Christian Aid opening statement to the Joint Committee on Finance, Public Expenditure and Reform, and Taoiseach

3 May 2018

Good morning, my name is Sorley McCaughey, and I am the head of Advocacy and Policy at Christian Aid Ireland. I am here today with Mike Lewis, who has been working with us recently on a consultancy basis, and was the principle author of the recent Christian Aid report on the impact of Ireland's tax policy on developing countries entitled Not Without Cost.

Christian Aid has been working on the issue of tax justice since 2007, when we became the first development NGO to identify tax as a development issue, and indeed as a justice issue. As such we are principally concerned with the erosion of the tax base in the world's poorest countries. It is estimated by the IMF, that developing countries lose up to 150bn/year to multinational tax avoidance.

We appreciate the opportunity to appear before this Committee today- thank you chair for the invitation.

The countries where we work, and where Irish Aid is spent, are not only amongst the world's most rapidly growing markets for digital services. Due to their lower levels of penetration compared to Europe and North America, they are also now the primary target markets for Facebook, Google and others. Indeed, in many developing countries, social media companies like Facebook have the ambition to *be* the internet.[1]

[1] Providing online access to selected websites through initiatives like Facebook's "Free Basics" – first rolled out in Zambia in July 2014, now covering 42 countries and over 600 million people in Africa, and more across Asia and South America).

Therefore, to the extent that all economic activities increasingly incorporate online activities, what we do now to tax digital economic activities may safeguard or undermine developing countries' tax bases long into the future.

We therefore welcome the ambition in the EU and other fora to explore new solutions for taxing digital economic activity.

However, our research -- including the papers we published last November on the global impact of Ireland's tax system -- suggests that the problems of taxing digital activities in developing countries are wider than the dysfunctions the new EU proposals are designed to address.

The evidence we present today argues that the EU proposals, both interim and final, can only be part of the solution. We want to talk briefly about possible limits to their **TECHNICAL SCOPE**, **PRACTICAL EFFICACY** and **INTERNATIONAL IMPACT**.

- We end by suggesting that there are wider proposals being developed elsewhere, including in the EU but also in the OECD and at the UN, which would provide some more systemic solutions.

TECHNICAL SCOPE

- The EU's "digital economy" proposals are effectively focussed on one part of that economy: providing digital services in a country – like online advertising, software or access to online content -- without having a taxable presence in that country.

- They will not deal (and are not intended to deal) with a much more pervasive area of activity: the way that online or digitally-facilitated sales mean that *non-digital* goods and services can be sold in a particular country, and the sales booked in a low-tax jurisdiction.

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https://www.theguardian.com/world/2016/aug/01/facebook-free-basics-internet-africa-mark-zuckerberg

- The first problem is really a subset of the second one: as our 'Impossible Structures' report showed, whether you're selling subscriptions to the LinkedIn website, or physical Microsoft Mobile phones designed for developing countries[2], in a digitised economy you can sell both through a 'booking centre' in a low-tax jurisdiction, without the need for a taxable, "bricks and mortar" presence in the country where your customers are based. Both online services, and sales of physical goods, can use the famous "Double Irish" and now "Single Malt" structures that we highlighted to shift profits and avoid having a taxable "bricks and mortar" PE in the country where your users or customers are based.

- The EU proposal therefore introduces a narrow solution (introducing the idea of the "**digital permanent establishment**") for taxing profits from sales of digital services, when other goods and services can use many of the same mechanisms to avoid tax, and won't be covered by the Commission's proposals. Indeed the proposals explicitly state that "*the mere sale of goods or services facilitated by using the internet or an electronic network is not regarded as a [taxable] digital service*."[3]

PRACTICAL EFFICACY

- Our November report highlighted how many of the structures used to avoid a taxable presence (PE) where you selling goods and services – which is really the overarching problem we're talking about here -- rely upon the standard terms of double tax treaties governing what constitutes a taxable PE and how profits should be attributed to it.

[2] https://www.christianaid.ie/sites/default/files/2018-02/impossible-structures-tax-report.pdf p.18-25

[3] European Commission, *COM(2018) 147 final. Commission Proposal for a Council Directive laying down rules relating to the taxation of a significant digital presence (SWD(2018)81 final)*, p.8, https://ec.europa.eu/taxation_customs/sites/taxation/files/proposal_significant_digital_presence_21032018_en.pdf

- The Commission's proposals explicitly acknowledge that they can't apply[4] in situations where sales are being booked in a jurisdiction which has a double tax treaty with the country where the users or customers are present. Most of the jurisdictions we're talking about – Ireland, Luxembourg and others – enjoy wide treaty networks, certainly with all other EU member states, and increasingly with developing countries.

- Even if developing countries were to adopt the kinds of solutions described in the EU proposals, they would also come up against this problem.

INTERNATIONAL IMPACT

- The obstacle of double tax treaties highlights the fact that even were the EU proposals to be adopted, and adopted more widely than the EU, they will come up against dysfunctions of wider international tax standards.

- These are being looked at in several different places, including the UN Tax Committee, international bodies like the Independent Commission for the Reform of International Corporate Taxation (ICRICT), and of course the OECD, which although it excludes most developing countries from any real decision making, has nonetheless produced proposals that include useful measures with a fairly wide degree of support from some of the key jurisdictions currently used by Facebook, Google and many, many others to avoid a taxable sales presence around the world.

- We therefore believe that the wider problem we've described above (the avoidance of a taxable presence when making sales of both digital and non-digital goods and services) will ultimately be tackled by fundamental root-and-branch change like unitary taxation systems, properly designed.

[4] This is why the Commission's proposals include an (unenforceable) recommendation for member states to amend their DTAs in line with the proposals – which will also cut across the global treaty reform that has just taken place last year via the OECD's Multilateral Instrument. See C(2018) 1650 final, https://ec.europa.eu/transparency/regdoc/rep/3/2018/EN/C-2018-1650-F1-EN-MAIN-PART-1.PDF

- But we also believe that there are aspects of the OECD's BEPS package that might help in the meantime with this wider problem, and for developing countries it's of concern that a global booking centre like Ireland, despite its vocal support for the OECD as the forum for international tax reform, is still not signed up to implement this package in full. In particular, relevant to the problems we're talking about today:
    - Ireland is still reserving its position on Article 12 of the OECD Multilateral Instrument, which is designed to tackle precisely the avoidance of a taxable presence we've been describing[5]
    - Ireland's transfer pricing rules -- which determine how profits are to be shared between centres of intangible assets or sales booking centres (like Ireland) and places where sales are made – are still on the OECD's 2010 version, and have not implemented the latest OECD recommendations. [6]
- Neither of these moves are panaceas: but they are things that are within Ireland's powers to do right now; are consonant with this government's own commitments and stated preferences to implement the OECD's recommendations; and would go some way to tackling the kinds of wider 'PE avoidance' problems with which the EU's Digital Economy proposals won't and can't deal.

[5] The Finance Department's Technical Note on this reservation, published in July last year, said that it was waiting to see the OECD's final work on attributing profits to PEs before it made a final decision. Now that these proposals have been reviewed by all members of the OECD Inclusive Framework, including Ireland, and published (on 22 March), we would be keen for the government to explain what its position now is, and whether it will now sign up to MLI Article 12.

[6] This was amongst Seamus Coffey's recommendations last September. This year's Budget would be an opportunity to do this.