BETTER POLICIES FOR BETTER LIVES

New CTPA Model of Effective Tax Rates (ETRs) on Investment Inclusive of Tax-Planning

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Presentation topics

- Effective tax rate (ETR) model – standard approach to assess tax distortions to investment.
- Previous and current work on ETRs:
  - *Taxing Profits in a Global Economy, 1991*
  - *Tax Effects on Foreign Direct Investment, 2010*
  - *New Sources of Growth* project, 2012.
- CTPA project to create & maintain a model measuring ETRs on investment:
  - coverage / key features
  - next steps.

Assessing tax distortions to investment

- Effective tax rate (ETR) model to assess tax distortions – associated with Jorgenson (1964), King-Fullerton (1984), Devereux-Griffith (2001).
- Summary ETR measures based on tax laws:
  - statutory CIT rate.
  - tax depreciation, interest deductibility.
  - tax incentives (e.g. investment tax credits).
  - non-resident withholding tax rates.
  - personal shareholder tax rates (interest, gains, dividends) influencing hurdle rates of return.
  - does not use actual taxpayer data (tax returns).

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Previous work

- *Taxing Profits in a Global Economy*, OECD, 1991:
  - first publication to report ETRs on domestic and cross-border investment in and between OECD countries.
  - assumes conventional sources of finance, immediate payout of earnings (ignores MNE tax avoidance strategies to avoid tax).
- *Tax Effects on Foreign Direct Investment*, Tax Policy Study No. 17, OECD, 2010:
  - develops methodology for incorporating cross-border tax planning of MNEs (e.g. offshore finance affiliates)
  - compares ETRs under standard model, and model with tax planning – finds large differences, relevant to tax policy analysis and reform.

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Current work

- *New Sources of Growth (NSG)* project:
  - examines R&D and resulting knowledge-based capital (KBC) as a key source of economic growth.
  - aims to improve understanding of policy challenges.
- Tax component of NSG project:
  - develops a transparent/tractable ETR model to examine tax support for R&D and manufacturing using KBC.
  - identifies common tax-planning strategies used by MNEs to avoid tax on returns on use of KBC.
  - examines behavioural implications of alternative policies for supporting R&D and innovation.
  - identifies areas for further work in 2013-2014.

Creation of a CTPA ETR Model

- Decision taken in 2012 by OECD countries for CTPA Secretariat to create and maintain an ETR model to examine tax distortions to investment.
- Key features
  - analyze domestic and cross-border investment
  - cover tangible and intangible assets
    - machinery and equipment, buildings, land, inventories
    - patented and non-patented knowledge-based capital (KBC)
  - incorporate common cross-border tax planning strategies, new financial (e.g. hybrid) instruments.
  - apply common definitions and assumptions to enable meaningful ETR comparisons across countries.

Creation of a CTPA ETR Model (cont'd)

- Next steps:
  - formation of a sub-group (Canada, US, UK, Germany) to further develop/ implement the ETR model (2013).
  - extend coverage to all OECD countries (2014-15).
  - provide all OECD countries with the model.
  - maintain the model in future years – work with Delegates to update tax parameters.
  - work with other interested countries/ organisations to share analysis, enable additional country comparisons.
  - incorporate analysis in new BEPS (base erosion and profit shifting) project of the CTPA.

Thank you!