Playground Politics: Are Multinationals really the new bullies of the global sandpit?

Reading much of the local and global press at the moment you would think multinationals are the new bullies in the global schoolyard. They are portrayed as stealing the lunch money from powerless Governments and hogging all of the cool toys in the sandpit. They stand accused of treating the school rules that the rest of us play by with contempt and disdain as they refuse to pay “their fair share of tax”.

In reality, we know that the vast majority of multinationals are good corporate taxpayers, however tax authorities are responding to the tax positions taken by a visible few by beefing up the rules. But the question we should be asking is whether the new rules are really solving the problem, and what is the cost of doing so?

In the post-GFC era, tax authorities have become increasingly focused on ensuring they secure and then defend their share of the global tax pie. This has resulted the explosion of legislation aimed at limiting opportunities for multinationals to move profits between jurisdictions, or exploiting tax loopholes for double-deductions and non-taxation of income. Think of the OECD Base Erosion and Profit Shifting (BEPS) working groups, Multinational Anti-Avoidance Law (MAAL), diverted profits tax, country-by-country reporting, etc. The paperwork required to keep all these authorities happy is becoming a compliance beast!

Tax authorities arguably need the data collected as part of documentation and disclosures to appropriately target resources towards taxpayers with a higher risk of being non-compliant, however for the majority of multinationals they face the burden of a significant increase in compliance costs without them doing anything ‘mischiefous’. Tax authorities are about to have a whole lot more data to digest. Let’s hope it’s used productively.

Perhaps even more concerning, is that given the varied pace of adoption and the disparity of the rules between jurisdictions, there is growing probability for multinationals of double taxation. This risk was highlighted early on when the US opted out of participating in BEPS.

Change (and positive progress) may be on the horizon however with the newly legislated tax changes in the US. Specifically, the lack of US taxation of offshore profits until they were repatriated to the US has been one of the key drivers behind some of the more contentious tax planning undertaken by multinationals. With this driver changing due to a reduction in the tax rate applying to repatriated profits, the motivation for aggressive tax planning is weakening.
At the same time, New Zealand is pushing towards the front of the pack in terms of adopting many of the changes proposed by the OECD BEPS working groups. Draft legislation was released in December 2017 is currently under consultation, with the rules expected to apply from 1 July 2018 for June balance dates. The majority of the changes align with those in the OECD papers, the notable exception being New Zealand’s proposals for interest rates on related party funding. In this regard, New Zealand is heading off on a tangent with its proposal to generally cap interest deductions to those based on the interest rates available to the global parent. This again highlights the potential for double-taxation for multinationals as a result of the explosion of rules in the transfer pricing sphere.

What does all of this mean? With the US removing one of the key drivers underpinning the more aggressive tax structures, and a significant tightening in tax rules globally, we believe that we are really going to see a step change in the taxation of multinationals. But what is the cost? There are already significantly and materially increased tax compliance and tax audit costs for all multinational taxpayers, and a very real risk of double taxation across multiple fronts. So rather than simply giving multinationals a “bit of a telling off” Governments seem intent on placing all multinationals in detention with a pile of extra homework to do, begging the question as to who the real bullies are.

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