fiscal Affairs Dept. 2015



The American Prospect, Fall 2015, p. 103. Action Aid protesters lampoon the role of Barclays Bank in helping clients set up offshore tax havens.



THE HOW TO AVOID TAXES MODEL:

Separate Enterprise-Arm's Length Principle (SE-ALP)

- Investment competition leads to taxation race to the bottom
- Erosion of country tax bases
- Influence on allocation of public funds
- Enhances pressures to privatize

One of the major reasons corporations can do this is because for tax purposes they are treated as separate, independent entities in each country and not as parts of global operation.

QUOTE FROM PAPER: The announcement by the EU Commission (summer, 2014) that it would launch an investigation of prominent corporate tax evaders, among them Apple, Starbucks, and Fiat, in regard to state subsidy regulations may be little more than a public relations move.

October 2015: Belgium and NL required to force Fiat and Starbucks to pay tax debts



Combating *corporate capture* on Taxation: What's on the table

OECD: Base Erosion and Profit Shifting BEPS

- Measures to ensure that profits are taxed where economic activity occurs and value is generated.
- require country by country reporting of revenues, profits, taxes paid, employees and assets. But not public reporting
- Ineffective on use of transfer pricing to avoid taxes.
No reform of SE – ALP
- Privatization of dispute resolution (arbitration provisions)
- Resource strain on poorer countries. No curtailment of tax incentive "race to the bottom"
- OECD: One step, but a limited basis, subject to heavy lobby. Countries protect "their" TNCs.

In September 2013, the BEPS Action Plan was approved as a G20 project and organized through the OECD for delivery by December 2015. The BEPS project is aimed at ensuring that multinational corporations are taxed 'where economic activities take place and where value is created'.

Stiglitz Group **ICRICT**

Independent Commission for the Reform of International Corporate Taxation

- Agreement on minimum tax on corporations among developed nations
- Taxation based on national income revenue (Apple: 35% of sales in US)
- apportion intellectual property income to country of origin, not tax haven



Alternatives and Recommendations

Taxation Policy

- Elimination of SE-ALP, introduction of unitary taxation of TNCs
- Global representation in reform process
- Greater cross-country transparency and publicity.
- Ending of "revolving doors"
- State laws to control capital flight
- Reframing and furthering discourses on public funds and services
- Mobilizing national and global union support – building alliances for just taxation