Globalization and Tax Justice

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How can we make globalization and tax justice compatible?

One of the most pressing policy questions of our time

- Clear by now that globalization is making redistribution harder
- Policy response so far: protectionism and/or let's all become tax havens (Brexit, Trump, race to bottom)
- Another route is possible, but it requires: (i) a good understanding of the issues, (ii) creative policies

Why globalization and tax justice are conflicting

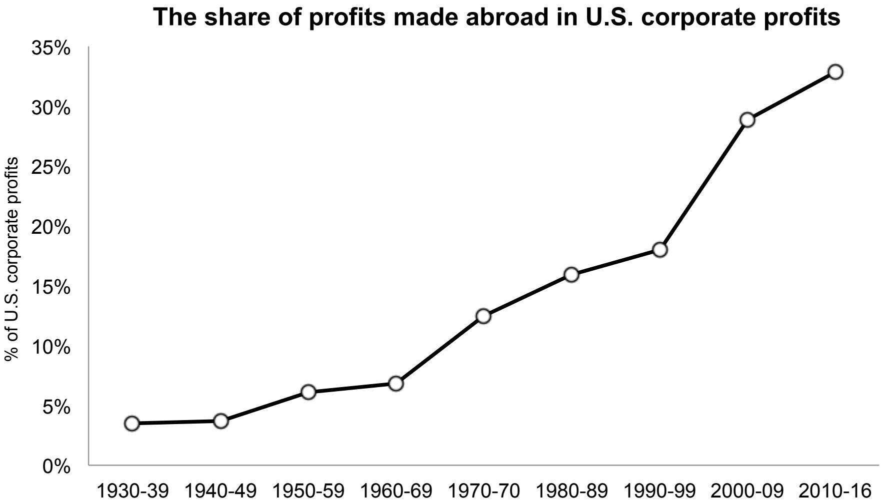
Tax havens severely affect national tax policies:

- Multinationals' artificial profit-shifting
- Rising personal tax avoidance and evasion
- Internalizing this, gov't cut capital taxes & top rates
- Cuts need to be offset by $\uparrow$ taxes elsewhere / less spending

$\rightarrow$ Does globalization have a future if it means ever lower taxes for the rich, and higher for the rest of us?

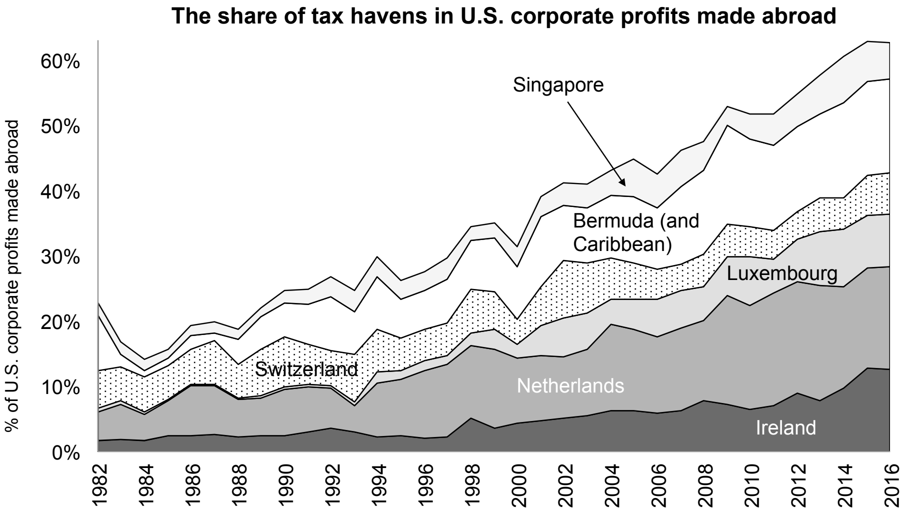
Multinationals' Profit-Shifting to Tax Havens

A growing fraction of global profits are made abroad



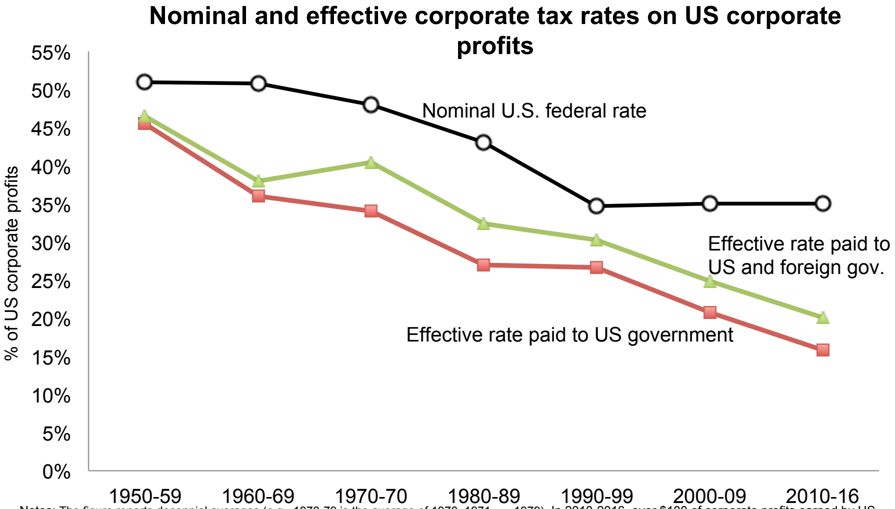
Notes: The figure reports decennial averages (e.g., 1970-79 is the average of 1970, 1971, ..., 1979). Foreign profits include dividends on foreign portfolio equities and income on US direct investment abroad (distributed and retained). Profits are net of interest payments, gross of US but net of foreign corporate income taxes. Source: author's computations using NIPA data, see Online Appendix.

63% of the foreign profits of US multinationals are now made in havens



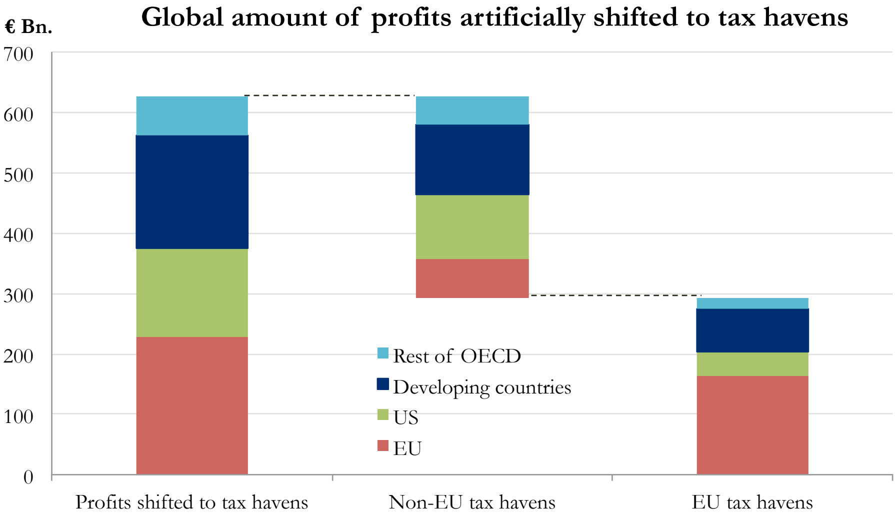
Notes: This figure charts the share of income on U.S. direct investment abroad made in the main tax havens. In 2016, total income on U.S. DI abroad was about $450bn. 16% came from the Netherlands, 8% from Luxembourg, etc. Source: author's computations using balance of payments data, see Online Appendix.

The effective rate paid by US corporations has been reduced by 1/3 since late 1990s



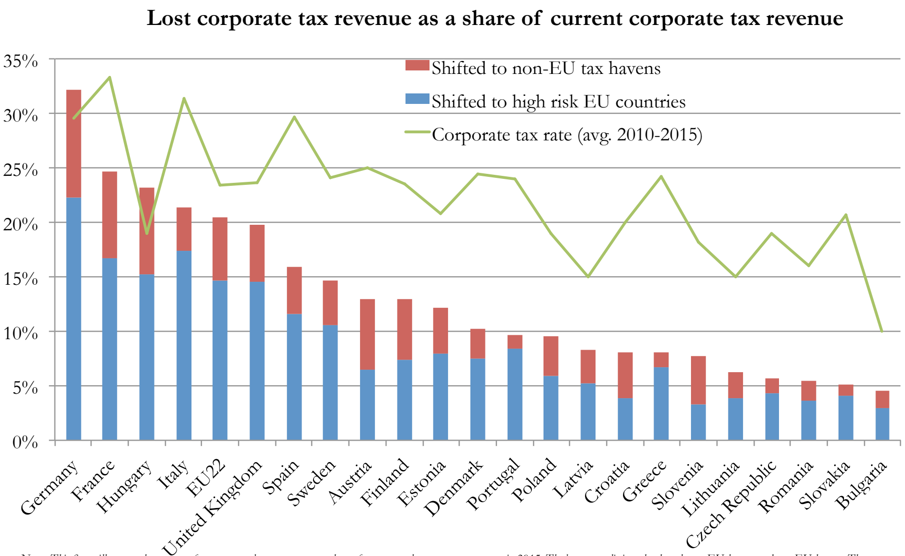
Notes: The figure reports decennial averages (e.g., 1970-79 is the average of 1970, 1971, ..., 1979). In 2010-2016, over $100 of corporate profits earned by US residents, on average $16 is paid in corporate taxes to the U.S. government (federal and States) and $4 to foreign governments. Source: author's computations using NIPA data, see Online Appendix.

Globally, 40% of multinationals' profits are artificially shifted to tax havens



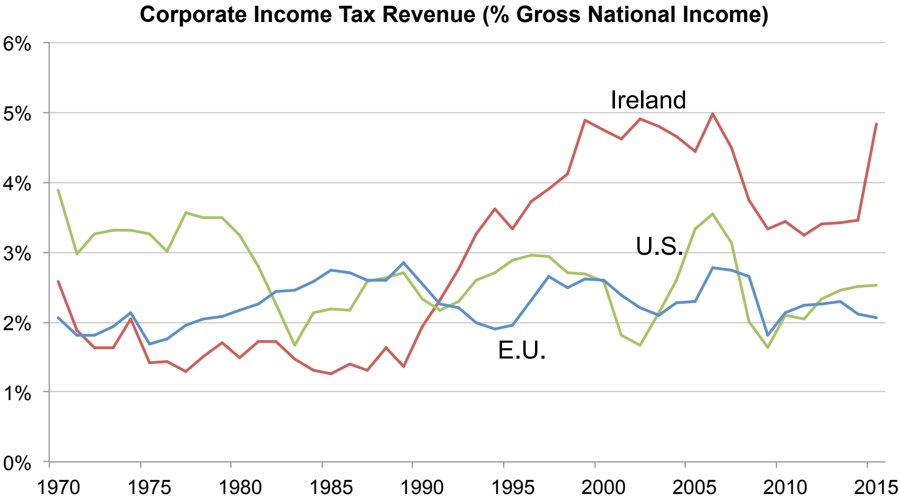
Note: This figure illustrates the amount of tax base wrongfully allocated to tax havens in 2015, as well as the regions from which it originates. The total profits shifted to tax havens is estimated at 627 billion Euros. The size of mis-allocated tax base is equal to the estimated "Excess Profits" of the havens. The profts are allocated to the countries of origin, proportionally to the sum of high-risk service imports and FDI interest payments by partner countries. Foreign income is defined as income made by non-tax havens on investments abroad. The foreign income in 2015 was 1.4 trillion Euros.

The EU loses 20% of its corporate tax revenue due to tax havens



Note: This figure illustrates the amount of tax revenue lost per country as share of current total corporate tax revenue in 2015. The bars are split into the share lost to EU-havens and non-EU havens. The green line shows the top statutory tax rates of the countries. The tax losses are allocated using the share of high risk imports and interest paid to tax havens (Our benchmark scenario).

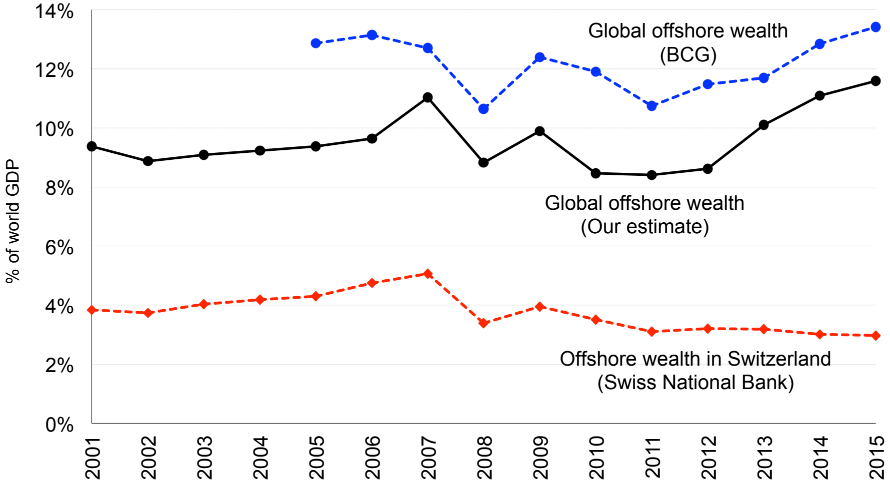
The winners: tax havens



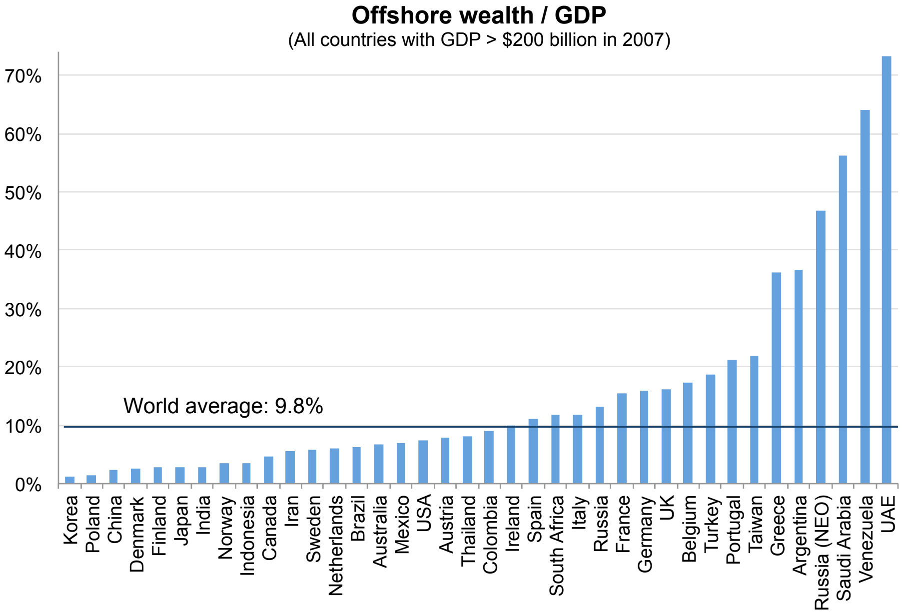
Note: EU is the average of France, Germany, U.K., and Italy.

Offshore Wealth

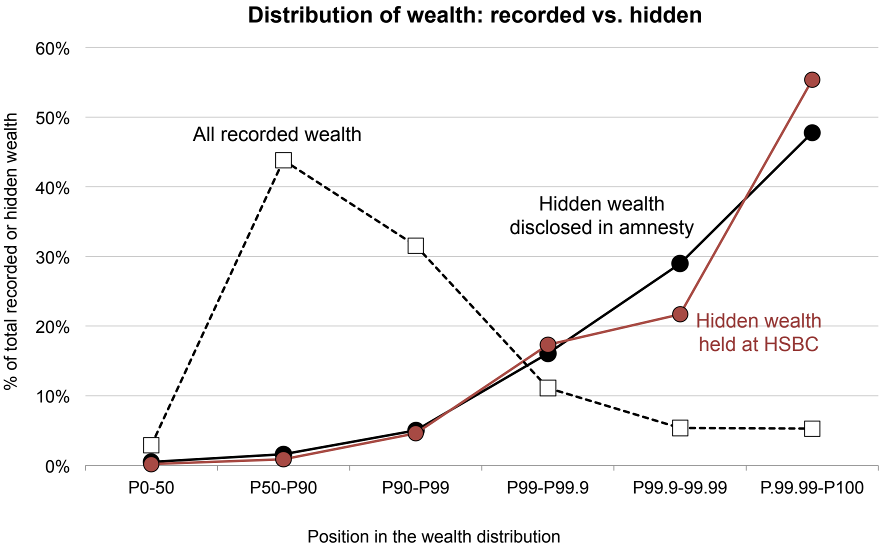
A high and growing amount of personal wealth is held in tax havens



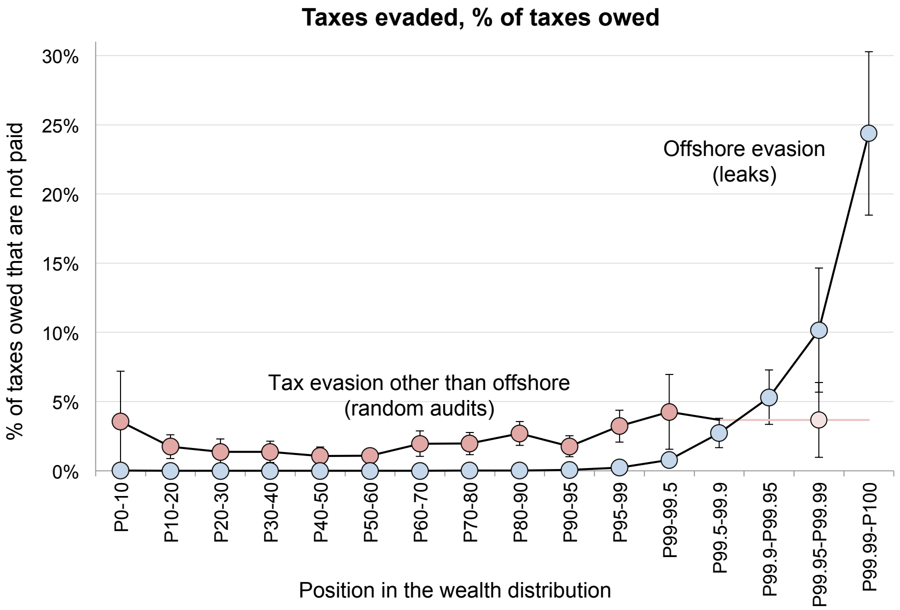
From some countries, offshore wealth is as high as 50% of GDP



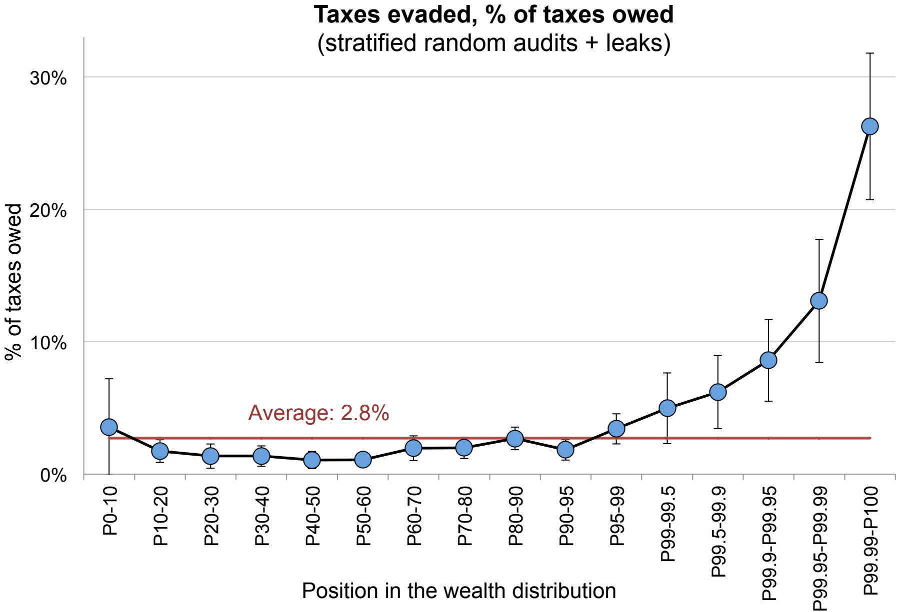
Hidden wealth is extremely concentrated



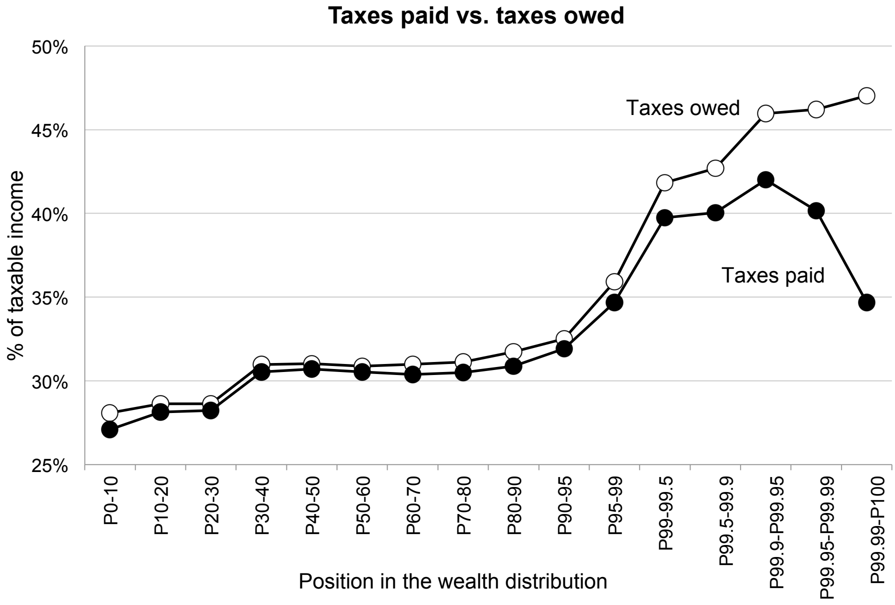
Combining offshore tax evasion with other forms of tax evasion



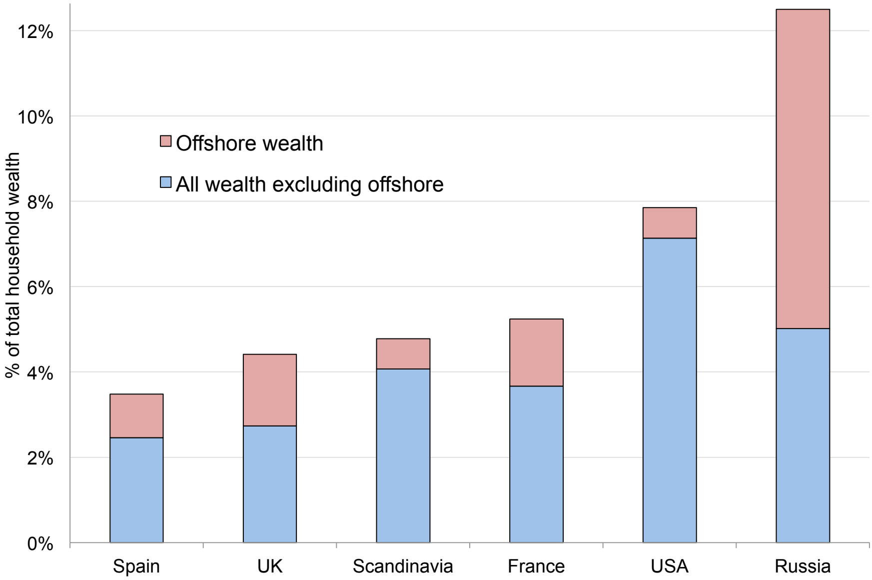
Tax evasion is widespread among the very wealthy



Tax evasion makes the tax system regressive at the top



Because of offshore wealth, we significantly under-estimate inequality



The Solutions

Despite recent policy initiatives, much remains to be done to fight tax evasion

Automatic exchange of bank info is becoming global standard: big progress.

Three obstacles:

- Incentives of offshore bankers
- Financial opacity
- Incentives of tax havens

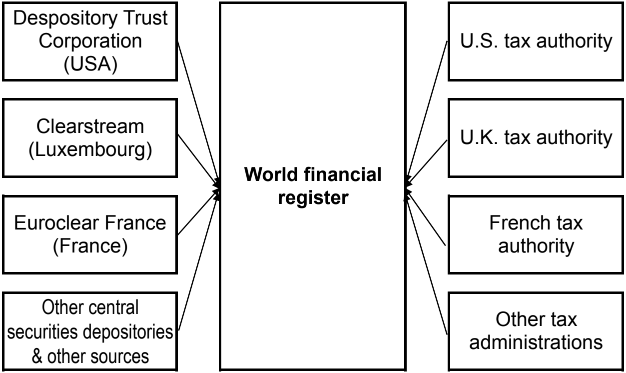
$$\Downarrow$$

What is missing: well defined sanctions and a world financial registry

We need a world financial register to fight financial opacity

The case for a world financial register

The companies Clearstream, Euroclear, etc. feed the world financial register. Tax authorities can verify that tax-payers indeed declare all the financial securities included in the register



Reforming the corporate tax

Formula apportionment

Works reasonably well for US States

Based on final sales to remove incentives to move real activity

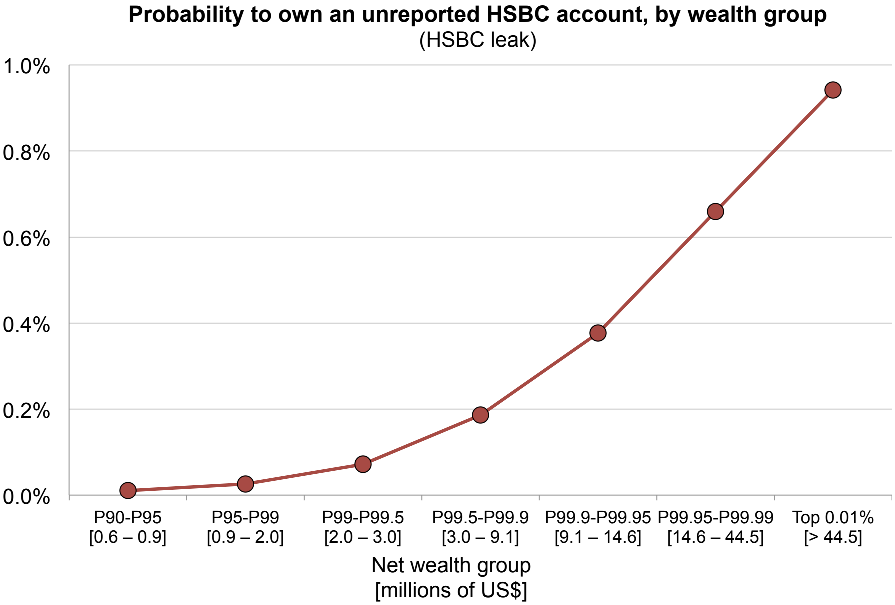
It's the best way to levy taxes efficiently and fairly

Can be done unilaterally

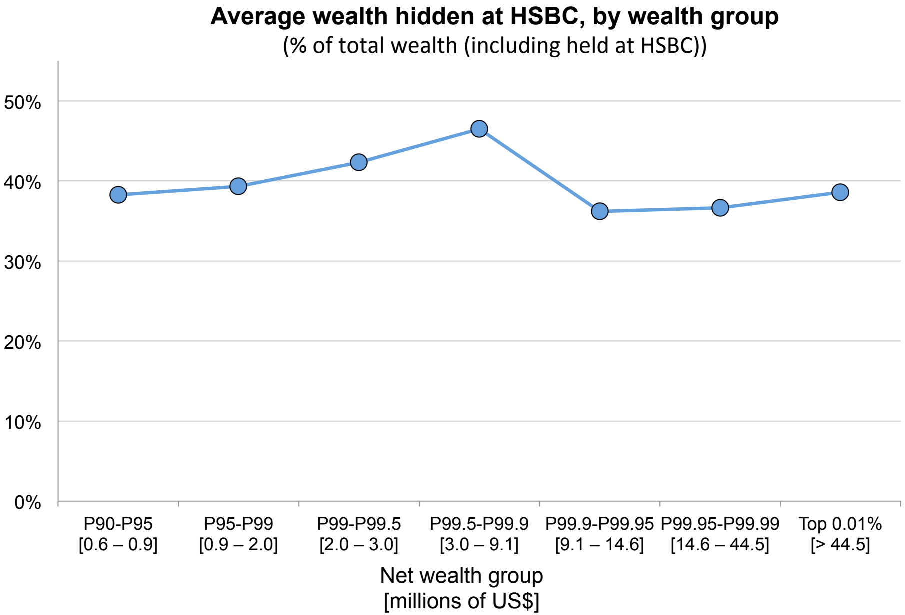
But best done multilaterally as part of free trade agreements

Supplementary Slides

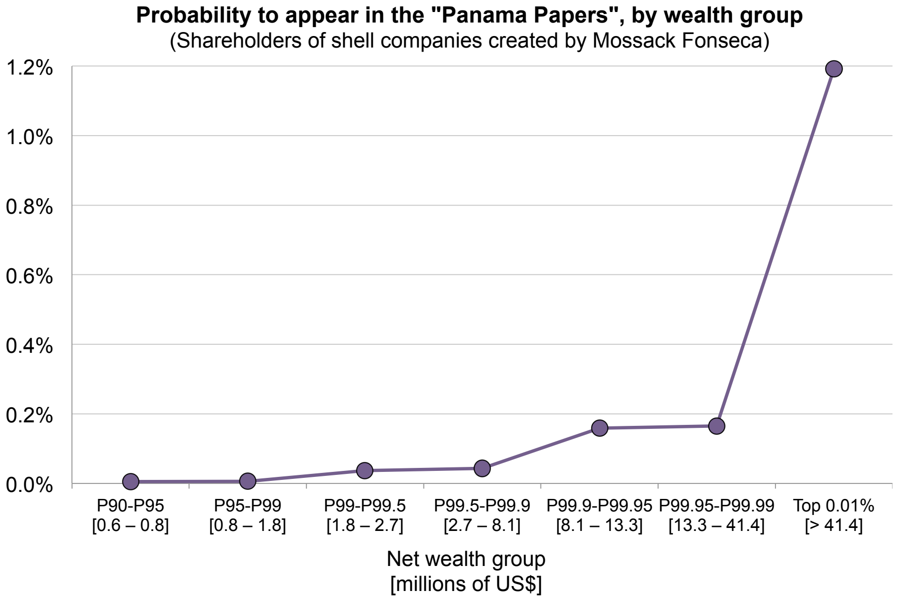
The proba to have an unreported HSBC account rises sharply within the top 1%



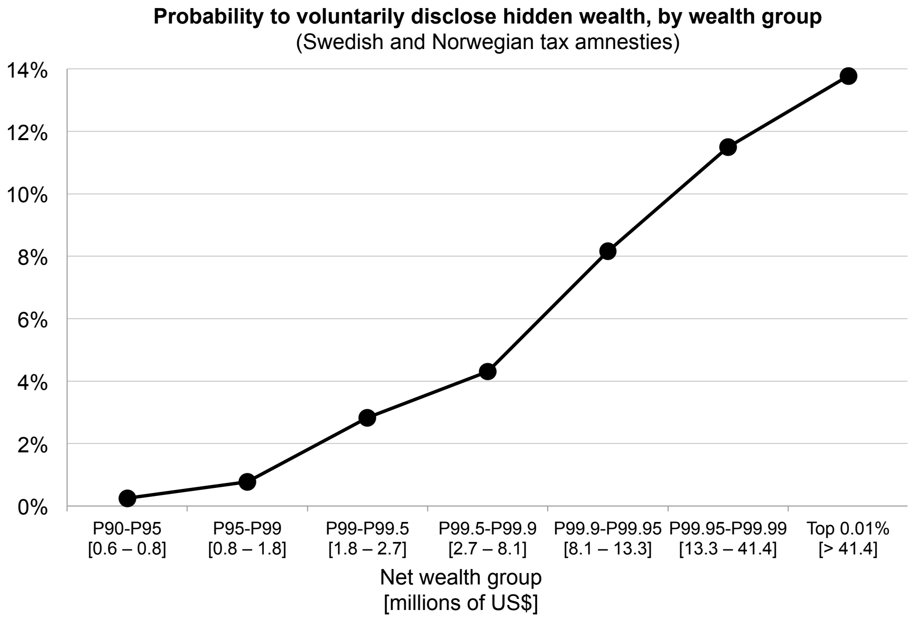
HSBC evaders hide close to half of their wealth at HSBC



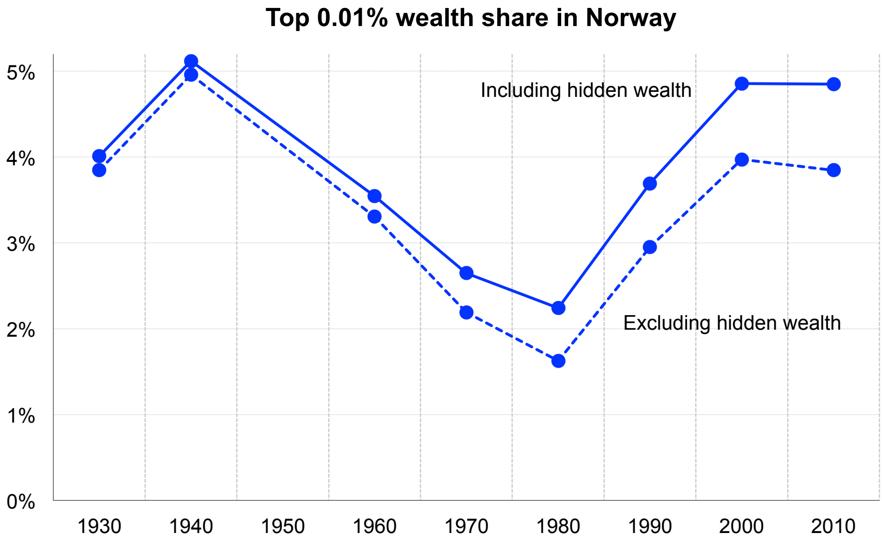
The Panama Papers confirm the sharp gradient in use of tax havens by wealth



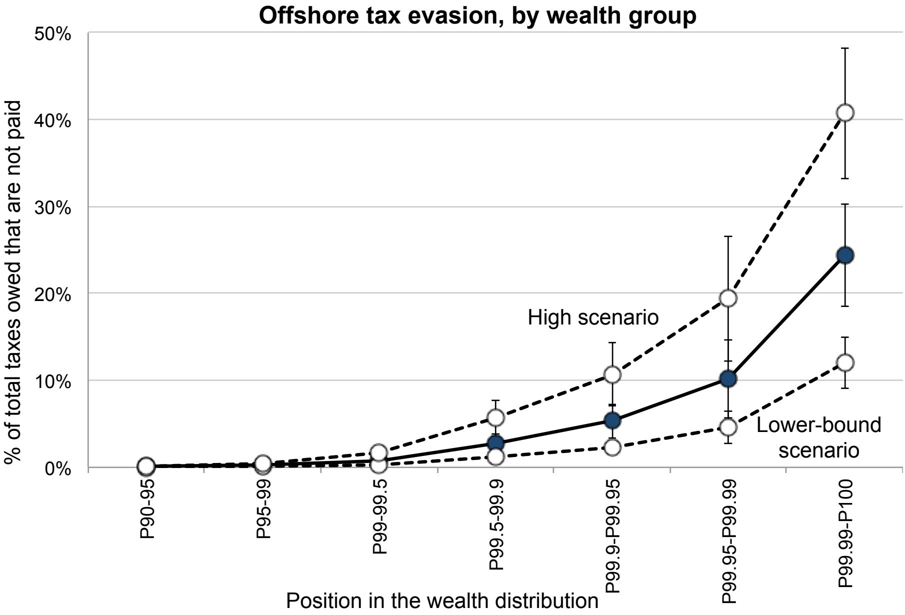
Amnesty data show widespread evasion at the top



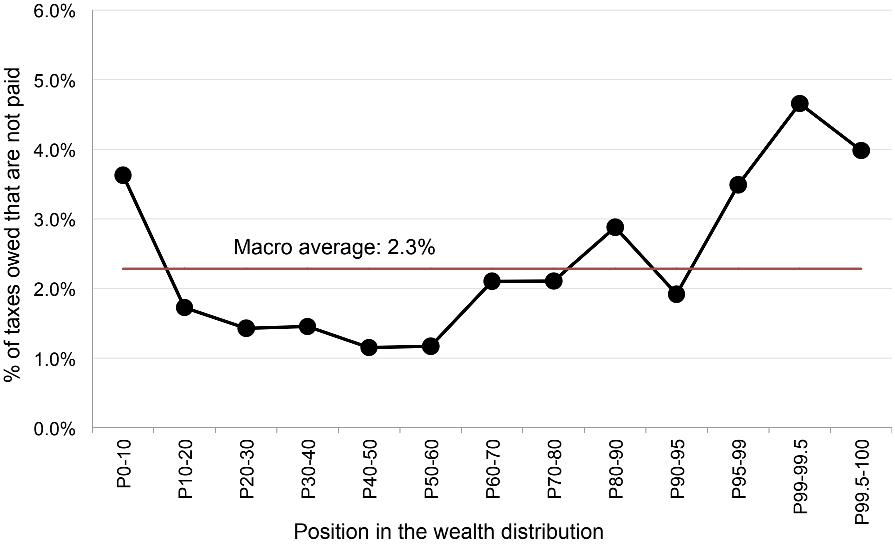
Even in countries with low total evasion, including hidden wealth ↑ inequality a lot



Tax evasion on hidden wealth

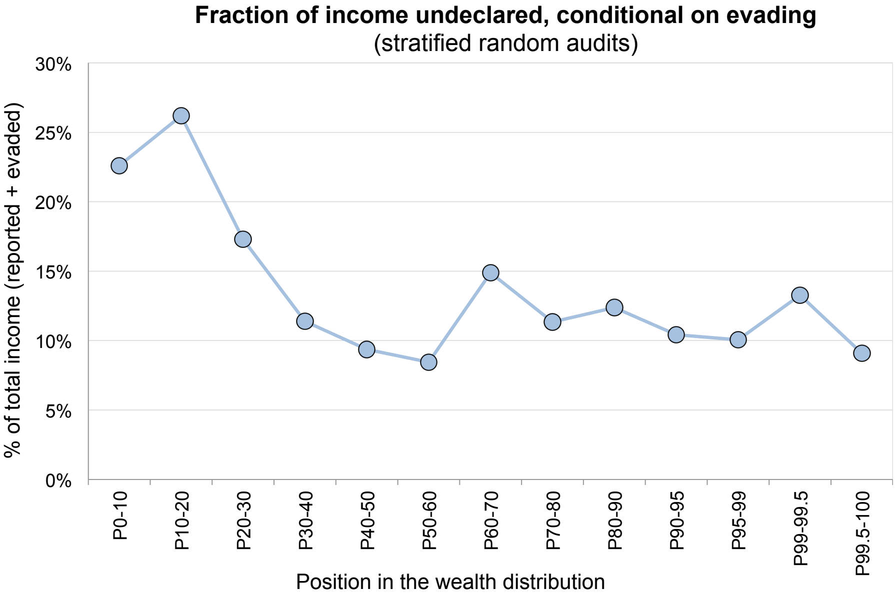


Tax evasion detected in random audits

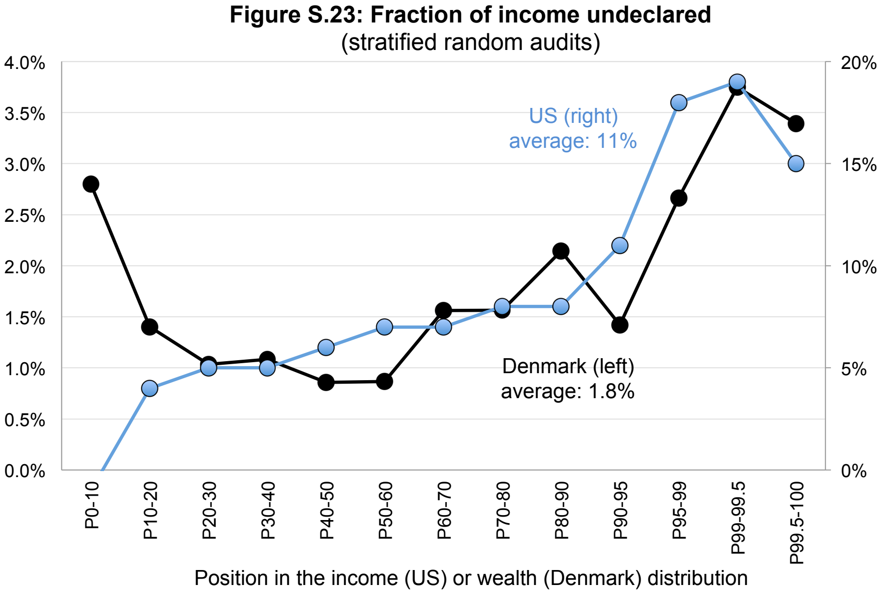


Random audits detect a lot of errors on tax returns

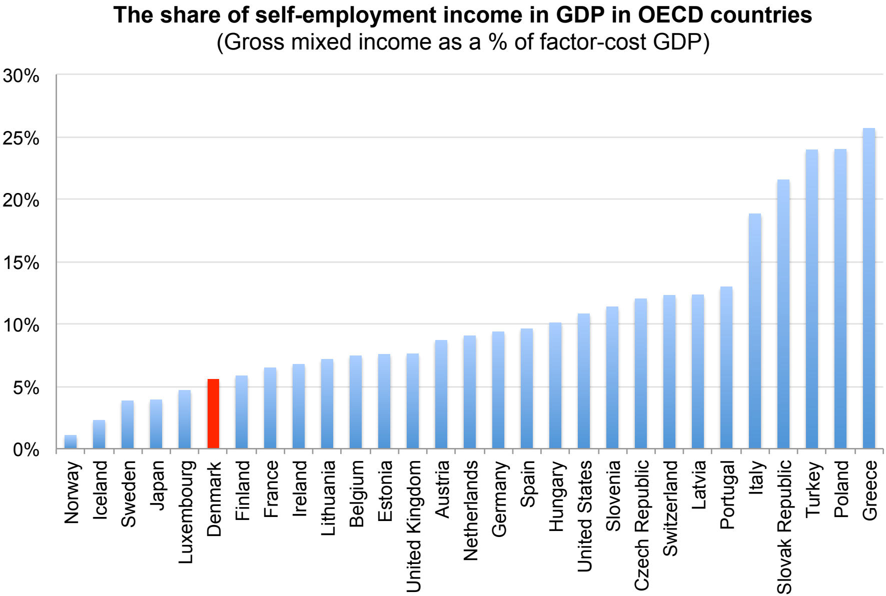
But random audits fail to capture sophisticated evasion at the top



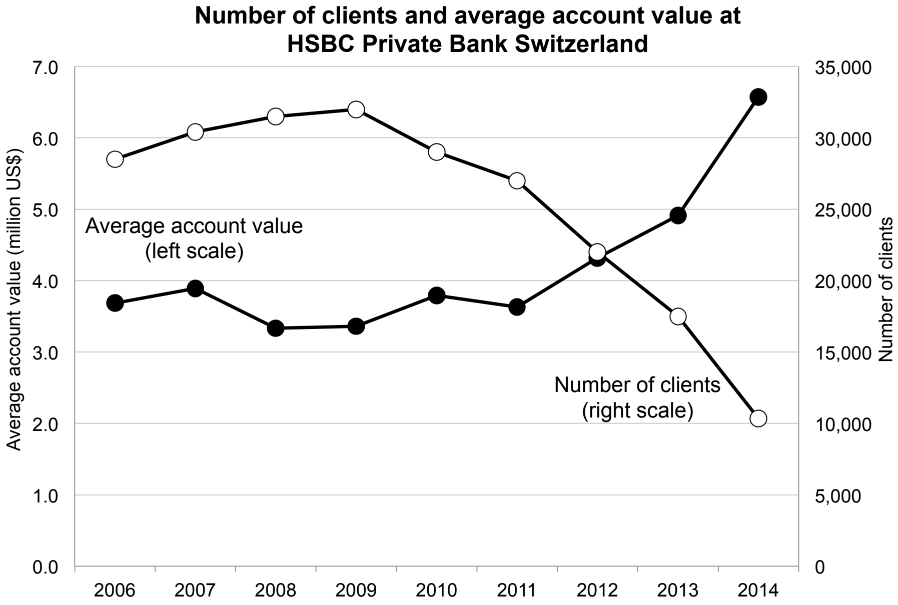
Tax evasion in random audits: US. vs. Denmark



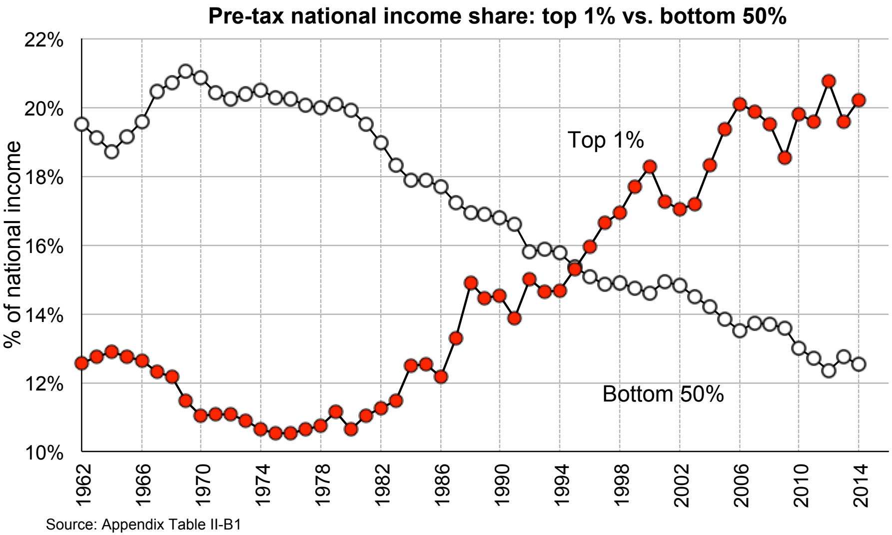
Why is detected evasion higher in US? DCE multiplier + self-employment



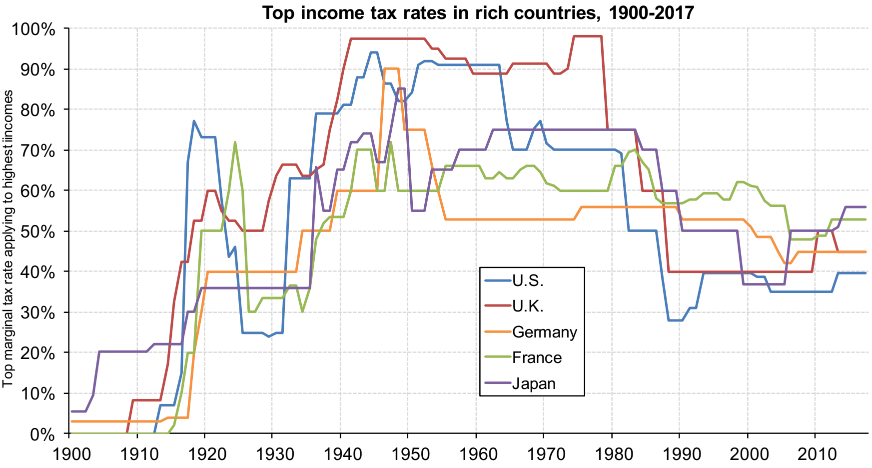
Stronger enforcement → fewer, wealthier clients



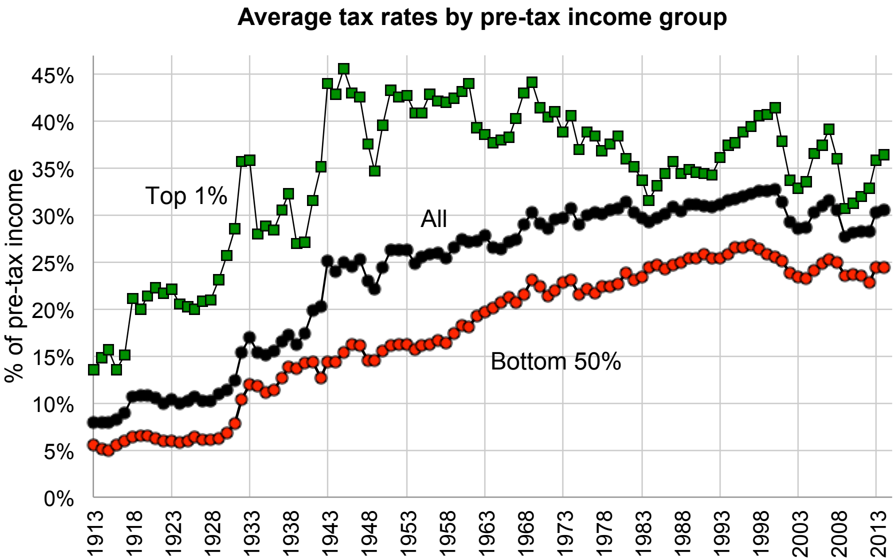
Income inequality in the United States



Changes in Tax Progressivity

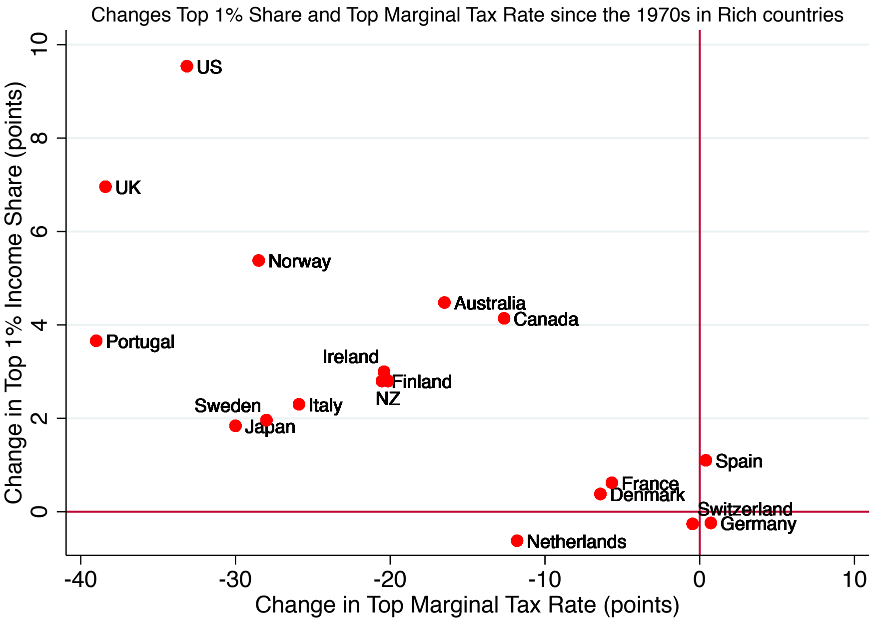


Tax progressivity in the United States



Source: Appendix Table II-G1.

Inequality rose more where top marginal tax rates were cut more



No growth for the U.S. bottom 50% since 1980