# Tax Justice and Debt

Presentation at the IAMREC's Corporate Power Seminar
Panama City
August 2, 2018

LEONCE NDIKUMANA
University of Massachusetts Amherst
ICRICT Commissioner

# Context

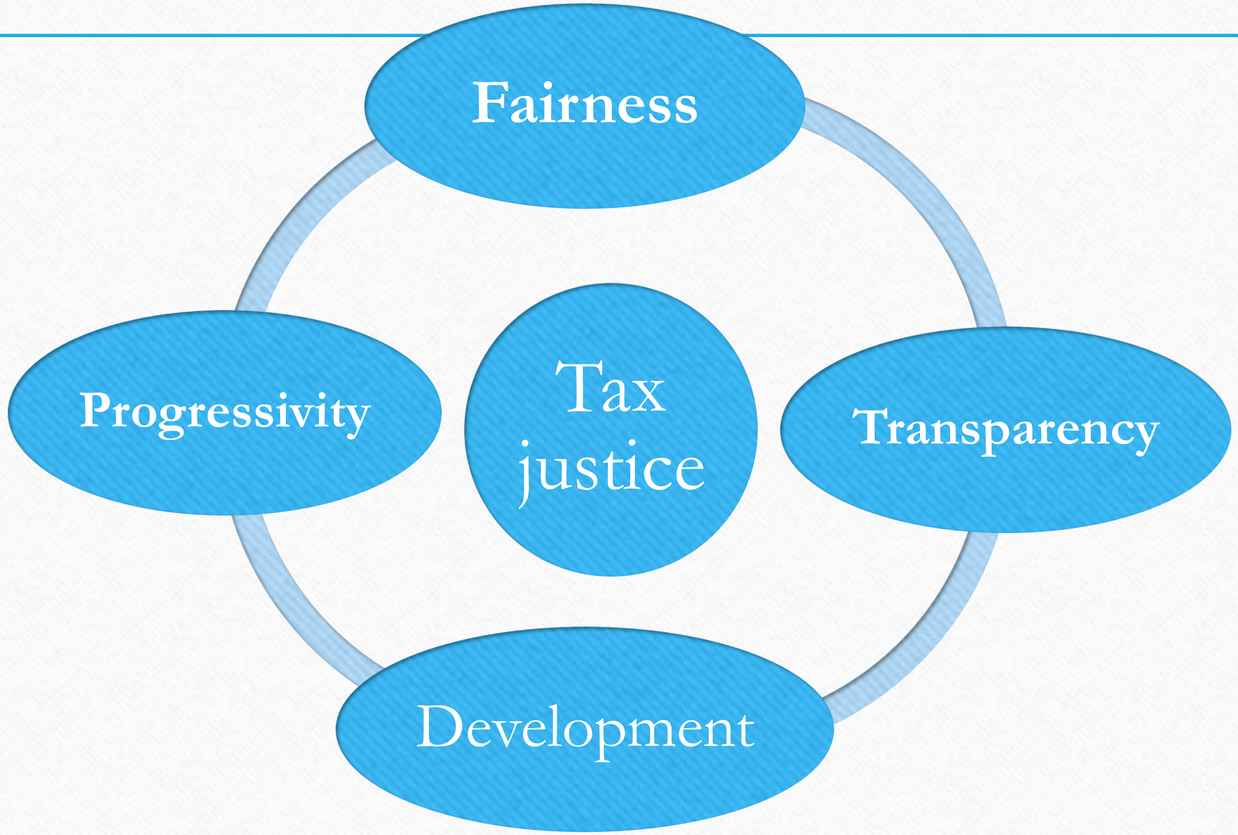
- The global economic system
  - Dominance of 'stateless' firms – multinational corporations (MNCs)
  - Resurgence of anti-regulation/deregulation movement – attack on regulation by "big capital"
  - Renewed attack against Labor Unions
  - Disproportionate burden of taxation falls on labor more than on capital
  - Capital mobility, secrecy jurisdictions, offshore finance, tax evasion and race to the bottom
- Global governance architecture
  - "Elite clubs" dominating global policy making – issues of voice and representation
  - Lack of global institutional framework for tax cooperation
- Third World debt and the capital flows paradox

"What is capitalism? It rewards those who work hard. But it also rewards those who **take advantage of others**"



Source: Video "The China Hustle", Regina Public Library (2017). https://www.reginalibrary.ca/film-theatre/browse-films/672673

# What is 'Tax Justice'?



One major constraint to sustainable development is inadequate domestic revenue mobilization. Actual tax revenue collection is low and below potential in the majority of developing countries.

**This results in large and widening financing gaps, and increased dependence on external financing including debt**

# Average tax rates 2008-2013 (% of GDP)

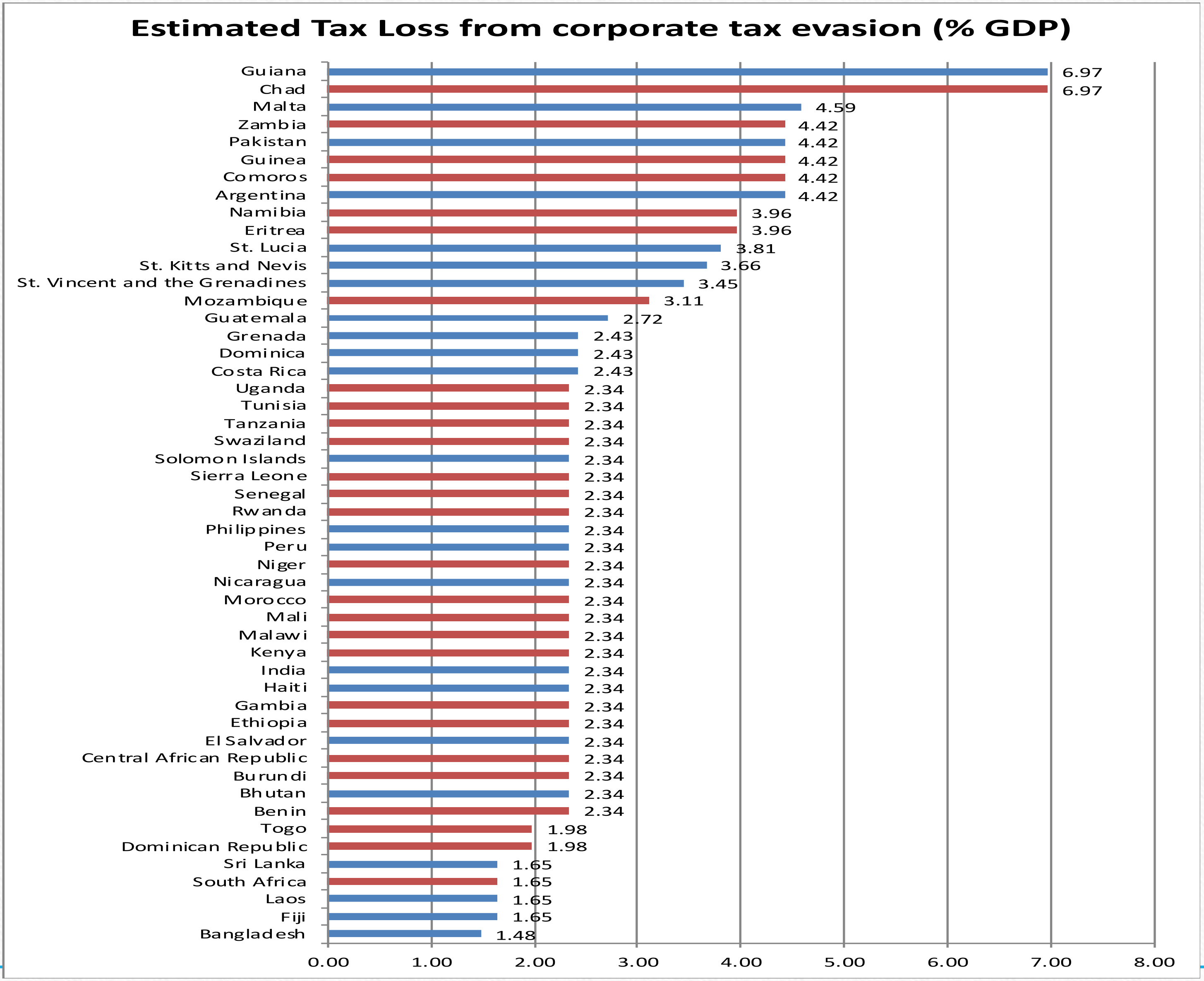
| | Total tax/GDP | Corporate tax/GDP |
|---|---|---|
| **Selected African Countries** | | |
| **Ethiopia** | 10.6 | 1.4 |
| **Nigeria** | 8.3 | 2.7 |
| **Lesotho** | 34.8 | 6.0 |
| **South Africa** | 26.3 | 6.6 |
| **Seychelles** | 31.6 | 7.2 |
| **Selected Latin American Countries** | | |
| Argentina | 21.0 | 2.9 |
| Brazil | 24.1 | 3.0 |
| Chile | 18.5 | 2.8 |
| Colombia | 14.4 | 1.8 |
| Panama | 10.8 | 2.4 |
| **Global averages by income group** | | |
| **LIC** | 14.2 | 2.1 |
| **LMIC** | 19.4 | 3.0 |
| **UMIC** | 20.9 | 3.2 |
| **HIC** | 24.6 | 3.2 |

# Taxation of Multinational Corporations poses critical challenges for tax justice

- Increasing complexity of the transnational corporation with regard to:
  - Ownership
  - Residence for tax purposes – often dissociated with the point of production
  - Dominance of intra-firm trade in global trade; facilitates trade misinvoicing and abiusive transfer pricing
- 'Unitary taxation' of multinational firms:
  - Enables MNCs to minimize tax by taking advantage of loopholes in national tax systems
  - Enables profit shifting among branches of the same corporation
- Lack of global coordination in taxation policy
  - Enables MNCs to game the system and minimize tax liabilities through **trade misinvoicing, transfer pricing, thin capitalization**, and other illicit practices.

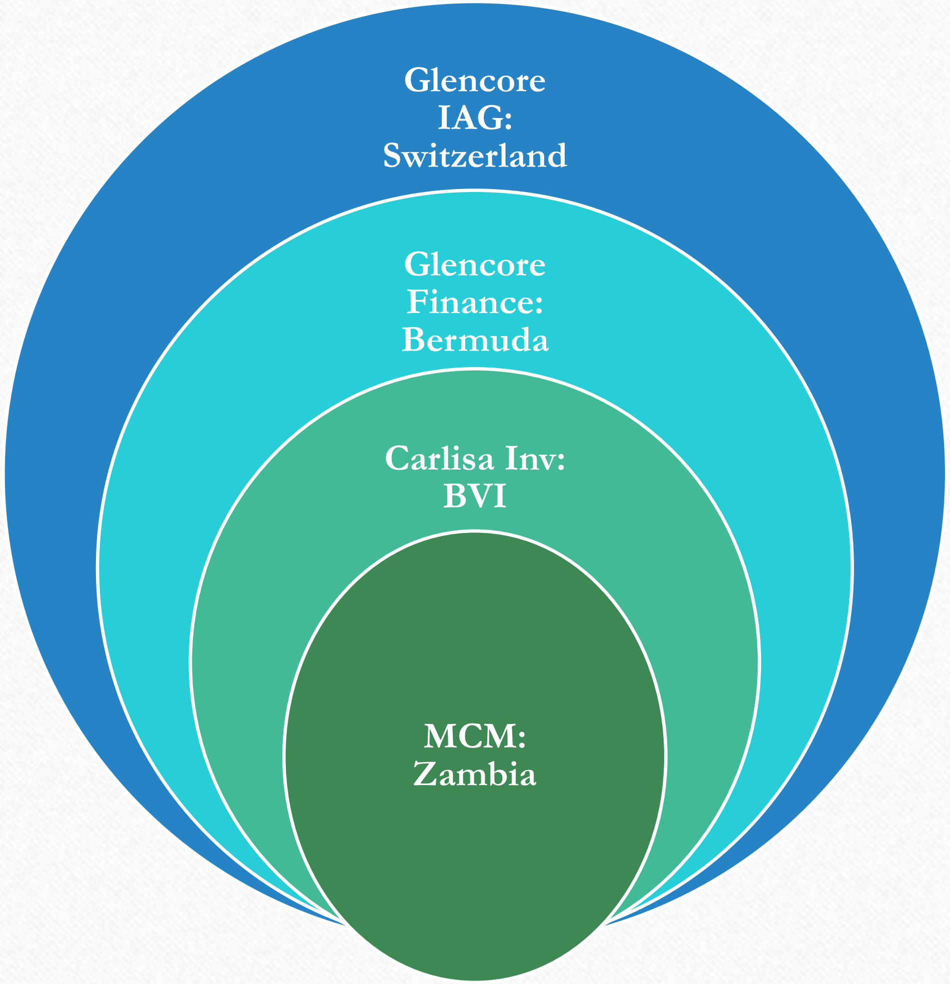
# Mechanisms of tax evasion by MNCs

- Banking secrecy allows the concealment of the origin of funds held abroad.
- Thin capitalization allows MNCs to artificially reduce taxable profits through intra-firm lending and borrowing
- Use of "nominees" to hide the identity of the true owner of assets held abroad.
- Limited or no disclosure of company accounts results in inconsistent reporting of corporate tax liabilities.
- High-level client confidentiality and banking secrecy prevent public scrutiny on trade and financial records of multinational corporations.
- Low or zero tax rates in some territories, including tax exemptions, allow corporations to shift expenses and revenues across jurisdictions, through subsidiaries and shell companies.



Estimated Tax Loss from corporate tax evasion (% GDP)
Guiana 6.97
Chad 6.97
Malta 4.59
Zambia 4.42
Pakistan 4.42
Guinea 4.42
Comoros 4.42
Argentina 4.42
Namibia 3.96
Eritrea 3.96
St. Lucia 3.81
St. Kitts and Nevis 3.66
St. Vincent and the Grenadines 3.45
Mozambique 3.11
Guatemala 2.72
Grenada 2.43
Dominica 2.43
Costa Rica 2.43
Uganda 2.34
Tunisia 2.34
Tanzania 2.34
Swaziland 2.34
Solomon Islands 2.34
Sierra Leone 2.34
Senegal 2.34
Rwanda 2.34
Philippines 2.34
Peru 2.34
Niger 2.34
Nicaragua 2.34
Morocco 2.34
Mali 2.34
Malawi 2.34
Kenya 2.34
India 2.34
Haiti 2.34
Gambia 2.34
Ethiopia 2.34
El Salvador 2.34
Central African Republic 2.34
Burundi 2.34
Bhutan 2.34
Benin 2.34
Togo 1.98
Dominican Republic 1.98
Sri Lanka 1.65
South Africa 1.65
Laos 1.65
Fiji 1.65
Bangladesh 1.48
0.00 1.00 2.00 3.00 4.00 5.00 6.00 7.00 8.00

# Example: Corporate Structure of Mopani Copper Mines (MCM)






Note: BVI = British Virgin Island. Source: Sharife, Khadija (2011) 'Transparency' hides Zambia's lost billions. *Al Jezeera.Net* 18 Jun 20, 2011.

Example:

# Estimated tax losses by African countries due to SABMiller's tax dodging

| Country | Royalty payments (thousand £) | | Payment of management fees (thousand £) | | Total estimated tax loss (thousand £) |
|---|---|---|---|---|---|
| | Royalties paid | Estimated tax loss | Management fees paid | Estimated tax loss | |
| Ghana | 304 | 52 | 932 | 160 | 212 |
| Mozambique | 367 | 44 | 552 | 66 | 110 |
| South Africa | 18,300 | 5,100 | | | 5,100 |
| Tanzania | 2,280 | 340 | 5,660 | 1,100 | 1,440 |
| Zambia | 3,300 | 830 | 3,140 | 720 | 1,550 |
| Total | 42,800 | 10,100 | 40,200 | 8,100 | 18,200 |

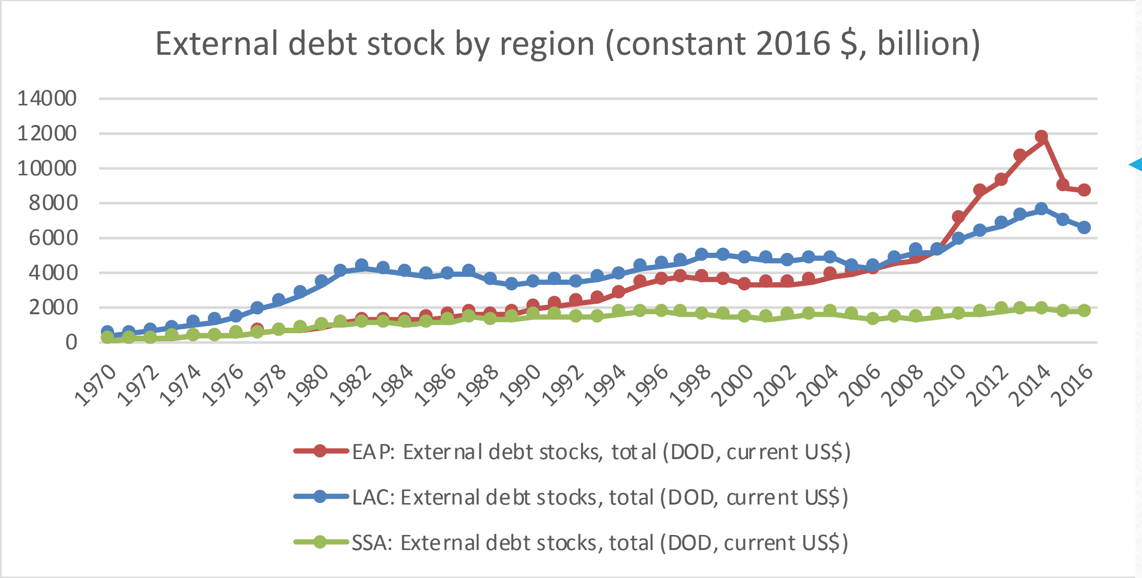
Source: Action Aid (2010). *Calling Time*. London: Action Aid.

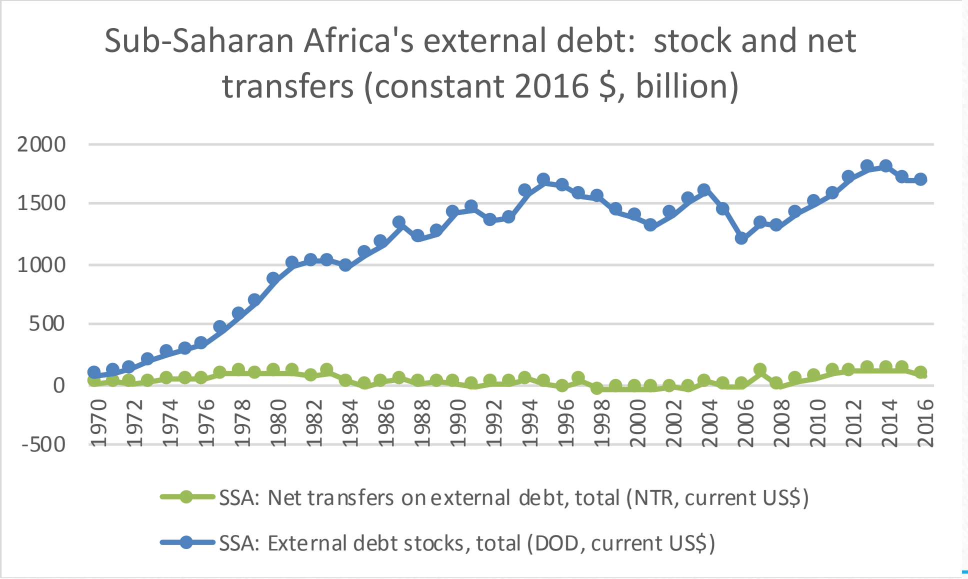
# Developing country debts and the capital flow paradox

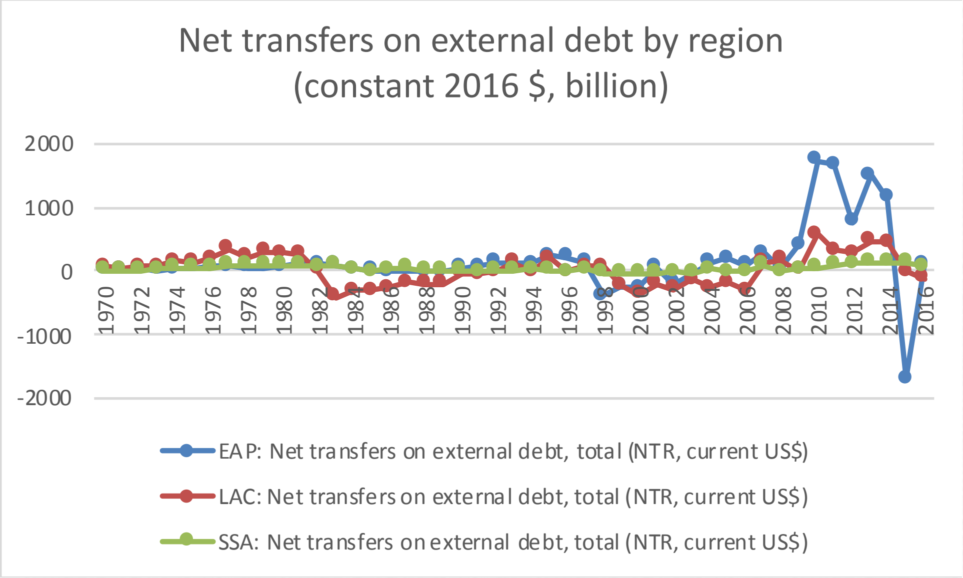
- Increasing burden of external debt
- But not corresponding to increased net resources for development financing
- At the same time, continued hemorrhage through capital flight and illicit financial flows
- Some of the capital flight is financed by external debt - 'odious debts'

# Rising indebtedness

Without commensurate increase in resource inflows



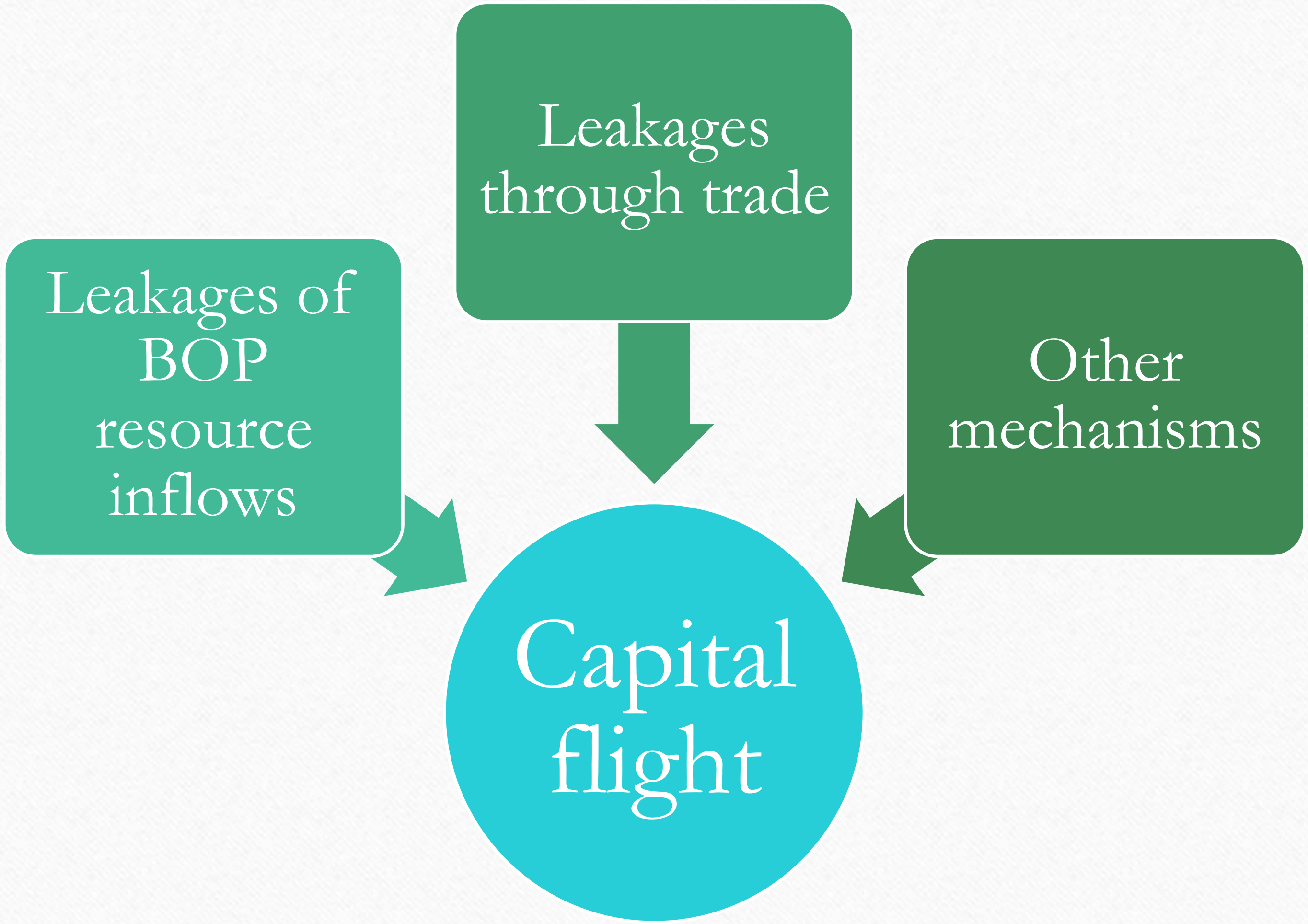



# Capital flight from developing countries

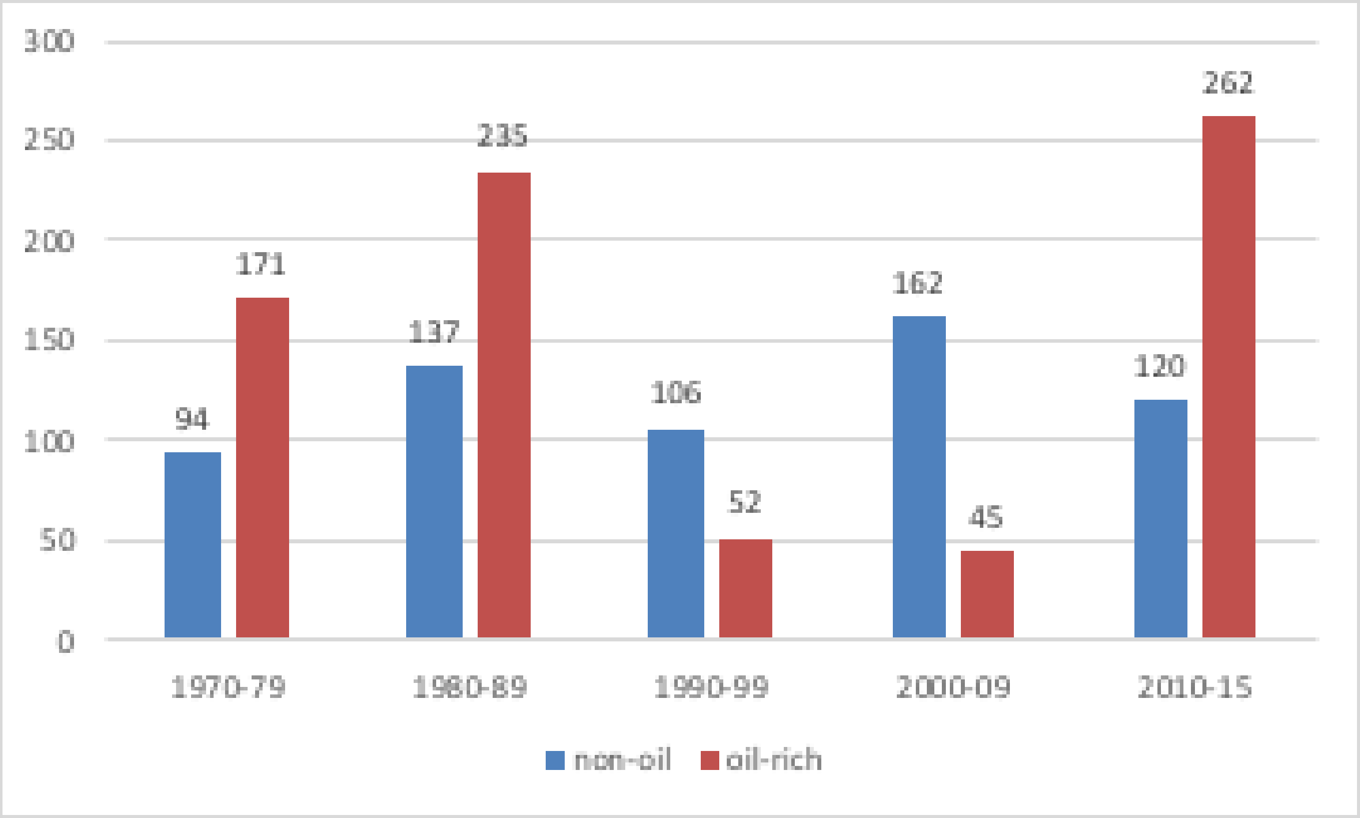
The volume of unrecorded outflows are large and increasing

It is a severe constraint to financing for sustainable development

# Key mechanisms of capital flight

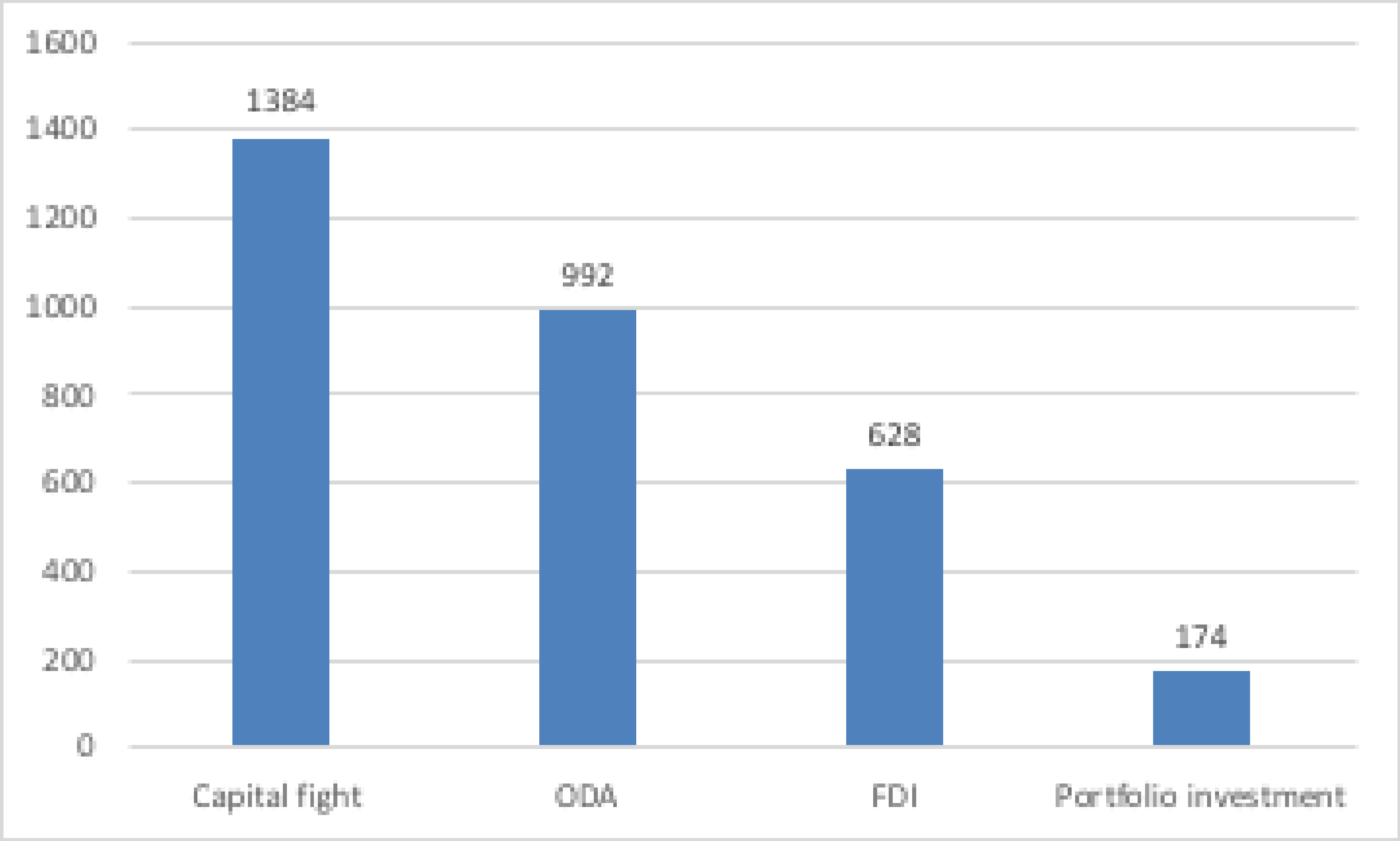


# **Estimates of capital flight from 30 African countries, 1970-2015** (billion, constant 2015$)



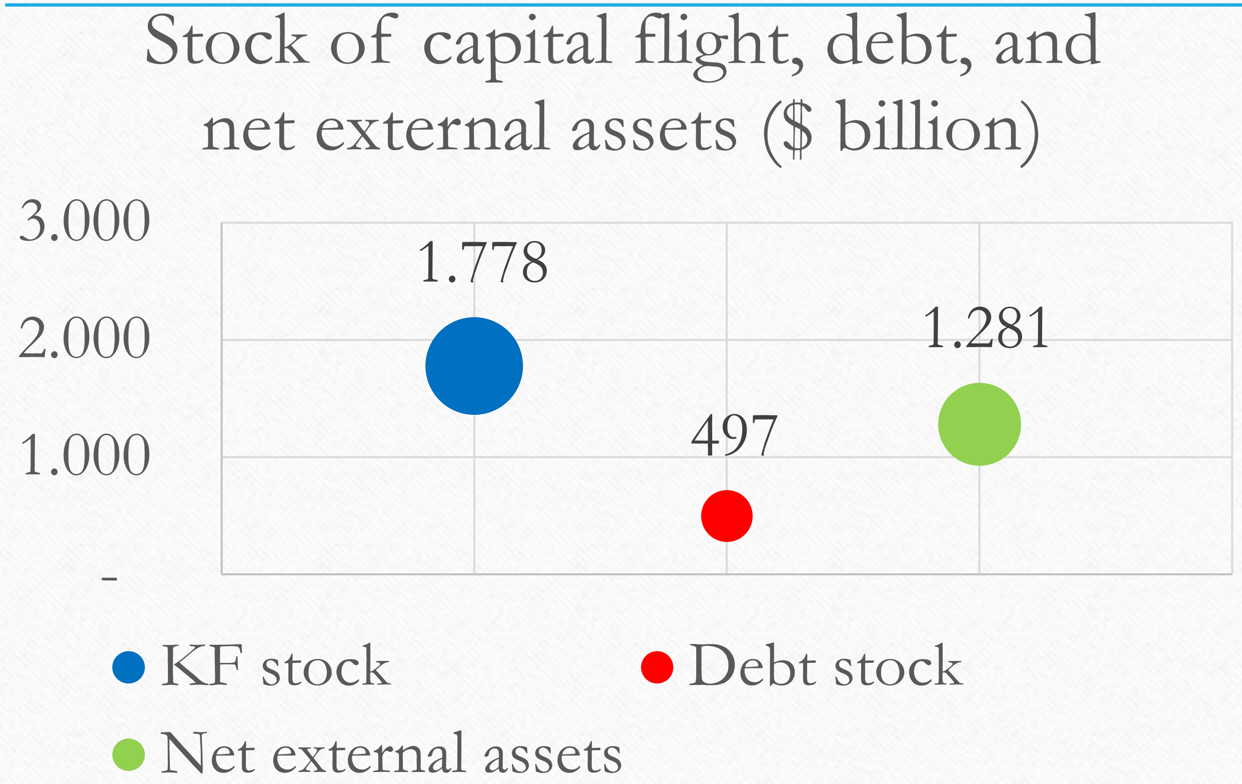

Source: https://www.peri.umass.edu/capital-flight-from-africa.

**Capital flight from Africa exceeds ODA, FDI and Portfolio Flows: Cumulative flows** (billion, constant 2015 $)




Source: https://www.peri.umass.edu/capital-flight-from-africa.

# Africa is a *'net creditor'* to the rest of the world!

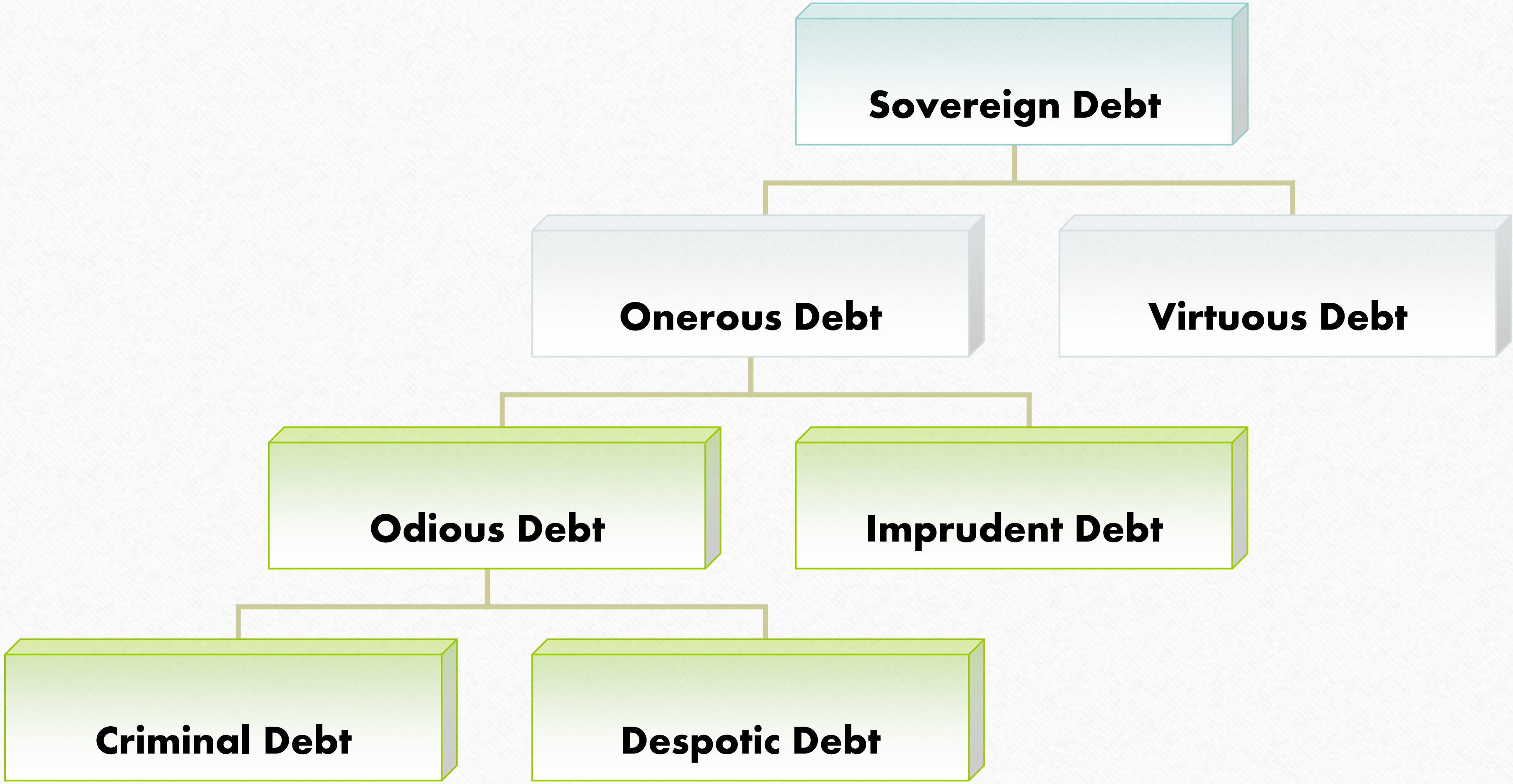



Net external assets = capital flight stock – debt stock

# Odious Debts

- Some of the capital flight is financed by external debt - 'odious debts'
- The people of developing (debtor) countries still incur the burden of servicing the full costs of debts, even those that they did not benefit from.
- Irresponsible lending and borrowing perpetuate severe economic injustice against the people of developing countries

# Not all debt is odious: Typology of Sovereign Debt



# What is the key to progress?

- Combatting the increasing imbalances between state (regulation) and corporations (laissez-faire); and between finance/capital and labor (workers)
  - Combat against the capture of the regulatory capacity of the state by the corporate sector and its support network (corporate lobby, free-market fundamentalists in academia and in think tanks, …)

- Changing the conversation: tax justice is a not developing-country problem but a global problem
  - Need to strengthen a global alliance against tax injustice

# Key to success (cont'd)

- Establishing the practice of **unitary taxation** (***see ICRICT proposal***); Enforce systematic/automatic exchange of information; enforce country-by-country reporting by firms.
- Leveraging the gains from success in bilateral arrangements against banking secrecy and corporate tax evasion (e.g., US against Swiss banking secrecy; US IRS Form 8975 on country-by-country reporting) to build stronger and inclusive multilateral bodies that advance the interests of both developed and developing countries
    - Resist reversions to nationalistic isolationism (e.g., repeal of the Dodd-Frank Act; US 'trade wars'; etc.)
- Knowledge, capacity building and advocacy
    - There is still inadequate investment in knowledge generation on tax justice, capital flight, odious debt; not 'subjects of conversation in polite company'
    - In the meantime, the beneficiaries of the status quo (corporations, banks, elites) consolidate their defense capacity; including through disinformation campaigns
- This is why this Conference is timely and welcome.