

MUTLTI-NATIONAL CORPORATIONS PROFIT SHIFTING Vs. CORPORATE INVESTMENT

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Thank you for the opportunity to participate in the conversation.

Whilst wishing to participate on a number of tax topics, this submission is limited to issues as they relate to BEPS (Base Erosion Profit Shifting), and the impact that Multi-National Corporations (MNCs) who exploit profit-shifting have on the host-countries where their profits are derived. And how we might change corporate behavior in relation to profit shifting, and guide them to investing in, rather than divesting from, the host country.

Use Of Terms

With a view to simplify my submission for the general benefit of those observers who care more for an understanding of the opinions offered in the “conversation”, than the terminology which can be confusing, and figures that can be daunting, I have attempted to expressed my opinions, in what I hope are “everyday” laymen terms.

In doing so, I respect that exactness in terminology and figures are essential in lawmaking, and in assuring that we are all talking about the same thing, hence no disrespect is intended.

There are many factors, components, drivers, impacts and elements that effect taxation. However my submission is specific to the impacts of “Base Erosion Profit Shifting (BEPS) and those Multinational Corporations (MNCs) who shift their profits offshore. Whilst there may be related factors, I have avoided their mention unless crucial to the point I am making. And terms that may have broader meaning should be read in the context as it relates to BEPS and Profit-Shifting by MNCs

MNCs	Multi-National Corporations also referred to as Multi-National Enterprises (MNE’s) or Trans-National Corporations (TNCs). MNCs, TNEs and MNEs may differ in terms of their organizational structures, however the precise distinctions are not required for the purpose of this submission, and are collectively referred to as MNCs. A MNC directly or indirectly controls or operates one or more partly or fully owned business components or subsidiaries outside of its home country.
Profit Shifting	As it relates in the context of MNCs who shift profits produced in one country, to another country for the benefit of tax mineralization and avoidance.
Home Country	The country where a MNC is based.
Host Country	A country where a MNC produces profits, but not necessarily the MNCs “Home Country”
Tax Base	The Tax Base is the sum total of Australia’s taxable activities, together with the combined value of its assets and properties, that are subject to tax. However , for the purpose of maintaining a simple approach in this submission, “Tax Base” will be used in the context of corporate tax and personal income tax, and unless stated otherwise, will refer to and mean; the portion of the over-all tax base that relates specifically to corporate tax and personal Income tax.
Units	To articulate concepts in this submission; I have attempted to avoid the use of numbers, and resolved to use the abstract term “Units” wherever possible. I note that yes, it is unusual to enter a tax discussion without wanting to use numbers. However in my opinion, the amounts are irrelevant if the points are made clear.
Per Centum	Each 1 percent of 100 percent.

Organization And Format of This Submission

I have made no assumptions as to the level of introduction or detail that participants and observers to “The Conversation” may expect. And accordingly, I have formatted my response in an informal manner, and with a level of detail that is already familiar to some observers, but may not be familiar to others.

This submission generalizes, only to sufficiently provide evidence that BEPS is of significant concern to the future prosperity of all Australia’s and MNCs alike.

Without the benefit of vital statistical data on the micro socioeconomics of the matter, my statements are therefore an opinion, and should be treated as such.

However, I do draw on my understanding from what both sides of the Australian government have commented on, together with departmental media statements, and also together with further reading on intergovernmental organizations (IGO’s), and the common challenges and trends they report on, and are actively engaged in shaping global policy on.

My background as a SBA (Senior Business Analyst) specializing in Process Engineering, equips me with a commonsense approach to the general issues related to profit-shifting, and the downwards trending spiral that the practice establishes, and the very real socioeconomic harm that such a trending spiral presents to the host countries, and therefore, also to future well being of those MNCs who engage in the practice, and whose prosperity relies on the economic health of the regions where they operate and produce their profits.

The Desired Outcome Of This Submission

The desired outcome of this submission, are to:

1. Raise the profile of the broader socio-economic impacts of profit shifting in the discussion.
2. Establish the destructive nature and effects that profit-shifting has on:
 - i) The immediate and future interests of Australia as a host-country, and;
 - ii) The medium and long-term self-interests of the MNCs who practice profit shifting.
3. Encourage the Australian government to examine the benefit of providing additional resource and effort to the production of materials for the purpose of:
 - i) Making available, specifically related statistical data and measure of tax burden calculations that clearly details:
 - a) The current extent to which profit shifting has shifted the tax burden to the shoulders of Australia’s domestic businesses, and average wage earners.
 - b) The direct, indirect, and trickle-down socioeconomic impacts that profit-shifting is already having on Australian individuals, businesses and communities,
 - c) The long-term direct, indirect, and trickle-down socioeconomic impacts on Australian individuals, businesses and communities, that profit shifting will have on our future.
 - ii) Encouraging MNC’s who are exploiting the practice of profit-shifting, on the basis of the evidence and commonsense, to:
 - a) Come to the understanding that the practice is destructive, and;
 - b) Come to the realization that their long term interests are best served by withdrawing from the practice, and,
 - c) Shift their thinking. And rather than exploit and divest their host-countries, invest in the prosperity of their host-countries. And by doing so, invest in their own future prosperity, that better serves their long-term self-interests.

Doubtless, for some observers, the suggestion that we might shift the thinking of MNC’s engaged in profit-shifting, would have instantly initiated echo’s of derivative laughter, and thought balloons with satirical captions such as “Oh really?” ”Right then, well good luck”. And that’s understandable, as I’m sure it echoes the same derivative laughter, and satirical thought balloons that would have once hung over the head of an earlier merchant, if his ships captain said “the world is round, and it offers a better way of getting there”.

There is no suggestion, and nor do I suggest, that all or most MNCs exploit profit shifting. However and regardless, at any measured percentage of those who-do and do-not, the current level of profit shifting is already having tremendous economic and socioeconomic impacts, both directly, indirectly and through trickle-down or roll-down effects on Australia as a host country.

What makes MNCs profit-shifting incredibly unfair, is that *at the moment*, the adverse impacts are exclusively only being felt by host-countries, their communities, businesses and their citizens who support the MNCs through the consumption of the products and services that the MNCs profits are derived from.

The quality of life for Australians, as with citizens of other countries, is not only dependent on what citizens, communities and businesses are able to produce for themselves, but also, heavily dependent on the services and infrastructure produced and managed by its government, and its structured government bodies and agencies.

The Australian governments ability to preserve and improve the services and infrastructures that it produces and manages, like other governments, is dependent on its revenue. And the Australian governments revenue is heavily dependent on corporate and personal taxes, and its States are heavily dependent on Goods & Services Taxes (GST).

The corporate and personal tax burden is proportionately spread between business and personal taxes at levels that the Australian Government believes businesses and citizens can withstand, but currently fall short of the government's true budget requirements. The levels of tax are high in proportion to the balance of incomes, and costs of living, and further increases to these taxes will inevitably stress both businesses and citizens alike.

Whilst there are a number of factors that contribute to individual levels of tax, the breadth of the "Tax Base" stands out above the rest, and can be positively identified as having the most significant and direct cause & effect on individual tax burdens imposed on businesses and working Australians.

Many Australians argue that extra breadth to the tax base places extra burden on themselves, but not withstanding the effects of other measures such as cost savings, broadening the tax base is a key strategy that provides governments the opportunity to then redistribute the burden, and reduce the burden to those who can least afford to contribute.

As with governments in other counties, the Australian government determines how the burden of tax is allocated across the sectors. In other words it legislates who must remit taxes, calculated on what is a fair distribution of the tax burden that balances the governments needs to fulfill its functions and have sufficient surplus to protect our gains in prosperity against unexpected downturns or future economic shocks. The total of the legislated taxes form the tax base.

It is likely that Australia's tax base (as legislated) is of sufficient breadth when calculating the makeup of the taxes that form the total base, whilst not limited to, but inclusive of multinational and domestic corporate profits derived from the sale of goods and services.

However, legislation is one thing, but in practice, the final burden is determined by how individuals and corporations alter their actions in response to the legislated taxes.

In some cases the incidence of tax is shifted from the intended source to another source as might occur when a business passes a tax onto the consumer by way of additional costs, thus in reality it shifts the tax burden onto the shoulders of the consumer, when the legislation was aimed at business. In this case the consumer has indirectly carried the burden and the tax is paid, producing no significant differences in the total tax collection even though market forces affected a shift in distribution of the tax burden.

If we were to look towards the trickle-down effects, we would see:

1. That the consumer is burdened with a tax intended for business.
2. That the consumer is also doubly burdened by additional GST taxes that applies proportionally to the increased cost.
3. That the consumer is then left with less disposable income.
4. That less disposable income leads to etc

But the news is not all bad, as the taxes are paid in any event, and the governments needs to fulfill its functions are met, and public infrastructure and services are provided, therefore economic benefits are redistributed across the broader community, albeit in this example, at the additional expense to the consumer.

In the case of profit shifting by MNCs, the burden of tax is shifted onto the shoulders of all Australians, domestic business, citizens and communities alike, however in a different manner, and with far more reaching trickle-down impact.

The profits that are shifted should be calculated to form part of the tax base, but in reality must be excluded, as the government cannot rely on taxes being derived on these profits, as no tax incident occurs.

As the profits are shifted outside of Australia's jurisdictional control, the potential tax base is significantly narrowed.

For example, using arbitrary amounts, let say:

1. The Government's needs are sufficiently measured at a total of 12-units, and legislated at a fair distribution rate of:

- a) 3-units personal income tax
- b) 9-units corporate tax.

And let's say that a number of MNCs create elaborate structures that allowed them to shift 4-units of corporate taxes offshore.

Then the government's budget would fall short by 33 per cent (4-units), and to meet its obligations, will need to:

- a) Borrow the entire shortfall, or
- b) Reduce or discontinue parts of its planned spending on infrastructure and services, or
- c) Borrow part of the shortfall, and reduce or discontinue a lesser part of its planned spending on infrastructure and services.

In either event the actions of the MNCs profit shifting of 4-units has directly:

- d) Deprived Australians of promised infrastructure and services, or
- e) Put Australians in debt, or
- f) Deprived Australians of promised infrastructure and services, and put Australians in debt

2. Following on to the next budget, let's say the Government:

- a) Felt that the planned infrastructure and services were vital to the immediate well being of Australians, and

- b) Opted to borrow the entire 4-unit shortfall in order to pay for its planned infrastructure and services.

The government again measures its needs at 12-Units, plus an additional 4.2-units comprising of:

- i) 4-units of debt
- ii) 0.2-units of interest servicing the debt

Hence, to achieve its revenue requirements, the government now looks to raise $12 + 4.2 = 16.2$ -units.

So far its simple mathematics, notwithstanding rises and falls in markets, and potential increasing trends towards profit shifting.

The government must now decide how it will allocate and distribute the burden, and must take into account:

- a) That based on the previous budget period; 4-units of the overall expected corporate tax profits will be shifted offshore, and therefore cannot be calculated into the tax base.
- b) That the tax base has now been eroded by 33 percent of the previous measurements, and the 16.2-units must now be re-distributed across the remaining 67 percent of corporate and personal income taxpayers that now form the total of the eroded tax base.
- c) In the previous budget the per centum spread of the 12-units was calculated by the government to be 0.12-units ($12 / 100 = 0.12$), and had the MNCs profit shifting of 4-Units been calculated at the time of the previous budget, the reduced tax base at 67 percent would have then be calculated at 0.18-Units ($12 / 67 = 0.18$).

Given that the government of the time, in considering affordability and other factors, calculated that a per centum tax burden of 0.12, was fair, the otherwise spread of 0.18 per centum would have represented a further 0.06 per centum ($0.18 - 0.12 = 0.06$), or 50 percent per centum rise falling upon the shoulders of the remaining 67 percent of Australian corporate and personal income taxpayers.

- d) What impacts that any increase to the current tax burden of corporate tax at 9-units, and personal income tax at 3-units, might have.

(As governments can, the government may spread the additional 4.2-units across several budgets periods to reduce the overall impact, so the government calculates and considers its option of spreading the debt across (say) 6 budget periods, leaving the increase at a nominal 1-unit)

On the basis that the government may still take the view that the current burden is only marginally fair based on affordability and other factors, let's say, that the government in its determination to minimize any immediate impact of the debt arising from MNCs practice of profit shifting in the previous budget period, opts to spread the debt across 6 budget periods, so therefore 13-units ($12 + 1 = 13$ -units) are sufficient to meet the immediate needs, and the government adjusts the spread accordingly.

So the government now measures the tax burden at 13-Units ($12 + 1 = 13$ -units), and remembering that the corporate tax segment has been diminished in its capacity to contribute, disperses the tax burden as such:

c) 4-units personal income tax

d) 9-units corporate tax.

In any attempt to calculate the ramifications of such an allocation, we need to remember that the corporate tax participation has been significantly reduced by not being able to include MNCs who shift profits.

If we base all calculations on the government's previous budget re the tax base and tax burden, as used in this submission's arbitrary example, given that the tax base is now eroded to 67 percent of the previous, the comparisons would look like this:

a) Without regard to the previous tax base: Per centum 0.13 ($13 / 100 = 0.13$)

b) As 67 percent in comparison to previous tax base: Per centum 0.19 ($13 / 67 = 0.19$).

Effectively, the additional increase of 1-unit across the eroded tax base represents a per centum increase of a staggering 0.07 ($0.19 - 0.12 = 0.07$ -units), or 58.3 percent per centum increase.

This example serves to demonstrate, that the shortfall generated by MNCs profit shifting cannot be effectively satisfied by a tax increase, regardless that the example shows that the government has made every attempt to minimize the impact by distributing the created debt across a further 6 budgets.

Hence, in this scenario, the solutions available to the government are limited, and to offset the losses to the Australian economy that are generated through BEPS, it would have no choice other than to accept debt, and reduce and/or eliminate existing and planned vital infrastructure and services that Australians rely on.

And so starts a spiral that diminishes the prosperity and well being for all Australians.

Note: So as not to mislead observers in this discussion, I should reiterate that the figures used here are arbitrary, and only intended for the purpose of articulating a reasonable example, and should not be relied on as actual measurements.

However the example suffices to demonstrate the point I intend to make.

The Stimulus Spiral

Australians on whole are voracious consumers of imported goods, making Australia a highly profitable marketplace for MNCs. If the corporate taxes lost to Australia through MNCs profit-shifting practices were applied to the tax base, then the tax base would be sufficiently broad enough to distribute the additional derived revenue between:

- a) Lowering the overall average tax burden on corporate and personal tax, and
- b) Increasing the quality and level of the services and infrastructure that it produces and manages on behalf of all Australians.

What if we were able to reverse MNCs behavior, and rather than divesting the host country as in the BEPS cycle, MNCs invested in their host countries future prosperity. What would a “Stimulus Spiral look like? An example may be:

The Setup Phase

1. The investment would be straightforward. MNCs would cease profit shifting, and contribute to the host countries tax base.
2. Subsequent budgets 1 and 2, may see little if any, immediate benefit to the MNCs bottom line as compared to profit shifting, however in this period, the host country benefits in the broadening of its tax base, and is able to plan how it might best start the economic healing process.
3. Once measured, the host country may decide:
 - i) To marginally reduce the tax burden on corporate tax.
 - ii) That there would be no immediate benefit to personal taxes, as the full benefit of the initial revenue should rightly go to business, thus rewarding its new MNC business partners for their participation.

And so, commence the initial process of reducing the tax burden on corporate taxes.

It may also decide that increases to further infrastructure and services might be held relatively in check during this initial process.

4. In a subsequent budget, the host country would then spread the benefit and make a further reduction in corporate tax, and an initial reduction in personal income tax, and commence allocating funds for additional infrastructure and services.

The Stimulus Cycle

5. The ongoing reduction of the average corporate tax burden, together with the initial reduction to the average personal tax burden, by its nature generates and establishes a natural stimulus cycle, which may be perpetual, or until it achieves the targeted milestones, at which point, the host country may then focus subsequent benefits towards:
 - i) Improving infrastructure and services, and
 - ii) Surpluses to protect its new prosperity against unforeseeable economic shock, and
 - iii) Further focus on specific tax reductions to those who can least afford their specific circumstances.

How It Works

- a) As the reduction of the average personal tax burden leads to higher personal wealth, it delivers higher levels of disposable income that stimulate higher levels of spending, which in turn
- b) Stimulates higher volumes of business turnover, which in turn
- c) Generates higher volumes of business profits, which in turn
- d) Generate higher (by volume) Government revenues, leading to further opportunities for the government:
 - i) To redistribute the resulting surpluses.
 - ii) Further reduce average tax burdens, and
 - iii) Further increase the quality and levels of services and infrastructure.

And then... simply go back the beginning of the paragraph, and continue the stimulus cycle ...

Notwithstanding the multitude of spinoff, but rating highly would be additional GST to states, and greater employment and manufacturing opportunities.

This ought to be a favorable proposition for MNCs to invest in, and a win-win for the host country, its MNC partners, and all Australians.

If we can agree that the stimulus spiral is a cause and effect of the positive actions that generate it, then we should also agree that the reverse actions of a BEPS cycle, will spin in the opposite direction and cause the opposite impacts, and this is where we are now.

The current BEPS cycle that MNCs have placed Australia in is a self-serving and shortsighted approach by MNCs, and unsustainable, as the model destroys what sustains it.

The medium and long-term view, is MNCs investment in supporting, thus sustaining the host, and in doing so, support their themselves.

How We Get This Done

In understanding how we might encourage and persuade Multi-National Corporations to change their corporate behavior towards its practices of BEPS, we should firstly examine the rational that drives the practice, secondly identify who is impacted by the practice (the stakeholders), thirdly examine the impact to each of the stakeholders, and fourthly identify the real and potential benefits and advantages for MNCs to take an alternative approach and invest in those who support them.

And ask our government to prepare and present this argument on our behalf.

Observations

There is obviously an argument that supports the reduction of both personal and corporate taxes, and the March 2015 Intergenerational report, suggests that the Australian Government endorses average tax reduction. However, the report also presses home that we must live within our means.

The Corporate practice of profit shifting erodes the tax base in the regions that such corporations operate, and in turn, their actions appear to be a significant factor in the government's inability to affordably reduce the overall corporate tax rate.

The practice of corporate profit shifting is a shortsighted approach to the immediate self-interests of these corporations.

It cannot be considered to be in the long-term interest of Multinational Corporations, if their profit shifting practices lead to economic stress and impoverishment of the regions they syphon. The natural downward spiral of economic stress can only lead to diminished human living standards, and an ever increasing downturn in consumer affordability and demands on the products and services the same Multi-Nationals offer.

The flipside of the coin is;

- a) That if not in fairness towards the regions that support their profitable enterprises, then
- b) For their own long-term self-interest, Multi-National Corporations support the economic health, growth and stability of the regions they operate within by a fair contribution to corporate taxes on the profits realized in those regions. Thus an investment in the region that leads to improved and sustainable economic conditions, leading to improved human conditions.

And whilst Multi-Nationals may have little or no concern in how such an investment beneficially impacts a regions populace, such as improved health, education, and social support, derived from the disbursement of government revenues, that are vital ingredients to the human condition of contentment and well-being, Multinationals may look towards government affordability to reduce personal tax, and corporate profits tax rates.

A Further Observation

Notwithstanding that a government is unlikely to increase tax rates, and is more likely to offset the eroded tax base by reducing planned infrastructure and services, this submission hopes to demonstrate what would likely be required if Australians attempt to hold a government to planned promises, with a threat of deliver promises or face dismissal in a following election.

The truth of the matter is, that regardless of the government of the time, the issues remain the same, and a change in government would only serve to set us all back on resolving issues generated by BEPS, as a newly elected government could be standing at a blank whiteboard, to start all over again.

However opposing governments do not stand idle, and develop their forward policies on a basis that they will be elected, or give it reason to block changes by an incumbent government if it considers the basis of the changes to be flawed.

Besides, if an opposing government believes it has already developed credible solutions to BEPS and the trickle-down impact on the prosperity of all Australians, then the responsible action would be to adopt a bipartisan approach and offer assistance to the incumbent government in resolving our economic challenges, and the responsible action of the incumbent government, would be to accept such assistance.

Perhaps what Australians need, are more senate working groups comprised of a balanced mix of all parties, who can jointly work through issues, and jointly submit single sets of recommendations that are agreed upon to parliament for action. And hence giving credit to all parties on the reforms that follow their joint recommendations, and thus benefit all Australians, and effectively eliminating those issues from party politics at election time.

Summary

All Australians, private citizens and businesses alike, feel the everyday pressures and effects on the Australian economy, and should support the governments current approach to bring all Australians into its confidence, in respect to its honesty on the current state of the economy, and the potential risks and challenges that we face as a nation.

Australians should reasonable expect its government, both incumbent and in opposition to adopt a unified bipartisan working relationship and approach to meet challenges that threaten Australia's economic viability, and to put in place, improved systems that not only resolve the know issues of today, but also provide a suite of shock resistant protective options, measurers and countermeasures against unforeseeable future shocks and events that may threaten both our domestic and international trade, commerce and economic viability.

I commend the Government in commencing this dialogue with the Australian people, for whom it represents, and also commend the Hon Joe Hockey MP, and the Government for its use of everyday common language in understandable layman terms, and trusting that in understanding the challenges, the Australian people will come onboard.

I also trust in todays "Government in Opposition" led by the Hon Bill Shorten MP, and its collective care and concern in the welfare of the Australian people, and the application of its social reform skills in support of the current government, thus adding further dimension to the benefits of such a bipartisan approach and effort.

Ultimately, and in any event; if MNCs cannot be encouraged or persuaded by their own volition to change their corporate behavior in regards to BEPS, then in the interests of all Australians, the Government, both incumbent and in opposition, must work jointly to take whatever actions are available, and eradicate the practice of BEPS from the Australian Business-Scape.