Corporate tax avoidance fathers austerity

In the wake of the tax scams in Luxembourg **Prem Sikka** explains how manufactured tax avoidance schemes are eroding social democracy

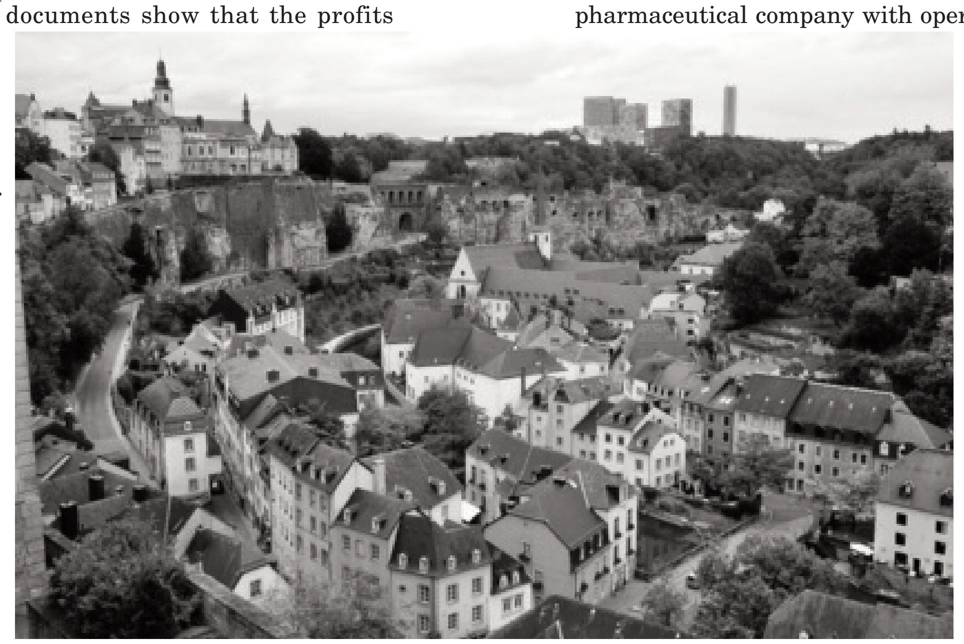
Globalisation has opened up new avenues for the advancement of neoliberalism. Not only does it demand light touch regulation, faith in mythical free markets and unhindered mobility of capital, it further demands that the state be starved of tax revenues. A state starved of tax revenues cannot meet citizens' demands for social democracy. With erosion of tax revenues, the state increasingly has to resort to debt to finance social infrastructure. In doing so, it increasingly falls under the spell of financial markets and becomes more concerned about, debt repayments, cost of debt and reducing public services. This leads to a smaller but more compliant state, so desired by neoliberals, whilst ordinary people face the erosion of rights and purchasing power, and almost permanent austerity.

The post Second World War social settlement required the state to attach greater weight to the concerns of citizens. This resulted in huge public investment in coal, gas, water, steel, shipbuilding, electricity, education, railways, pensions, biotechnology, information technology, the NHS and much more. The settlement was beneficial to business; it supplied goods and services to the state at an unprecedented rate. The social settlement provided stability, so vital for profitable business activity. However, all this is now unravelling as economic elites want higher returns without necessarily taking greater risks. They no longer consider themselves bound by the old settlements. Organised corporate tax avoidance is a key part of a strategy that increases private returns without any additional risks and at the same time starves the state of tax revenues.

Tax avoidance games

The latest evidence for starving the state comes from some 28,000 pages of leaks by a former PricewaterhouseCoopers (PwC) employee-based in Luxembourg, a place well known for secrecy, lax regulations and a government that enables corporations to undermine tax revenues in other places. The leaked documents relate to over 1,000 corporations and are available at the website of the International Consortium of Investigative Journalists (www.icij.org). They show that PwC designed complex tax avoidance schemes for hundreds of companies. Of course, PwC is not alone as it together with other big accountancy firms (KPMG, Deloitte & Touche and Ernst & Young) manufactures tax avoidance schemes at an industrial scale to enable their clients to escape taxes. The beneficiaries include Abbott Laboratories, Aviva, Axa, Citigroup, Deutsche Bank, Dyson, Disney, e-on, Heinz, HSBC, IKEA, Koch, Pepsi, Procter and Gamble, Shire, Skype, Taylor Wimpey, Wolseley, and many more. No sector of the economy is immune from the tax avoidance games.

The avoidance schemes are mass marketed. They involved the creation of complex corporate structures to enable companies to shift profits from comparatively high tax rate jurisdictions to a low-rate jurisdiction, such as Luxembourg. Profits are shifted through spurious royalty fees, intergroup loans, management fees and intragroup pricing of goods and services. For example, in intragroup loan agreements the subsidiary company making the interest payments receives tax relief for servicing its debt and is thus able to reduce its taxable profits. At the same time, another member of the same group of companies located in a low-tax jurisdiction receives the income. This income, depending on the local tax laws, is either subject to low or no tax. In the transaction described above, no cash actually leaves, but the group of companies is able to reduce its total tax bill. The leaked documents show that the profits transferred to Luxembourg were taxed at less than 1%.



Luxembourg: Home from home for tax avoiders

In 2013, an inquiry by the House of Commons Public Accounts Committee (PAC) showed that the Big Four accountancy firms are at the heart of a global tax avoidance industry. A whistleblower informed the PAC that PwC would sell a tax avoidance scheme which had only a 25 per cent chance of withstanding a legal challenge. As Labour MP and PAC chairman Margaret Hodge put it: 'You are offering schemes to your clients where you have judged there is a 75 per cent risk of it then being deemed unlawful'. Partners of KPMG, Deloitte and Ernst & Young admitted to 'selling schemes they consider only have a 50 per cent chance of being upheld in court'. Rather than expressing any remorse, the firms defended their practices through obfuscation and denial. The firms denied that they mass marketed tax avoidance schemes. Such pretences are laid bare by the Luxembourg leaks, which showed tax avoidance schemes on PwC headed paper and signed by the firm's partners. So in December 2014 the PAC recalled PwC.

At the reconvened hearing of PAC, PwC deployed its usual strategy of denial. PwC is a global brand. It has a global board and CEO. It has a global logo, headed paper and website. In tendering for business it frequently describes itself as a 'global' organisation. Its website proclaims that it is "One firm - a powerhouse of a commercial enterprise that does the right thing for our clients, our people and our communities." Under scrutiny from the PAC, all such claims dissolved. The firm's partner said that PwC was a loose collection of national firms. Each firm is apparently independent and able to refer or pass business to each other and even share the knowledge base, but they are local rather than global. As many UK based companies had used the avoidance schemes, it would be reasonable to assume that there was co-ordination between the UK and Luxembourg parts of the firms, but the PwC partner was not too forthcoming on that. All too often, he took refuge in 'duty of confidentiality' to parry searching questions. The PAC hearing also focused on the tax affairs of one of its clients - Shire, a major pharmaceutical company with operations in the US, UK and Ireland. The company located its treasury function in a Luxembourg subsidiary. The Luxembourg company did not produce anything tangible, but over a five year period lent around $10bn (£6.4bn), equivalent to two year's sales revenues of the entire group, to other members of the group. It booked just under $2bn in interest income in Luxembourg and paid tax of about $2 million. The Luxembourg office of Shire had just two middle-ranking employees and incurred annual employment costs of just $135,000 (£106,000) a year.

Luxembourg leaks

The Luxembourg leaks make a mockery of the corporate claims of social responsibility. Various corporate websites disarm citizens with claims of ethical and responsible citizenship, but none provide any details about their tax avoidance schemes or corporate tax paid in each country of their operations. The 28,000 pages of leaked evidence does not contain even one instance where PwC or any company considered the impact of their practices on ordinary people who will either have to forego hard won social rights or pay even more in taxes to sustain a crumbling social infrastructure.

The leaked documents have not prompted the UK government to investigate any of the companies or accountancy firms peddling tax avoidance schemes. No accountancy firm has ever been investigated or prosecuted for peddling tax avoidance schemes, even after they have been declared unlawful by the courts. No firm has been disciplined by any professional body either. The current chairman of HMRC is a former KPMG partner and has maintained public silence. The leaks also raise serious questions about the tone at the top of the European Union. The tax avoidance deals were secretly negotiated between corporations, accountancy firms and the government of Luxembourg. They were approved by a government led by Prime Minister Jean-Claude Juncker, who was also its Finance Minister. The same Mr. Juncker is now President of the European Commission, charged with tackling organised tax avoidance. He is unfit to lead the charge for protection of tax revenues, but has clung on to office. Accountancy firms are in the frontline of the war against the state and the people. They receive fees from corporations for starving the state of tax revenues. They also advise the state on privatisation of publicly-owned enterprises, Private Finance Initiative (PFI) and debt finance. Such processes enrich a few, but also force the state to dance to the tunes of markets and demands of creditors who increasingly dictate policies. Through PFI, the state ends up guaranteeing profits for corporations, whilst its ability to meet its obligations is constrained by erosion of tax revenues. The squeezed state has been forced to prioritise the interests of finance and is now implementing the longest ever austerity programme. We are witnessing a revolution in the relationship between capitalism and democracy.

Osborne's budget deficit: mind the 'Google' gap

Tory Chancellor Osborne announced a Diverted Profits Tax, popularly known as the Google Tax. He thinks it would raise £1 billion over five years, assuming that companies have not already moved to negate it. This is poorly thought out and does not amount to a reform of the corporate tax system.

In February 2013, the government said that it will deny public contracts to those involved in tax avoidance. So far not a single organisation so involved has been denied public contracts.
The amount of tax revenue lost due to corporate tax avoidance is not known. HMRC has published figures for Tax Gap, which consists of all tax arrears, avoidance and evasion. It now admits to £35 billion per annum, but does not provide details of its model for estimating the figure. Tax Justice Network provide an alternative model, developed by Richard Murphy. He estimates a tax gap of about £120 billion
PS.