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Citation:

Morgan, JA (2017) Taxing the powerful, the rise of populism and the crisis in Europe: the case for the EU Common Consolidated Corporate Tax Base. *International Politics*. pp. 1-19. ISSN 1384-5748
DOI: <https://doi.org/10.1057/s41311-017-0052-x>

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Tackling corporate tax avoidance: The case for the EU Common Consolidated Corporate Tax Base*

Jamie Morgan

Now Jonah's Captain, shipmates, was one whose discernment detects crime in any, but whose cupidity exposes it only in the penniless. In this world shipmates, sin that pays its way can travel freely, and without a passport; whereas Virtue, if a pauper, is stopped at all frontiers. (Melville, 2013: p. 52)

Key words: corporate tax avoidance, CCCTB, unitary taxation, European Commission

Introduction

Concepts of populism define it awkwardly as a form of complex collective simplification of the world in terms of causes, consequences and solutions to problems that are in some sense real but reduced or misrepresented.¹ Populist simplicity is a profound contemporary problem. It is intrinsic to current debates regarding the future of the European Union (EU), as well as the significance of Brexit and the election of Donald Trump (see Morgan, 2017; Fullbrook and Morgan, 2017). Crises of legitimacy are occurring at all scales of government and governance. Corporation tax policy is an important, but often neglected, aspect of contemporary problems of international politics. People tend to be aware that it is an issue of concern, one that provokes strong feelings regarding justice, but the issue is often considered too technical. It typically sits as one aspect of the dark side of globalization as an example of how the world enables corporations to act with impunity. At the same time, few beyond expert activist networks and policy communities are aware that solutions exist and that progress is possible. This is important because tax policy can either be part of problems of legitimacy or part of solutions. It can be centrifugal or centripetal. This is particularly the case for corporation tax.

Corporate tax avoidance by multinationals continues to be a source of public concern (Morgan, 2016b; Morgan and Sun, 2017). Multinationals have proven adept at structuring their organization to pay little or no tax. Every few months the popular press report another scandal involving some of the world's most prominent companies (Apple, Facebook, Microsoft, McDonalds and many others). States have increasingly articulated their opposition to tax avoidance and their commitment to address it via the G7, G20, OECD, EU and UN. Yet tax avoidance has two sides, the activity of firms and the opportunities created or not closed by states. This occurs within a system. In the following paper I set out

* Thanks to Sol Picciotto, David Quentin and Prem Sikka for generous provision of their work. Thanks also to participants at the Global Wealth Chain workshop organized by Leonard Seabrooke and Duncan Wigan and hosted by Ronen Palan at CityPERC (Political Economy Research Centre) City University London, February 2017.

¹ This should not be conflated with dehumanization. Those who are seduced by populism are not idiots, though the collective response may be idiotic. For example, many who voted for Trump were highly reflexive regarding their choices and quite aware of the risks involved. They were not ignorant of who they were voting for though given the lack of policy clarity they were by definition ignorant of precisely what they were voting for.

some of the key aspects of tax avoidance in order to make the point that there are limits to reform within the current system. There is a case for a more transformative approach to the problem of corporate tax avoidance based on unitary taxation by formula apportionment. The European Union (EU) already has a version of unitary taxation that members could adopt: the Common Consolidated Corporate Tax Base (CCCTB). The CCCTB represents an opportunity to address one of the major abuses of our time. It has long run collective benefits. However, the CCCTB is an intervention into an already existing system. Its adoption requires EU members to move beyond current embedded and divisive interests. Moreover, the case for the CCCTB involves more than technical matters, an economic argument and a change in formal rules. It involves a change in what we mean by an economic argument and a change in attitudes to rules. These are ethical or normative issues of fairness. They are intrinsic to issues of legitimacy and so also intrinsic to problems of contemporary international politics. The CCCTB has the potential to be legitimacy enhancing.

The problem of corporate tax avoidance

Strictly speaking there is no such thing as a multinational *corporation* (MNC). They are more accurately multinational enterprises (MNEs). The term MNC conceals a basic distinction between an economic whole and a territorial-legal unit (Picciotto, 2011, 2012). MNEs are typically 'firms'. In public discourse they are referred to by their standard trading name, Barclays or Amazon or Google. We recognize them as unified organizations. We understand they are strategic wholes subject to a directing will. However, they decompose into many subsidiaries, affiliates, and separate corporations located in many jurisdictions. Transactions between entities are intra-firm but inter-corporation. This creates a potential for abuse.

Entities can have separate legal existence. At the same time, one corporation can be the directing influence over another. As a legal person a corporation can own the equity, assets, and debt of other entities. It can own the intellectual property that underpins the business activity of those other entities. There may be good business reasons for an MNE to have multiple locations and thus many entities. However, the capacity to create such entities encourages MNEs to locate them to exploit differences in tax rates, differences in tax law, weaknesses and loopholes in tax treaties, and differences in the way states are willing to treat the particular MNE.² This is a form of arbitrage activity. The result is tax avoidance. Avoidance is the use of the law/regulation to adversely reduce tax. The specific way this is done is open to challenge from tax authorities, but the activity is distinguished from evasion, which is simple illegal non-payment of owed tax (for nuance see Quentin, 2014).

The key point is that MNEs can locate entities in no or low tax jurisdictions and then use various strategies to direct or concentrate the reporting of income or profit in those locations (see Kleinbard, 2011). There can, therefore, be significant differences between where actual economic or business

² Most significant entities for tax purposes are termed permanent establishments (they have a physical base and have been present for at least 6 months). This concept is increasingly anachronistic given the capacity of firms to operate effectively without continuous presence.

activity takes place and where income ultimately ends up being reported. States are not innocent in this context, but do face conflicts of interest. They have *individual* interests in attracting the reporting of income. They also have an interest in accommodating MNEs via tax policy, since they hope to attract real investment and employment as well as reporting. At the same time, individual states have a vested interest in protecting their tax base and in ensuring taxes are collected. They must also consider the popular politics of taxation. A tax system can be perceived as more or less legitimate. Governments are perpetually aware of this, especially at times when public spending is being cut and the media is reporting egregious examples of corporate tax practices. However, the underlying problem remains MNEs can engage in tax arbitrage between states and states can and manifestly do engage in tax-related 'competition'. The current context is inherently problematic for legitimacy.

It is important to note that the current capacity for arbitrage and competition is a systemic problem that has evolved over the last century (Picciotto, 1992, 2011). The basic constituents of international taxation emerged during a previous era of globalization. In the early twentieth century, the flow of physical goods dominated trade. In a Fordist system manufacturing MNEs tended to reproduce their production and administration systems in strategic localities. The major tax issue of the time was that both the country of origin of an MNE and the locations in which it operated might find themselves taxing the same income. The problem to be solved through international tax treaties and regulation was double taxation. However, we now live in a differently globalized neoliberal and digital age. Services are now a large proportion of trade. A great deal of activity occurs through the Internet, creating scope for deliberate ambiguity regarding where activity occurs. Branding and intellectual property are now routinely separated from actual production, as is administration. Based on new technology, administration can be networked and distanced. Information technologies also mean that constructing and managing complex structures of entities has become both feasible and affordable. Highly specialised financial, tax, and consultancy services have also developed to facilitate this process. These too are MNEs; specialised units within the universal banks and the accountancy 'Big 4' of Deloitte & Touche, PricewaterhouseCoopers, KPMG and Ernst & Young (Sikka, 2015).

Opaque complex structures are now the norm for MNEs (Bryan et al, 2016). For example, in 2014 BP was reported to have 1180 affiliates in 84 countries in a twelve-tier structure (Palan and Mangraviti, 2016). In 2011, HSBC and Barclays were reported to control 940 subsidiaries in tax havens alone, including the provision of tax efficiency services to clients (Murphy & Nehru, 2013). The problem is no longer one of double taxation but rather the potential for double non-taxation. MNEs are able to structure their affairs so that little or no tax is paid anywhere. Revenue is routed through complex networks of entities and held 'offshore' and may benefit from offsets through debt structures along the way. 'Offshore' is a slightly misleading term in two ways. First the localities need not be geographically remote, merely specialised as jurisdictions, such as Delaware. Second, well-known offshore or international finance centres, referred to by critics as tax havens or secrecy jurisdictions, are destinations the efficacy of which require the complicity of many parties, including the main financial

centres and many states. Their operation is an ordinary part of global business activity (Shaxson, 2011; Palan et al, 2010).

The contemporary international tax system is a combination of institutional arrangements of individual states and regional blocs and a patchwork of bilateral treaties based on the OECD model treaty. The OECD convention is now in its ninth iteration. The underlying framework takes as its point of departure the separate legal entities of an MNE. The primary focus is 'transfer pricing', which is the allocation of values between entities within an organization. The transactions between entities are assessed to establish whether they occur at a recognizable market price. This is termed the 'arm's length principle' (Article 9 of the OECD model convention). The rationale for this is that a market price supposedly indicates that transfer pricing is *not* being used to advantageously shift where income is being reported. It is implicitly fair. There are currently five accepted methods of assessment for transfer pricing (OECD, 2010).³ Concomitantly, tax authorities investigate whether specific arrangements or schemes used by MNEs violate some aspect of law or regulation. For example, recent high profile issues have included: (1) the use of 'patent boxes', which offer reduced corporation tax rates for reported income from intellectual property, (2) whether tax agreements ('advanced pricing agreements') between MNEs and particular states violate EU state aid rules (constituting unfair competition), and (3) whether intra-organization transfers are genuine debts created for investment purposes (or exist notionally merely to offset a tax liability).⁴

There are many reasons why the current system is dysfunctional. Transfer pricing is fundamentally inconsistent as a concept. The existence of a firm implies cost savings based on reduced 'transaction costs' *within* an organization, but the arm's length principle assumes that a representative price is derived from a market interaction between *separate* entities. The different logics mean prices *should not* coincide. Furthermore, the application of the principle involves numerous practical problems. Between 60 and 70 percent of international trade is now intra-firm. This means it is difficult to establish a market reference price for many transactions. This is a problem compounded for many modern goods and services whose value is rooted in unique brands and intellectual property. Challenging the values used in transfer pricing and the strategies or schemes via which MNEs shift where income or profit is reported is necessarily a case-by-case process. It requires information, resources and time. There are millions of transactions and thousands of MNEs. Challenges are unlikely. As Sikka notes (2015), based on UK House of Commons Public Accounts Committee hearings, the Big 4 have advised clients regarding schemes that they estimate have only a 50% chance of surviving legal challenge. Furthermore, the very nature of the system provides great scope for MNEs to contest any

³ For example, the Comparable Uncontrolled Price method is based on direct comparison of prices. The other four involve some kind of proxy calculation.

⁴ The EU now monitors and provides voluntary guidelines on the use of patent boxes. Many members have them, including the UK and Ireland. The UK patent box introduced in 2013 allows a reduced rate of 10% corporation tax on reported income from the commercial exploitation of patents. The company can be part of a group and eligible patents from which income derives can be registered at any of a range of different patent offices. The EU stipulates the reduced tax must be directly linked to research and development activity but the reality is far more ambiguous. See <https://www.gov.uk/guidance/corporation-tax-the-patent-box>

challenge. The current system may formally oppose tax avoidance but is unable to effectively prevent it (for context see Rixen, 2008; Sharman, 2006).

The consequences of tax avoidance and the limits of progress

The consequences of tax avoidance are significant. Clausing provides a neat summary, expressing the problem in terms of base erosion and profit shifting (BEPS) effects:

Recently, the OECD (2015) finds that the annual net tax revenue loss from tax planning is about \$100 billion to \$240 billion and compares its estimates with those of the IMF, the Joint Committee on Taxation, and others. A study by three IMF economists (Crivelli, Keen, and de Mooij (2015)) also finds that base erosion problems are large. Their short-run estimates indicate that OECD countries lose \$207 billion in revenue (0.23 percent of GDP) and that developing countries lose \$105 billion in revenue (0.84 percent of GDP). Long-run estimates are \$509 billion for OECD countries (0.6 percent of GDP) and \$213 billion for developing countries (1.7 percent of GDP). Keightley and Stupak (2015) and Gravelle (2015) describe the large and increasing problem of BEPS in the United States and elsewhere. Indeed, the stylized facts are overwhelming in their confirmation of the scale of the profit-shifting problem. For U.S. multinational corporations, the share of income reported in foreign countries has been steadily increasing, and income booked in low-tax countries is implausibly high by any reasonable metric. As reported by Gravelle (2015), U.S. affiliate corporate profits were 645 percent of Bermuda's GDP and 547 percent of the Cayman Islands' GDP in 2004. As absurd as those numbers are, by 2010 they had increased to 1,614 percent for Bermuda and 2,065 percent for the Caymans. Further, estimates indicate that U.S. multinational corporations have accumulated more than \$2 trillion in permanently reinvested earnings in low-tax locations, more than \$1 trillion of which is held in cash. (Clausing, 2016)

As she notes all figures are likely underestimates, given the problem of data collection. Her own research puts the figure at around \$280 billion per year globally by 2012 and she also notes that around 20% of US corporation tax may be avoided annually. The European Commission (EC, 2012), estimates tax avoidance and evasion for just the European Union at around €1 trillion per year. HMRC estimates annual UK tax avoidance at around £3 billion as part of a tax gap (tax that could be paid but is not) for 2013-14 of £35 billion. Richard Murphy provides a far higher estimate for the UK tax gap at £120 billion (2014).

There has, however, been some progress. Corporate tax avoidance has become a high profile issue over the last 5 years and this was recognized in 2013 by the G7 and G20, resulting in the BEPS project under the auspices of the OECD. BEPS has produced a series of reports, resulting in 'Actions' and a framework for monitoring, review and standard setting (first reported in 2014, and updated in 2015 and 2016). The stated main aim has been to eliminate double non-taxation and 'aggressive' tax planning for avoidance. Significantly, participant states have committed to requiring MNEs to engage in country-by-country reporting of

revenue, profit and actual tax paid by 2017 (Action 13. OECD, 2015). In principle, this should provide individual tax authorities with more information to challenge MNEs actual tax practices. However, the International Centre for Tax and Development has supported a network of well-known researchers who provide a more critical analysis of the issues and progress of the OECD work and its context. As Picciotto notes, BEPS is characterised by incremental reform (2016). This approach tends to encourage greater participation in the process, ensuring some progress. At the same time, actual changes tend to be limited and carry with them the underlying problem that is built into the system.

The underlying problem is that treating the different components of an MNE as separate entities encourages firms to channel reporting of income to entities located in low or no tax jurisdictions, and encourages states to compete as locations for reporting. This is irrespective of other interests they may have and the rhetoric they may espouse. The OECD BEPS reports recognize that firms should be 'taxed where economic activities occur and value is created' (OECD, 2013a). At the same time, the reports recommend that a transfer pricing approach remains basic and that any new tax rules respect the sovereignty of states. As Palan notes (2002), many states have 'commercialised' their sovereignty. This creates tensions for any collective approach to the problem of tax. Ultimately, incremental reform perpetuates the systemic dynamic in which MNEs still have motives to engage in arbitrage. States still have motives to attract business through approaches to tax the very context of which are competitive in pathological ways, despite any commitment to the contrary. As such, it seems premature to claim that the problem of corporate tax avoidance is now in hand and tax havens' days are numbered. There seems to be, therefore, a clear need for a transformative approach to policy.

Apple in Ireland

Consider the long running case of Ireland and Apple. This case first came to prominence as part of the now notorious 'double Irish' practice exposed by the US Levin Congressional Committee in 2013. Based on differences in tax status between the US and Ireland, Apple was able to structure key entities as tax resident in no jurisdiction. According to the report, Apple Operations International (AOI) was incorporated in Ireland. AOI as a legal person owned through various routes Apple's other entities outside the US. However, though incorporated in Ireland it had not been managed or controlled *from* Ireland, but from the US. Based on Irish law it was not classed as tax resident. US law mainly taxes on the basis of location of incorporation so AOI was not classed as tax resident in the US either. For the purpose of taxation AOI was effectively 'stateless'. Apple Sales International (ASI) was also incorporated in Ireland and ASI owns the rights to Apple's intellectual property outside the US. Given the nature of Apple's business, significant portions of its income have been channelled to ASI, but little tax has been paid in Ireland. Senator McCain put the matter starkly in his opening statement to the US Senate Subcommittee:

Although Apple is by all accounts an American company, its holding company in Ireland currently retains the bulk of its profits. The Subcommittee's investigation has uncovered a disturbing truth. Apple's

three primary Irish entities [including also Apple Operations Europe or AOE, which is owned by AOI] hold 60 percent of the company's profits, but claim to be tax residents nowhere in the world. It is completely outrageous that Apple has not only dodged full payment of U.S. taxes, but it has managed to evade paying taxes around the world through its convoluted and pernicious strategies. Specifically, from 2009 to 2012, Apple Operations International received roughly \$30 billion in dividends from other Apple subsidiaries around the world. That made up 30 percent of Apple's total worldwide net profits over the last few years. However, Apple Operations International did not pay corporate income taxes to any national government. Furthermore, Apple Operations International, a company with tens of billions of dollars in cash, has never had any employees and appears to be completely directed by Apple in California. Perhaps sensing that it might need to maintain some semblance of legitimacy, Apple Sales International, another subsidiary with no tax residence and no employees through 2011, began employing 250 people in 2012. However, with \$22 billion of income in 2011, Apple Sales International only paid one-twentieth of 1 percent in Irish taxes. As Apple funnels billions of dollars through its numerous Irish entities, even those entities that do pay taxes enjoy a negotiated tax rate of less than 2 percent. Apple contends that none of its subsidiaries in Ireland reduce its U.S. tax liability by one cent. This statement is demonstrably false. (McCain in Levin 2013: p. 9)⁵

As Levin notes:

Why Ireland? Another highly successful but, until now, hidden tax strategy is that Apple has quietly negotiated with the Irish Government an income tax rate of less than 2 percent, well under the Irish statutory rate of 12 percent as well as the tax rates of other European countries and the United States, well below those statutory rates. And as we have seen, in practice Apple is able to pay a rate far below even that low figure [nothing in some cases, less than 1% for ASI]. In 2012 alone, due to the cost-sharing agreement [a transfer pricing strategy] essentially shifting profits from all Apple sales outside of the Americas to Ireland, ASI received \$36 billion in income in a nation where it pays almost no income tax. (Levin, 2013: p. 5)

Ireland has committed to phasing out the double Irish by 2020. However, it has already put in place a 'patent box' system to attract the reporting of group income based on intellectual property. The case also led in 2013/14 to a European Commission investigation, led by the Competition Commissioner into the status of 'negotiated' agreements in Ireland. Reached in 1991 and 2007, these advanced pricing agreements (APA) act as 'supplements' to standard transfer pricing based on the OECD methods and the arm's length principle. The investigation has turned on whether the 1991 and 2007 agreements (rulings)

⁵ For Apple's rejoinder see the testimonies of Timothy Cook CEO and other Apple representatives in Levin, 2013

represented an accepted and correctly applied transfer pricing methodology and that tax paid based on the APAs were comparable to the 'ordinary tax system' 'under market conditions'. If not then Ireland had illegitimately denied itself revenue and the arrangement also created a situation of unfair competition.⁶ In an initial 2014 decision the Commission stated that there were grounds to conclude that the arrangement *did* constitute state aid. Ireland was invited to respond. Following further lengthy investigation, the Commission eventually ruled 30th August 2016 that:

[T]wo tax rulings issued by Ireland to Apple have substantially and artificially lowered the tax paid by Apple in Ireland since 1991. The rulings endorsed a way to establish the taxable profits for two Irish incorporated companies of the Apple group (Apple Sales International and Apple Operations Europe), which did not correspond to economic reality: almost all sales profits recorded by the two companies were internally attributed to a "head office". The Commission's assessment showed that these "head offices" existed only on paper and could not have generated such profits. These profits allocated to the "head offices" were not subject to tax in any country under specific provisions of the Irish tax law, which are no longer in force. As a result of the allocation method endorsed in the tax rulings, Apple only paid an effective corporate tax rate that declined from 1% in 2003 to 0.005% in 2014 on the profits of Apple Sales International. This selective tax treatment of Apple in Ireland is illegal under EU state aid rules, because it gives Apple a significant advantage over other businesses that are subject to the same national taxation rules. The Commission can order recovery of illegal state aid for a ten-year period preceding the Commission's first request for information in 2013. Ireland must now recover the unpaid taxes in Ireland from Apple for the years 2003 to 2014 of up to €13 billion, plus interest. (EC, 2016a)⁷

The US and Irish response to the EC decision are revealing. The US Treasury immediately responded that the EC was in effect denying the US the tax revenue referred to. This implies that eventually revenue would be repatriated and that the US had the primary call on it. There is some logic to this given that the US

⁶ The 2014 EC state aid decision clarifies the terms: "According to Article 107(1) TFEU, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the provision of certain goods shall be incompatible with the common market, in so far as it affects trade between Member States... The main question in the present case is whether the rulings confer a selective advantage upon Apple in so far as it results in a lowering of its tax liability in Ireland... The Court of Justice has confirmed that if the method of taxation for intra-group transfers does not comply with the arm's length principle, and leads to a taxable base inferior to the one which would result from a correct implementation of that principle, it provides a selective advantage to the company concerned." (EC, 2014: p. 14-15)

⁷ At the time only 6% of Apple's pre-tax global income was allocated to jurisdictions *other than* Ireland or the US. Ireland employed 4% of Apple's global workforce and the territory accounted for 1% of sales. AOI paid no corporation tax and filed no corporate income tax returns between 2009 and 2012, although its estimated income was \$30 billion. (see Seabrooke and Wigan, 2017: p. 16)

Congressional investigations have maintained that the tax was merely and dubiously reported in Ireland and had been earned globally by a US MNE. From this point of view, the EC decision represents a tax grab, but only if one accepts the issue as a problem of double taxation, when in fact it had arisen as a problem of double non-taxation. The EC approach was to tackle the non-taxation within the bloc based on rules for state aid. Clearly, once tax arbitrage begins to take place the disjunctures between regions and states create grounds for conflict.

The Irish response, articulated by its Finance Minister Michael Noonan was to begin a process of appeal to the European Court of Justice, *rejecting* its claim to the €13+ billion. The response is ostensibly bizarre but has a rationale. According to Noonan, the decision constitutes unwarranted interference in the sovereign affairs of Ireland. Ireland's economy and also its recovery from the financial crisis have been built on attracting capital flows from, and the incorporation of, MNEs. Some of this has involved real investment and employment, so these two and the attraction of reporting are entangled.⁸ Tax competition is integral to Ireland's economic model. MNEs pay low tax in Ireland, a headline rate of 12.5%, a reality in many cases of virtually nothing. Concomitantly, Ireland offers an additional service via which other states are deprived of potential tax. Clearly, the low rate and deprivation create a mutual loss of revenue for all states. However, there is also an ancillary gain in Ireland beyond this specific loss because of other effects. If Ireland accepts the EC decision and collects the tax then this may well make it difficult for Ireland to continue to attract MNEs based on its current strategy.

The Apple case is not unique but it illustrates an important point.⁹ The current international tax system encourages fragmentation. It is a common system but not a genuinely coherent one (for context see Rixen, 2011; Woodward, 2006). Gradual and piecemeal reform cannot easily resolve this. One reason why it cannot is that the system is inherently divisive. States have a collective interest in ensuring tax is paid but individual motives to accommodate MNEs in ways that undermine the capacity of all states to tax MNEs effectively. The main beneficiaries of this are MNEs. When the Irish Finance Minister places the problem in terms of sovereignty what does this really mean? Sovereignty in the context of a representative democracy evokes the issue of who is represented and in what ways. The balance of representation seems to be towards the interests of MNEs rather than Irish citizens (sovereignty is 'commercialised'). However, given the entanglement of tax competition with real investment and employment the matter is not clear cut. Still, it remains the case that if MNEs pay little or no tax then more is paid by citizens, even if this derives in part from income earned at MNEs. Otherwise, public debt rises or public services suffer. The same public services that MNEs then rely on: infrastructure, a fire service, schools to educate future staff, hospitals to keep current staff healthy. In any case, it would be dubious to infer that citizens find it *acceptable* that MNEs are able to exercise power and influence to pay little or no tax.

⁸ Apple employs over 1,500 people in Ireland. There are more than 1,000 MNCs located in Ireland employing in total more than 150,000 and this constitutes the highest proportion of total employment in any OECD country.

⁹ Google, Amazon, Microsoft, Facebook, McDonalds, Fiat and many others have also come under scrutiny, as has Luxembourg and various other EU members. In July 2016 UK HMRC revealed that it had more than 140 APAs.

Acquiescence from a position of weakness is not support. Moreover, evidence from research on 'tax morale' tends to indicate perceived fairness matters to the legitimacy of the tax system (see OECD, 2013b).

The very fact that MNE tax behaviour is categorized as avoidance and is quasi-legal undermines the public perception that contemporary democracy is ethically grounded. This in turn leads to toxic forms of populism and cynicism regarding politics in general. Tax avoidance is part of the complex of problems of legitimacy that regional bodies and individual states confront. Concomitantly, the sovereignty problem raises the issue that citizens of other states, who are denied tax, are not represented when decisions are made in Ireland. This is mirrored by likely future events in the US. Trump campaigned on an economic nationalist agenda, combined with tax cuts and simplifications. One aspect of this has been to encourage (if not coerce) corporations to repatriate capital. In the real context of the complexity of global tax activity, this will likely be just one more way in which tax competition undermines the capacity of all states to tax MNEs effectively.

A regional bloc such as the EU exists in part to reconcile inter-state conflicts of interest. Moreover, in theory such conflicts are what the international tax system and the various bilateral treaties are supposed to address. The intervention of the European Competition Commissioner is explicitly about what is fair. But this does not mean the system as is *encourages* fairness; the fact that MNEs are treated as many separate entities, subject to transfer pricing, promotes inequity, and sometimes iniquity.¹⁰ A case-by-case response has resource limits and any success simply invites innovation of current strategies of avoidance. Country-by-country reporting provides information to contest strategies and this is important, but information is not necessarily power, though it can be ammunition for further change. The problem is *systemic*. Ireland's decision to reject €13+ billion in tax revenue highlights this. The decision is not irrational given the context, but it is perverse because of that context.

The EC decision also has context. Clearly, the Commissioner is aware that the income in Ireland has been earned across the EU and beyond. Requiring Ireland to collect more of it is in a sense enforcing a fiction. It is a decision to apply the rules that currently exist in a way that remind MNEs and Ireland that they cannot act with impunity. This is likely to be limited in its impact. Though it has spawned headlines it is a small act since both Apple and Ireland have appealed. Apple, conscious of negative publicity in the US have argued that more of the disputed tax should be owed in California, since this is where its research and design hub is located. In its most recent response the EC rejects this, since Apple's structures give rights to intellectual property outside the US to the Irish entities, and it is this income based on the actual structures that is at issue (EC, 2016b). The EC remains focused on state aid. However, the response does not

¹⁰ The problem is of course widely acknowledged. For example, *OECD Harmful Tax Competition: An emerging global issue* (OECD, 1998). The EC/EU has various initiatives, which attempt to develop a concept and tests of fair competition, as do many states. The UK's approach is still underpinned by the 2001 HM Treasury/Inland Revenue document, 'Large Business Taxation: the Government's strategy and corporate tax reforms – a consultation document', which identifies 6 components for competitive tax: a broad base, low rate, transparency, consistency, flexibility, neutrality and responsiveness to market failure. 'Fairness' remains a difficult problem based on the current system (e.g. in what sense does it relate to 'low' and 'market failure').

that other EU members may seek to claim some of the €13+ billion if they can establish that sales attributed to Ireland should have been recorded in their locality. It seems likely that the case will drag out for years and little of the actual tax may eventually be collected.

However, the case is a signal. In a curious way, it is an act on behalf of democracy by a relatively remote, if formally elected and selected, institution. Constraining MNEs is to return some potential sovereignty to *all* citizens of the EU within their member states, something that individual governments can be either disinclined to do or unable to do. The capacity of the EC to do this is perhaps an unintended consequence of the democratic deficit within EU institutions. This is by no means a positive argument for the perpetuation of that deficit given its other consequences, not least Brexit. For example, the Democracy in Europe Movement addresses this.¹¹ At the same time, the Apple case exposes the limits of the current approach to tax avoidance. Something more transformative seems to be required. In its absence corporation tax remains an issue liable to contribute to public cynicism and thus problems of legitimacy. The EC has already developed an alternative ‘unitary’ system for corporation tax: the Common Consolidated Corporate Tax Base (CCCTB). The CCCTB represents a potentially transformative approach to policy. However, it is controversial, precisely because it is transformative, and must confront a series of further challenges that are more than simply technical. It is important to highlight these since they underscore that tax is a matter of behaviour in relation to context, ethics and responsibility.

The Common Consolidated Corporate Tax Base

The CCCTB is not new. It has been supported by the EC across a series of presidencies. It first emerged in an EC Communication (2001, p. 3), and was subsequently discussed as a ‘non-paper’ in 2003 and 2004. This resulted in the creation of working groups, which produced a technical outline for the CCCTB in 2007. Dispute over the CCCTB followed and this was exacerbated by the global financial crisis. However, a draft EU directive was published in March 2011 and provisionally endorsed in March 2012 by the European Parliament (with proposed amendments). The CCCTB has remained under development and discussion since then (see conclusion). The CCCTB is a version of unitary taxation by formula apportionment (see Panayi, 2013, 2008). Unitary taxation treats the many otherwise separated entities of a MNE as a single entity for tax purposes. The CCCTB has four aspects:

1. A set of consolidated accounts is produced for all the entities in an MNE’s organization. The firm is treated as a whole. However, since the CCCTB is an EU initiative this can only be done for EU member locations, but the intent is to create a common corporate tax base within the EU, which will then become a prototype of good practice for emulation.¹²

¹¹<https://diem25.org>

¹² The CCCTB automatically requires consolidation of all subsidiaries defined in terms of parent company ownership of capital (75%+), profit entitlement (75%+), and voting rights (50%+). Importantly, the existence of intermediates in a chain that do not fulfil these criteria does not break the consolidation for the next in the chain (see Articles 54, 59, & 109, EC 2011a)

2. The consolidated accounts are reported to a designated tax authority, likely the home base of the MNE within the EU.
3. The reported income/profit is then distributed to member states based on a formula that calculates the proportion of real economic presence of the MNE in each member state.¹³
4. Each state then taxes the income/profit allocated to it. The actual tax rate applied is *not* set by the CCCTB but by the member state. The 2011 directive includes no mechanism to harmonise tax rates or to impose a minimum.

Unitary taxation by formula apportionment is transformative because it consolidates accounts, treating the MNE as a whole. It thus eliminates intra-group transactions and the basic systemic problems created by separate entity status and the application of transfer pricing methods, subject to the arm's length principle. It goes beyond a requirement for country-by-country reporting. Since income or profit to be taxed is allocated based on real economic presence, there is no advantage for the MNE in engaging in profit shifting within the EU to concentrate reporting of income. The formula is (EC, 2011a: Article 86, p. 49):

$$\text{Share A} = \left(\frac{1}{3} \frac{\text{Sales}^A}{\text{Sales}_{\text{Group}}} + \frac{1}{3} \left(\frac{1}{2} \frac{\text{Payroll}^A}{\text{Payroll}_{\text{Group}}} + \frac{1}{2} \frac{\text{No of employees}^A}{\text{No of employees}_{\text{Group}}} \right) + \frac{1}{3} \frac{\text{Assets}^A}{\text{Assets}_{\text{Group}}} \right) * \text{Con'd Tax Base}$$

Share A refers to the individual EU member state and Group to the total for the organization in all member states for each of three measured factors. For reasons of simplicity the three factors were given equal weighting in the original 2007 formulation and this has remained the case thereafter. Sales of goods and services are measured in terms of proceeds at the point of destination to customers/clients. This is subject to the proviso that the MNE must have a genuine sales point in the country of destination. This is to prevent 'nowhere sales'. Nowhere sales arise where the MNE registers the sale of its goods or services in a locality in order to benefit from low or no tax on those sales; it typically does not reflect actual sales activity. For example, there is no genuine branch or affiliate. Where this is identified a 'throwback rule' applies.¹⁴ The employment factor is split into two sub-categories: the number of employees, and the value of the payroll where employees work. The value of the payroll and the number of employees are both significant indicators of an MNE's presence. The measure defines employment as where employment is actually exercised

¹³ Note, I am using income for simplicity, the CCCTB uses the term revenue and this is subject to a technical definition that seeks to capture all possible ways of stating relevant income (see EC, 2011a: Article 4(8)).

¹⁴ According to Article 96 of the 2011 draft directive: "Sales of goods shall be included in the sales factor of the group member located in the Member State where dispatch or transport of the goods to the person acquiring them ends. If this place is not identifiable, the sales of goods shall be attributed to the group member located in the Member State of the last identifiable location of the goods." And "If there is no group member in the Member State where goods are delivered or services are carried out, or if goods are delivered or services are carried out in a third country, the sales shall be included in the sales factor of all group members in proportion to their labour and asset factors." (EC, 2011a: Article 96 (1 & 4))

and defines employees as those engaged in common activities. The former prevents potential abuses based on manipulating where the employee is registered as employed and where they are paid. The latter prevents manipulation through subcontracting portions of the workforce. To simplify the asset component of the calculation, assets are restricted to tangible assets. The intention is to provide a measure of capital investment whilst excluding financial assets and inventory.¹⁵ Employment and assets represent the supply side of income generation and sales represent the demand side (CCCTB WG, 2007: p. 12). The greater the share of the three weighted factors in any given member state then the greater the share of the common tax base that is eligible for taxation in that state.

Due to the common base, unitary taxation by formula apportionment addresses both double taxation and double non-taxation. It is an elegant solution to a systemic problem. However, it is not easily introduced precisely because the system to which it provides a solution already exists. Though the current system is problematic transforming it is disruptive. One reason why opposition to the CCCTB has arisen is that individual parties are not focussed on the long run collective benefits of a fully functioning form of unitary taxation. Perception is influenced by embedded divisive interests, corporations engaged in arbitrage and states engaged in competition. These must be addressed if the CCCTB is to be adopted. These are not purely technical matters though they may have technical constituents.

The Single Market and the CCCTB: tensions in concepts of efficiency and rationality

One important issue is the basic tension inherent in the contemporary framework of the EU. Since its inception the CCCTB has been conceived as a key component of the Single Market. This is first stated in the original EC Communication of 2001 (p. 3), it is reiterated in the technical outline of 2007 (CCCTB WG, 2007: #67, p. 16), and is fleshed out in the 2011 directive:

The Common Consolidated Corporate Tax Base (CCCTB) aims to tackle some major fiscal impediments to growth in the Single Market. In the absence of common corporate tax rules, the interaction of national tax systems often leads to over-taxation and double taxation, businesses are facing heavy administrative burdens and high tax compliance costs. This situation creates disincentives for investment in the EU and, as a result, runs counter to the priorities set in Europe 2020 – A strategy for smart, sustainable and inclusive growth. The CCCTB is an important initiative on the path towards removing obstacles to the completion of the Single Market and was identified in the Annual Growth Survey as a growth-enhancing initiative to be frontloaded to stimulate growth and job creation. [...] A key obstacle in the Single Market today involves the high cost of complying with transfer pricing formalities using the arm's length approach. Further, the way that closely integrated groups tend to

¹⁵ This is sub-divided into depreciable assets, whose value needs to be adjusted, and non-depreciable assets, such as land, which are valued at cost.

organise themselves strongly indicates that transaction-by-transaction pricing based on the 'arm's length' principle may no longer be the most appropriate method for profit allocation. (EC, 2011a: p. 4)

The key point is that one of the main ways the CCCTB has been justified is as a means to *complete* the Single Market. The idea that tax should be fair and tax competition should not be harmful is not ignored. However, the 'completion' argument concerns economic efficiency imperatives *for* MNEs, where it is assumed that MNEs can be encouraged to be cooperative by removing tax obstacles. There is a tension here. The argument assumes a more cooperative approach. However, many MNEs have taken, often tacitly, an oppositional stance -- if only by seeking to shape how and what they will cooperate with. This is camouflaged conflict that sometimes breaks cover, rather than cooperation. The CCCTB only exists because MNEs have exploited tax opportunities to engage in avoidance. Actual MNE behaviour and the reality of the Single Market concern relations of power. To address this, the transition to the CCCTB and then the effective functioning of it must involve more than an economic argument and a change in formal rules. It must involve a change in what we mean by an economic argument and a change in attitude to rules. It must internalise ethical and perhaps informal mechanisms within the CCCTB. As a mechanism it must also be an appropriately configured practice. The tension, must, therefore, be recognized and addressed rather than perpetuated, which it currently is.

For example, the EC has produced a series of cost-benefit analyses that set out the potential benefits of the CCCTB for MNEs (EC, 2011b; 2011c). The models take the best possible assumptions regarding transaction costs, assuming that consolidated accounts actually reduce compliance costs, resulting in a possible annual reduction in such costs to existing MNEs of €700 million. The models then assume that reduced transaction costs actually increase the growth of firms across national boundaries, since the costs are a barrier to entry. This results in further attributed annual benefits of €1 billion. However, the assumption that consolidation of accounts will simply reduce transaction costs because it reduces, in principle, the costs of producing compliant accounts sits awkwardly with the existing complexity of tax behaviour and what it indicates. The construction of many entities in different locations, the opacity of accounts and the employment of tax specialists to create strategies are not accidental. Firms may complain about 'red tape' but they have not lobbied for a simpler system and actively worked towards simplifications of how they comply with that system. Tax avoidance is intentional activity, it is the *creation* of a legal space in which tax is minimised or negated.

The cost-benefit analyses proceed on the basis that the existence of different tax regimes creates distortions that raise the costs of both MNEs and tax authorities, whilst also creating an impediment to the expansion of MNEs *to* new territories, because differences in tax regimes may act as a barrier to entry. However, this was not the original problem that called forth the CCCTB. It is a different rationale than MNEs engaging in shifting incomes and incorporations *between* territories. It is less about tax avoidance and more about recognizable economic benefits of tax compliance with an efficient system. As of July 2016, the issue of tax avoidance has been subsumed under a different proposed EC directive (EC, 2016c). The proposals in the directive are important but the focus

is similarly technical, providing member states with mechanisms to dispute how and where income has been reported. Moreover, the framework is still one that juxtaposes fairness to efficiency.

The underlying logic in the way the CCCTB has been positioned is that a single simpler common approach to corporation tax creates the basis for the spread of investment, employment and economic growth through MNEs. However, one must differentiate between economic inefficiency of the textbook variety and what is effective based on perceptions of interest in a real economic situation. The current system may be *inefficient* from the point of view of a perfect market in which there could be lower transaction costs for all and perhaps related transnational growth. However, it is also an *effective* system in terms of enabling tax avoidance. MNEs may still oppose the CCCTB and may still seek to subvert it and may do so by lobbying for exemptions and creating new kinds of complexity actually increasing their transaction costs. They may decide that such higher costs are a necessary concession in order to protect the opportunity to avoid tax and so protect profits.

What the example illustrates is that the CCCTB cannot simply be a set of technical conditions expressed in regulation and law. It ought to, for example, address global wealth chain (GWC) potentials. That is, appropriately explore how wealth is captured and protected rather than merely focus on how more wealth might be created (Seabrooke and Wigan, 2017). To be effective it must also encourage and help to shape appropriate commitments from MNEs to pay fair tax and by states to ensure that tax is paid. The architects of the anti-tax avoidance directive and the CCCTB are aware of the issue but the tension continues. The cost-benefit analyses, for example, start from the assumption that MNEs choose to comply or cooperate. The OECD likewise recognizes this. In its *Principles of Good Tax Administration* it specifically states that voluntary compliance is a cornerstone of effective taxation (2001). The CCCTB is important because its formal construction takes corporate taxation out of the context of separate entities and problems of transfer pricing. It seeks to tax on the basis of real economic presence. But the problems of changing the attitude of MNEs to paying tax and of states in how they compete with reference to tax remain important. These are normative or ethical issues regarding how one behaves. Ethics-as-fairness continues to be awkwardly juxtaposed to how economic decisions are structured (see Morgan, 2016a).

MNEs continue to claim that they follow the law and pay all legally required taxes. They also continue to argue that they have a fiduciary duty to minimise taxes in order to maximise shareholder value.¹⁶ This creates significant scope for firms to pay far less than headline rates of corporation tax. It implies a duty that shades into justifications for manifestly unethical behaviour. The CCCTB changes the context in which behaviour occurs, but there is also a need to transform the attitudes that underpin any and all behaviour by the firm in order to prevent subversion of the CCCTB once implemented. Economic theory traditionally treats evasion, and by extension avoidance, as rational behaviour. It is what one would do if not prevented. The CCCTB takes a different position. Tax

¹⁶ This is despite that shareholder value is a fictitious commitment in various practical and conceptual ways and that the law in many countries formally requires more nuance from the firm. For example, the UK Companies Act 2006 requires firms to consider the long-term impact of their behaviour on communities.

avoidance becomes an economic irrationality that a rational agent will put behind them as part of completing the Single Market. Neither concept of rationality explicitly places ethics as core to economic decisions, where a primitive sense of rationality is replaced by explicit ethical economic reasoning. Clearly, the intent is that MNEs do precisely this, but more thought needs to be put into how this can be achieved. Recent work on Tax Morale has potential in so far as it explores the ‘non-pecuniary’ aspects of behaviour. However, much of it is narrowly posed in terms of nudging behaviour to increase taxes paid. There is a great deal of scope to address how firms are *socialised* based on explicit ethical obligations, which become integral to how they view their economic and business activity. One should not conflate this scope with the widespread failures of the discourse of corporate social responsibility. It is broader than this, involving an aware citizenry, civil society pressure and social movements working cooperatively with experts (such as the Tax Justice Network). The socialised firm is not simply about naively asking MNEs to be nice. It is about creating a critical context in which it pays to be ethically grounded.

The EU already has a Platform on Tax Good Governance that helps to pursue this agenda. Its success and that of movements like the Tax Justice Network hinge on more public awareness and pressure, including pressure to introduce the CCCTB. However, the point to emphasise is that for the CCCTB to be transformative there must also be transformations in how conduct is conceived and rules are followed. This in turn implies that for the CCCTB to be effective may require broader transformations in the socio-economic framework. Moreover, the tensions have potential significance for the issue of the use of tax as a component in competition between states.

One of the major sources of resistance to the CCCTB from member states has been because it may ultimately result in tax harmonization (see also Spengel, 2007). That is, the imposition of a common tax rate.¹⁷ The European Parliament’s set of preferred amendments recognizes that the issue needs to be revisited to prevent tax competition leading to a race to the bottom (EP, 2012: p. 5). It may be the case that an effective CCCTB ultimately requires corporation tax to become a non-competitive aspect of economic activity. The EC have been unwilling to address this fully. EC documents argue that the existence of the CCCTB creates a common base and a single transparent system. Concomitantly, within that system the effective tax rates paid in each country are likely to be clearer and so there will be greater vigilance, and hence pressure, which it is inferred will reduce aggressive tax competition. Moreover, an EU-wide CCCTB creates a united front to challenge the activities of ‘non-cooperative’ tax jurisdictions and particular MNEs activities beyond the EU. However, nothing about these claims prevents a logic of tit-for-tat reductions in tax rates within the EU. The EC’s reluctance to go further is clearly strategic. It is a current concession to sovereignty arguments in the hope of reducing member state opposition. It owes more to political reality within the EU based on economically divisive state interests (typified by Ireland’s response in the Apple case) than it does long term collective interests or coherent argument.

¹⁷ As Devereux et al (2008) note, the EU Ruling Committee recommended a 30% minimum rate for corporation tax in 1992. This was lower than actual rates in Europe at that time (but clearly far higher than is the case today because of tax competition).

Conclusion: current prospects for the CCCTB

The European Parliament endorsed the EC CCCTB directive of 2011 in 2012. However, this was not without dissent.¹⁸ The proposal was then blocked by heads of state sitting on the European Council. Many member states remain concerned about its implementation. The key concerns focus on sovereignty and the right to tax, tax harmonization and then the unintended and transitional consequences for individual states that will occur because of a shift to an apportionment formula. Ultimately, these arguments do not concern the long-term collective benefits of unitary taxation. They are nonetheless important. For the CCCTB to become law it must be adopted unanimously by member states. The EC remains the main driving force behind the CCCTB. There is no consensus amongst EU members via the Council or Parliament regarding the CCCTB precisely because of embedded fragmentation. At the same time members cannot ignore the problem of tax avoidance nor deny that it is a common and collective problem. Each continues to espouse the need for a more effective approach and their opposition to 'aggressive' avoidance. After a strategic rethink the EC released a new Action Plan in mid-2015, and began a consultation on the CCCTB. In January 2017, the CCCTB was relaunched within a new two-step strategy, beginning first with achieving agreement on the benefits of a common tax base and then on a fuller consolidated approach leading to eventual legislative agreement for a CCCTB.¹⁹ The Action Plan (EC, 2015) restates the issues: avoidance has become easier in a modern context, the current approach based on transfer pricing is increasingly anachronistic, and ensuring corporations pay 'fair' tax is important to legitimacy. The Action Plan and relaunch cover five areas but have two key aspects. It endorses the OECD BEPS agenda to introduce country-by-country reporting, close loopholes, tighten the application of transfer pricing rules, and goes further by suggesting the limits of current approaches and the ultimate intention to tax where economic activity occurs.²⁰

¹⁸ The vote was 452 for, 172 against, and 36 abstentions. The EC is under no obligation to incorporate suggested amendments from the EP into a directive. However, under Protocol No 2 (subsidiarity) of the Lisbon Treaty a national parliament of a member state may submit a written 'reasoned opinion' if a legislative proposal is deemed to interfere in the sovereignty of the member state. If 18 of the possible 54 votes held by national parliaments oppose the proposal then it must be reviewed. This is termed a 'yellow card' (see Gilleard, 2011). The UK, Ireland and a collection of relatively new members states have invoked a 'yellow card' against the CCCTB. The Netherlands, Sweden and Malta have also submitted 'reasoned opinions' (comments on the consequences of aspects of the CCCTB). Latvia, Poland, Slovakia and the Czech Republic have variously expressed concern regarding the formula and also harmonization. The CCCTB apportions based on the scale of activity. This creates potential problems for smaller and more volatile economies. Moreover, new members have tended to be sites of relocation of production but are, because of scale and income per capita, less significant as points of sale. As such, the EP proposed (Amendment 16) increasing the weighting of employment and tangible assets to 45% each and reducing sales to 10% (EP, 2012: p. 8). The EC rejected this proposal. Ireland commissioned Ernst & Young to produce its own assessment of the CCCTB (see Cline et al, 2011).

¹⁹ For example, the documents propose that the CCCTB be made mandatory for MNEs. The 2011 directive proposes a voluntary system.

²⁰ As a policy document rather than a piece of analysis the Action Plan puts aside the underlying issues that may account for the path-dependent and conservative approach to change typical of international initiatives. There is a limited pool of expertise to call on in developing highly technical tax regulations. There is significant reliance on people trained by or seconded from the

Moreover, one should not neglect that the EU allows for the preliminary adoption of some proposed new legislation based on ‘enhanced cooperation’. Article 20 in Title IV of the Treaty on the European Union and Articles 326-334 in Title III of the Treaty on the Functioning of the European Union set out the terms of enhanced cooperation (FCO, 2008: 16-17 and 187-190).²¹ A minimum of nine participating members is required to create a functioning unit for some prescribed institutional-policy purpose, such as the implementation of the proposed CCCTB directive. Amendment 6 of the European Parliamentary response to the 2011 EC directive includes a specific recognition that the CCCTB could proceed without unanimity between member states (EP, 2012: p. 3).

As the Action Plan and relaunch state: the EU creates unique scope to introduce unitary taxation that may then spread. The EU is a source of regional legislation that can create a united front. It provides an important platform for something transformational that should not be rejected through conflation with the problem of democratic deficits in EU institutions. The CCCTB seems to be an example of where that deficit has, at least to some degree, provided an opportunity to address one of the major abuses of our time. However, as the 2015 document also states: ‘Ultimately, the key to reforming corporate taxation in the EU [and across the world], to make it fairer and more efficient, is in the hands of member states. Member states need to overcome their differences for the sake of fairness...’ (EC, 2015).

Ultimately, the CCCTB has context in terms of problems of government and governance. Corporate tax avoidance is a legitimacy issue for both states and the EU. If reform allows states to continue to pursue tax competition and MNEs are able to engage in arbitrage then tax policy will contribute to contemporary problems of cynicism and of populism. Brexit, the election of Trump and problems in the EU has many causes but a common sentiment: a deep sense that systems and practices favour the few over the many. The CCCTB offers something potentially transformative. The CCCTB is also important because one increasingly hears that collecting corporation tax has become too difficult and that it should be scrapped. This could easily be counter-productive. Tax is a signal and symbol that speaks to the nature of society. Tax issues may seem technical and so easily neglected on the basis that there are more important matters to be concerned with at the moment. However, to address tax is to address an underlying cause rather than to focus on consequences and symptoms. There is something symbiotic here: public awareness and pressure increase the likelihood that tax policy can be transformative, and that awareness and pressure internalise changes within society that both increase the potential efficacy of initiatives like the CCCTB *and* enhance the legitimacy of the society in which those changes occur.

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Big 4, creating issues of human capital bias (this is what we know and this is where our skills are), group think, capture and conflict of interest. Around £25 billion of the Big 4’s combined annual turnover of approximately £75 billion derives from tax advice.

²¹ The Treaty on the European Union is the 1992 Maastricht Treaty and The Treaty on the Functioning of the European Union is the renamed 1958 Treaty of Rome, both amended as part of the Lisbon Treaty.

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