Doing Business should stop promoting tax competition

By José Antonio Ocampo and Edmund Fitzgerald

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The World Bank Group has just released *Doing Business 2017: Equal Opportunity for All*, the latest version of its flagship report. According to the Bank, the annual report is one of the world's most influential policy publications, as it encourages countries to reduce the regulatory burden on the private sector. But there is a serious flaw in the report's formula: the way it treats corporate taxation.

Doing Business reports rate 11 areas of business regulation in 190 countries, using data on compliance burdens collected by PricewaterhouseCoopers (PwC). The Bank then formulates an overall score that supposedly reflects the ease of conducting commercial activities, and ranks countries according to that score. The lower the regulatory burden on businesses, the higher a country ranks.

The problem is that "regulatory burden," according to *Doing Business*, includes the collection of taxes that are necessary to fund public infrastructure and basic social services – both of which are critical to enhance growth and employment. Even the report recognizes that, for most economies, taxes are the main source of the government revenues needed to fund "projects related to health care, education, public transport, and unemployment benefits, among others."

Beyond promoting budget-straining tax competition among countries, *Doing Business* exaggerates the tax burden on companies. For one thing, it considers all the kinds of taxes firms might pay – not just corporate income tax.

Specifically, the report's estimates for "total tax rate as a proportion of profits" include taxes for employees' health insurance and pensions; property and property transfers; dividends, capital gains, and financial transactions; and public services like waste collection and infrastructure. Those are taxes that should be categorized as social contributions or service charges.

Augmenting estimates further, *Doing Business* does not measure only expected tax payments. It considers the cost (in staff time) of activities like filing returns, making claims, and, beginning this year, post-filing processes, to be part of the tax burden on businesses.

In reality, corporate-tax payments, as a share of gross profits, are quite low. According to *Doing Business*' own data, the world average amounts to just 16%, with the European Union coming in at 13%, the United States at 19%, and Latin America, Asia, and Africa at 16%.

But even those figures are probably too high, because of another reality that *Doing Business* overlooks: tax avoidance and evasion. Whatever a country's official corporate-tax rate might be, the reality is that few companies actually pay the full amount.

Indeed, while a small manufacturer for the domestic market might adhere to the official rate, the large domestic and multinational firms that account for most production and exports worldwide are well-positioned to take advantage of tax avoidance schemes. And they typically do not hesitate to do so.

The OECD has estimated that tax avoidance by multinationals averages $200 billion per year – a figure that far exceeds total international development assistance. PwC itself is in a good position to enlighten the Bank on this issue. As the famous "LuxLeaks" of 2014 revealed, from 2002 to 2010, the firm assisted its multinational clients in obtaining at least 548 tax rulings in Luxembourg, enabling them to avoid corporate income tax globally. All of this

places smaller local firms at a substantial competitive disadvantage.

This may sound like an argument for overhauling *Doing Business*' "paying taxes" indicator. But what is really needed is for *Doing Business* to drop that indicator altogether, because the assumption underpinning it – that low corporate taxation promotes growth – does not withstand scrutiny. Research conducted by the International Monetary Fund and others indicates that tax competition does not promote productive investment worldwide.

In assuming the opposite, *Doing Business* becomes riddled with contradictions. It recognizes that "higher income inequality is associated with a smaller tax base and therefore lower tax collection." Yet it advocates giving corporations a respite from taxes, thereby undermining tax collection in a way that, by potentially promoting inequality, could intensify that impact.

The report praises countries like the Dominican Republic, Guatemala, Peru, Portugal, Senegal, Tajikistan, and Uzbekistan for reducing their corporate-tax rates, while scolding Greece for increasing it – ignoring the need for government revenues and public investment in those countries. It also supports reduced labor protection and overlooks environmental externalities – stances that controvert the Bank's own commitments.

This year's *Doing Business* report made some positive changes, adding indicators for women in business and public procurement. But, when it comes to the paying taxes indicator, the report has things all wrong. Indeed, it runs counter to the global consensus on the need for effective international cooperation to ensure equitable collection of tax revenues, including measures to limit tax avoidance by multinationals and other private firms.

A race to the bottom in corporate taxation will only hurt poor people and poor countries. If *Doing Business* is to live up to its own slogan, "equal opportunity for all," it should abandon the tax indicator altogether.

José Antonio Ocampo, a professor at Columbia University and Chair of the UN Economic and Social Council's Committee for Development Policy, was Minister of Finance of Colombia and United Nations Under-Secretary-General for Economic and Social Affairs. Edmund Fitzgerald is Emeritus Professor at Oxford University and a member of the Independent Commission for the Reform of International Corporate Taxation.