Looking for Loot in Other People's Pockets

By Richard W. Rahn

INTERNATIONAL BUREAUCRATS WANT THEIR 'FAIR SHARE' OF CORPORATE TAXES

Well brought-up individuals are taught not to take things from other people's pockets: "Thou shall not steal." There are those who never learned the lesson — criminals, and many in the global political class. The latest targets of the global looters are multinational corporations. As reported in Britain's The Guardian newspaper: "The U.N. has urged governments to stem the flow of funds to tax havens after companies funneled $221 billion into countries with low tax rates last year." The article goes on to say, "[U.N. Conference on Trade and Development] said the growing practice among multinational corporations of diverting profits to low tax jurisdictions denied vital investment funds to developing world countries."

During the last few years, there has been an effort by high-tax countries (many of which are rich) to establish global minimum corporate taxes and for international tax bureaucrats to determine how taxes on a company should be allocated among the jurisdictions in which it operates. Even though the effort is cloaked as an issue of "tax fairness," it is really an effort of more powerful countries and their political classes to take away more from those who earned it and spend it on themselves and their friends.

This effort to tax companies more raises a series of questions. First, is it wrong for corporate officers to try legally to minimize their company's tax bills? No, in fact, corporate officers have a fiduciary responsibility to their stockholders, employees and even their customers to minimize costs, including taxes.

Second, should corporations be taxed at all? Given that corporations are merely a legal convenience and necessity for big companies to acquire and properly allocate large amounts of capital, they are not people, and only people can pay taxes. The corporate tax is paid by their customers in terms of higher prices, their workers in terms of lower wages, and their stockholders in terms of lower dividends and capital gains. If there were no corporate taxes, their customers would have more money to spend on other things, which would likely be subject to some form of sales tax, and their workers and stockholders would have higher incomes which, in most places, would be subject to an income tax. To the economically ignorant (including the media and many politicians), it sounds like a free lunch to tax corporations. But, in reality, if there were no corporate taxes, there would be better capital allocation and hence, higher growth, more jobs and, ultimately, more tax revenue for governments at lower rates.

Third, is it possible to "fairly" allocate corporate tax profits when the corporations operate in many jurisdictions? The Apple iPhone contains parts and software from more than 30 countries, and the product is sold in nearly 100 countries. While most of them are assembled in China, the iPhone was mainly designed and conceived of in the United States, where much of its intellectual property resides. Nestle, the world's largest food company with more than 2,000 brands, has plants in something like 86 countries and sells some of its products in almost every country in the world, but its headquarters is legally and operationally located in Switzerland, where it was founded 150 years ago. There are software companies with little physical presence anywhere in the world but employ software engineers and programmers in many countries and sell their products almost everywhere over the Internet. It is not possible to determine how much profit for the above (and millions of other enterprises) can be attributed to any one tax jurisdiction.

Are multinational corporations depriving developing countries of needed investment capital? As the distinguished, late development economist Lord P.T. Bauer correctly observed, those countries with the right policies and institutions will attract all of the capital they can productively utilize, but those with the wrong policies and institutions will waste whatever capital that is invested or given to them. Businesses invest where their money is well treated. Places that used to be poor but now are prosperous, such as Hong Kong, Taiwan, Singapore, Estonia and Chile have attracted huge amounts of private capital because they possess the rule of law, little corruption and sensible economic policies, including the protection of private property. Studies have shown that multinational corporations have been the best engines of economic development, not only because of their capital investments but, more importantly, for the jobs they create and the management, organizational skills, technologies and training they bring to developing countries.

It is no surprise that the efforts to increase and artificially allocate corporate profits are led by politicians, lawyers, government bureaucrats and officials of nongovernmental organizations, who have little or no experience in real job and wealth creation. Many have lavish expense accounts, facilities and great job security, and those in the international organizations have managed to obtain income tax exemptions for themselves.

The corporate income tax is a highly destructive tax because it misallocates capital, hides the true cost of government, and cannot possibly be "fairly" allocated across tax jurisdictions. Such efforts will only lead to more corruption and slower global growth. The correct answer to "the problem" of corporate income shifting is to eliminate the tax. No tax, no problem.

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