PUBLIC SERVICES
INTERNATIONAL

SUB-REGIONAL OFFICE FOR OCEANIA
PO Box 24233 Melbourne
Victoria 3001 AUSTRALIA
Mob/+61 467070242
tom.reddington@world-psi.org

Global agreement on corporate taxation – PSI submission to The Treasury consultation

31 October 2022

About this submission

Public Services International (hereafter PSI) is a Global Union Federation that represents public service workers from more than 700 trade unions representing 30 million workers in 154 countries. We are dedicated to promoting quality public services in every part of the world. Our members, two-thirds of whom are women, work in social services, health care, municipal and community services, central government, and public utilities such as water and electricity. PSI represents public sector and private sector workers who work in public services. Decisions around tax systems, in Australia and around the world, are central to our members interests as it raises the revenue required to fund quality public services.

PSI agrees to the publication of this submission.

Introduction

The Australian government published on 4 October 2022 a consultation paper on the G20/ OECD agreement on corporate taxation. Whilst the consultation seeks comments on Pillars One and Two of the global agreement, it is understood that the Australian government is exploring options for the immediate implementation of a global minimum tax (Pillar Two).

PSI welcomes the opportunity to submit its observations on such important corporate tax reforms. At the same time, we are concerned that several of the questions focus on cost and administrative burden on multinational enterprises. Just as water always goes to the lowest point, it should be expected that businesses will raise significant objections to increased effective tax rates and accompanying compliance costs. These objections must not justify poor ambition in public policies. The lack of decisive action to tackle profit shifting and tax competition generates very significant cost to society in general, and to workers in particular.

In recent years there has been a heightened public awareness that many multinationals do not pay a fair share of tax. This not only robs communities of the public services they need to thrive, but it also erodes trust in taxations systems and the institutions which govern them.

This submission calls for a global minimum tax setting a 25% minimum rate, with a broad scope of application and a design that guarantees a fair outcome to both source and residence countries. It also calls for continued multilateral negotiations with a view to eventually address the under-taxation of digitalized businesses.

The following section 1 recalls labour main demands for corporate tax reform. Section 2 provides an overview of the costs and benefits of the G20/ OECD agreement from a workers' perspective. Sections 3 outlines PSI recommendations for the implementation of a global minimum tax. Section 4 calls for further negotiations on a Pillar One, which in its current form does not address the tax challenges arising from the digitalization of the economy.

1. Public sector workers' demands for corporate tax reform

Public sector unions are actively engaging with policymakers on the dire need to address the chronic underfunding of public services across all jurisdictions in Australia. The importance of frontline line public sector workers has been etched in the community's mind from the experience of the COVID-19 pandemic, yet governments are increasingly reverting to austerity politics which cuts the pay, conditions of these workers. Clamping down on corporate tax avoidance and ensuring they pay a fair share of tax provides an important opportunity to contribute revenue for sustainable and effective public services across the country.

We are calling for stronger regulations to tackle corporate tax avoidance. We pursue in particular the following three priorities:

- Enhanced tax transparency[1];
- A 25% global minimum tax rate;
- Unitary taxation, on the basis of fair apportionment factors – including employment, assets and sales.

Governments failure to tackle profit shifting and tax competition harms employment in at least three ways.

First, expanded fiscal space is of the utmost priority to the public sector unions. In a context of post pandemic bottlenecks, prospects of low economic growth and negligible employment generation, growing debt at sovereign, corporate and household level, energy crisis and increased cost of living, workers and their communities are deeply concerned about possible resurgence of austerity measures, that may lead to the worst case scenario of stagflation: recession with high inflation.

More and more progressive tax revenues are needed. Corporate tax avoidance costs some $500bn-$600 bn globally in lost progressive tax revenues. This robs communities of the services they need to thrive and undermines the ability of governments across all jurisdictions to fund health and education services, social protections and general public services to keep people safe and also to keep the economy running.

Second, aggressive tax planning stands in the way of a fair share of corporate profits. Profits are extracted from workplaces and sent to tax havens where they are not available for wage bargaining, productive investment and job creation.

Third, complex company group structures obscure employment liabilities. The artificial structures used to minimise corporate income taxes are the same ones that are used to circumvent labour law obligations. For instance, letterbox companies are a frequent vehicle for social fraud in Europe. Overall, when management is hidden behind several layers of artificial corporations, workers and their unions find it difficult to effectively exercise social dialogue.

Whilst the G20/ OECD agreement lays some foundation for much needed corporate tax reform, it has not achieved a level of ambition necessary to a fair and effective international tax system.

[1] On 2 September 2022, PSI submitted observations to the Treasury consultation on multinational tax integrity and tax transparency. In this submission we called for mandatory public country-by-country reporting, on the basis of the GRI tax standard with a wide scope of application.

2. The G20/ OECD agreement : costs and benefits to workers

Lack of impact assessment

Overall, PSI is concerned that a global deal has been reached in the apparent absence of reliable impact assessment. The economic study released by the OECD in 2020 is based on early versions of Pillars One and Two. Since then, the whole Pillar One has been completely rewritten and significant concessions, including a domestic top up tax, have been inserted into Pillar Two. Importantly, country-by-country estimations have not been released. For several countries, possibly including Australia, it even appears that accurate revenue estimations have not been carried at all.

In addition to revenue estimations, the G20/ OECD agreement should have come with a behavioural impact assessment with a view to anticipate possible responses from businesses and any side effect on employment.

The absence of reliable impact assessment goes against good regulatory policy principles. It also deprives stakeholders from information essential to form an opinion and to actively contribute to the public debate.

PSI therefore encourages Treasury to publish a complete and transparent impact assessment of various policy options before finalizing any policy decision.

Pillar One

PSI is very critical of the current transfer pricing rules, which we regard as both a key enabler for profit shifting and the main reason for the under-taxation of highly digitalized businesses. Digitalized businesses can indeed shift around unique and highly valuable intangibles without much constraint from the arm's length principle.

The labour movement has long been calling for a decisive switch towards unitary taxation and formulary apportionment. Only then would multinational enterprises be treated for what they are: global entities with a coherent business and tax strategy throughout the firm.

With Pillar One, the OECD formally recognizes that unitary taxation is the only way to deal with the digitalization of the economy. As such, Pillar One is a significant shift away from transfer pricing rules. However, that shift is restricted to a very small proportion of corporate profits. The significance of the reform is further undermined by the recognition of one allocation factor only (sales), leaving aside other factors of value creation, including employment.

As a result, the concrete impact of Pillar One is negligible. According to a recent study, the proposed Pillar One only affects 78 MNEs of the world's 500 largest companies[2]. It is worth noting that according to this study, the decision to exclude financial companies from Pillar One has reduced the expected allocation of profits by around half.

If the Pillar One Convention is ratified by a critical mass of jurisdictions, countries will be expected to renounce digital services taxes or equivalent unilateral measures. Because of the extremely limited scope of the proposed reform, some countries are bound to be losing revenues. Thus, it is very unclear how Pillar One is tackling the overall under-taxation of highly digitalized businesses.

Pillar Two

By introducing the principle of a minimum effective tax rate, Pillar Two represents a fundamental shift away from the tax competition narrative. It also has the potential to undermine the incentives for companies to use tax havens and thus over time "break the tax haven model".

[2] Devereux, Simmler (2021), *Who will pay Amount A?*

The global labour movement has therefore expressed a strong support for the principle of a global minimum tax[3]. At the same time, trade unions are critical of the OECD model rules, which contain important weaknesses. If implemented, these concessions will significantly undermine revenue raising potentials. The weaknesses include:

- a minimum rate of 15% that is too low to stop tax competition. It should be recalled that the average effective tax rate in OECD countries ranges between 20-25%. ;
- a limited scope (high threshold and sectoral exemptions), which leaves most corporations out of reach;
- A substance based carve out excluding significant corporate income from the tax base;
- An important concession to tax havens in the form of a domestic minimum tax, which may ultimately defeat the whole purpose of a global minimum tax rate;
- A design that gives priority to countries where the companies formally establish their headquarters, to the detriment of all other countries hosting economic activity. This last aspect is particularly detrimental to developing economies, which are comparatively more reliant on corporate tax revenues than OECD economies.

PSI warns against a "copy-paste" exercise of the OECD model rules as the structural weaknesses of the global agreement do need to be addressed.

3. PSI recommendations for an effective global minimum tax

PSI calls on Treasury to build on the momentum for a global minimum tax while at the same time addressing its structural weaknesses. Australia could set an influential precedent for countries around the world to capture lost corporate tax revenues, This is indispensable to effectively stop corporate tax competition, to reduce profit shifting and to raise substantially more corporate income tax revenues. In the longer term, progress at national level will constitute a decisive element for the negotiations of more robust multilateral reforms.

Australia has a unique opportunity to show the way and set precedent for countries to capture missing tax revenues and to fund vital public services around the world.

A broader scope of application

The USD 750 mn turnover threshold excludes the majority of companies in Australia and worldwide. The threshold should therefore be reduced. A good practice is Spain, which has in its 2022 budgetary law already established a global minimum tax for enterprises with a net turnover equal to or exceeding EUR 20 mn or to entities having elected for the tax consolidation scheme irrespective of their turnover.

Furthermore, the scope of the minimum tax should be extended to all sectors. Sectoral exemptions brought significant limitations to the scope of Pillar Two. Investment and pension funds, international shipping, and domestic companies seeking to expand internationally would not be affected. Yet, the financial sector in particular is significantly under-taxed due to their tax planning activities.

Rejection of domestic minimum tax with a regressive design

The consultation suggests implementing a domestic minimum tax in Australia. The domestic minimum tax is a last minute addition into the Pillar Two model rules, inserted without any concertation with stakeholders. The OECD model rules do not give any indication on what a domestic minimum tax should look like.

[3] See for instance: G7: More urgent action needed to make a fair corporate minimum tax a reality - PSI - The global union federation of workers in public services ; Minimum global corporate tax rate: a launchpad for greater ambition - International Trade Union Confederation (ituc-csi.org) ; ETUC urges EU to back global tax deal - and go further in EU | ETUC

The labour movement strongly opposes the domestic minimum tax if this means further weakening the potential impact of Pillar Two. Such would be the case in particular of a proposal currently being discussed in the European Union[4].

According to the European version of a domestic minimum tax, a source country could decide to enforce a minimum effective tax rate not for all corporate profits but only for the profits that fall within the scope of the Directive. A relevant element in the decision of EU tax havens to introduce a domestic minimum tax instead of raising effective tax rates for all corporate profits is the so-called substance carve out: companies would still enjoy tax cuts for the income that is not included in the Pillar Two tax base. As evidenced by a recent economic study, those tax cuts could go as low as 0% at no or little cost to the tax haven[5].

If countries choose to implement a domestic minimum tax following the European proposal, effective tax rates will be set under 15% (for the income falling within the substance carve out as well as for companies excluded from the scope of the Directive) whilst at the same time ensuring that other countries do not claim taxing rights for the corporate income that falls within the tax base of Pillar Two.

Therefore, the introduction of a domestic minimum tax into Pillar Two is a game changer. It has the potential to cancel revenue prospects for high tax countries. Pillar Two could still remain a useful tool to address the worst forms of tax incentives. It would, however, fail to increase fiscal space, which is a fundamental trade union priority.

Towards a progressive domestic minimum tax

PSI calls on Treasury to consider the implementation of a progressive domestic minimum tax. The OECD model rules do not give any indication as to what a domestic minimum tax should look like. Thus, what constitutes a potentially serious defect of the OECD model rules could also be turned into a powerful instrument for raising effective tax rates in Australia and worldwide.

This progressive domestic minimum tax must include 1. a wide scope of application, without carve out nor sectoral exemptions, and 2. an at least 25% effective tax rate.

Implementing an ambitious domestic minimum tax in conjunction with the OECD model rules means that Australia would come first in the collection of the top-up tax – whether it is home to a multinational enterprise or whether it hosts some of its economic activity – but also that it can apply a rate that is much closer to Australian statutory rate. The table below evidences the very significant revenue differences between 15% and 25% rate in Australia. (Note: these estimations are for a global minimum without carve out).

Table 1: Revenues of a global minimum tax of different tax rates in 2021 billion € based on country-by-country data of the fiscal year 2017

[4] Proposal for a Council Directive on ensuring a global level of taxation for multinational groups in the Union COM (2021) 823 final

[5] Devereux, Vella, Wardell-Burrus (2022), *Pillar 2 : rule order, incentives and tax competition*

	Revenues in billion EUR (2021) for a minimum tax rate of....			
Parent Country	15%	21%	25%	30%
Argentina	0.1	0.2	0.2	0.3
Australia	1.8	7.0	11.8	17.8
Brazil	1.5	6.2	10.5	16.1
Canada	24.4	43.8	56.7	72.9
Chile	0.0	0.0	0.1	0.3
China	6.1	29.7	61.1	100.7
India	0.5	1.1	1.5	2.2
Indonesia	0.1	0.6	1.3	2.3
Isle of Man	0.1	0.1	0.2	0.2
Japan	5.9	19.5	46.2	80.0
Korea	0.0	6.9	15.5	26.3
Malaysia	1.6	4.6	6.6	9.1
Mexico	0.4	0.8	1.1	1.6
Norway	0.3	2.4	4.7	7.7
Peru	0.1	0.4	0.8	1.3
South Africa	3.8	7.1	9.4	12.3
Switzerland	7.5	12.4	15.9	20.6
United Kingdom	11.0	29.4	43.4	60.8
United States	57.0	150.0	229.1	331.6

Source: EU Tax Observatory, October 2021

4. Pillar One – the need for further negotiations

Tackling the tax challenges of digitalisation has been a priority for the G20/ OECD since 2015[6]. This priority has still not been addressed. Under Pillar One, the vast majority of corporate profits of highly digitalised multinationals will continue to be taxed according to the current, ill-adapted, transfer pricing rules.

Whilst unprecedented, the current proposals are not enough. The labour movement continues to call for a longer-term fundamental reform of the international tax system. Unitary taxation should be introduced for all corporate profits and based on allocation factors representing all factors of production, including assets and employment - not just sales.

END.

For Inquires relating to this submission please contact
Tom Reddington, Sub-regional Secretary for Oceania, Public Services International
Tom.reddington@world-psi.org
0467 070 242

[6] Action 1, Tax Challenges arising from Digitalisation, BEPS Action Plan 2015