Tax Losses and Good Tax Governance in Ireland

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Key points:

- Ireland loses over $14bi in tax every year to global tax avoidance. This is equivalent to 22% of its tax revenue per annum.
- The average effective tax rate for foreign-owned multinational corporations was 11.1% in 2020, lower than the 12.5% headline rate.
- The tax loss is equivalent to over 73% of the country's spending on health and over 97% of education spending.

Introduction

The issues of tax transparency and tax regulation are at the centre of current debates on the fairness of tax systems. Where tax havens exist, they are often shrouded in secrecy, a secrecy that facilitates tax evasion. Corruption experts assert that Ireland still has a lot to do to combat endemic corruption in politics and to repair the country's international reputation as a 'lightly regulated economy' (Devitt and Gillanders, 2021). 'Lightly regulated economy' is often a proxy for 'tax haven', which Ireland has often been labelled.

Table 1 – 20 Lowest Statutory Corporate Income Tax Rates in the World, 2020

Country	Continent	Tax Rate
Barbados	North America	5.5%
Uzbekistan	Asia	7.5%
Turkmenistan	Asia	8%
Hungary	Europe	9%
Montenegro	Europe	9%
Andorra	Europe	10%
Bosnia and Herzegovina	Europe	10%
Bulgaria	Europe	10%
Gibraltar	Europe	10%
Kosovo, Republic of	Europe	10%
Kyrgyzstan	Asia	10%
Paraguay	South America	10%
Qatar	Asia	10%
The former Yugoslav Republic of Macedonia	Europe	10%
Timor-Leste	Oceania	10%
China, Macao Special Administrative Region	Asia	12%
Republic of Moldova	Europe	12%
Cyprus	Europe	12.5%
Ireland	Europe	12.5%
Liechtenstein	Europe	12.5%

Source: Tax Foundation (2020).

The tax haven label is normally promptly rejected by national governments offering low corporate taxes. Previous research has identified a high risk of corruption linked to favourable outward tax incentives, which potentially lead to an increased risk of tax avoidance and evasion, as government policy effectively facilitates tax benefits that are lucrative to international companies (Killian, 2006). The Irish government has publicly fought the tax haven tag and argued that the country does not meet international standards for being classified as such and that this labelling is incorrect and misleading (Tobin and Walsh, 2013).

Nevertheless, Ireland has been labelled as a corporate tax haven by multiple academic studies, financial reports, and media accounts mostly due to its favourable corporate tax regime. This includes the controversial 12.5% tax on corporate income. Despite other countries having even lower taxation (see Table 1 above), including other European countries such as Hungary, Ireland is an attractive location for foreign investment. A favourable tax regime is undoubtedly an important reason for this (e.g. facilitated profit shifting, the existence of domestic tax tools providing companies with tax exemptions, tax confidentiality and tax secrecy), but other factors can also play a part: access to the European market, EU membership, English as an official language, rapid institutional adaptation, a good education system and a concentration of large pharma and ICT companies (Tobin and Walsh, 2013). This includes US-based technology firms and, more recently, international investments funds – which, according to specialists, help to sustain the country's infamous title as 'the biggest tax haven for multinationals' (Rusina, 2020; Tørsløv et al. 2018; Ferriter, 2018). The remainder of this paper examines the elements of Ireland's special tax regime that underpin its label as a tax haven as well as the public funding lost to tax avoidance.

Taxation Policy, Tax Haven and Ireland's Reputation

Independently of the terminology used, such as tax haven, offshore centre, non-cooperative jurisdiction, fiscal paradise, what all these terms share is that they facilitate tax avoidance and tax secrecy - with the latter being the biggest enabler of money laundering (European Parliament, 2017). Being labelled a tax haven is seen under a negative light not just because of the potential corruption a country's tax legislation might tolerate as well as unfair competition, but also because tax revenues that could be used to alleviate poverty or spent on welfare programmes are actually lost, therefore representing a substantial loss for society in general.

Tax policy regulation affects the volume and location of foreign direct investment (FDI) (Rusina, 2020; Davies et al., 2021). Countries competing for multinational investment frequently re-examine their tax policies with a view to creating an environment which encourages corporate investment from overseas. The Irish State's flexible response to the needs of FDI have made Ireland a magnet for foreign money, especially U.S. companies. FDI and corporate tax are a central part of Ireland's economic model. Foreign-owned multinationals paid 82% of total net corporate tax in 2020 (€9,657 billion), and accounted for 32% of employment and 49% of employment taxes (Revenue Commissioners, 2021).

Ireland is known for its low headline 12.5% rate, which is half the average OECD's countries corporate tax rate of 24.18% (Tax Foundation, 2017). While the Revenue collected €195.3bn from tax profits reported in 2019, the overall aggregate effective tax rate for foreign corporates was officially lower than the headline rate, at 11.1%. According to the Revenue Commissioners, this rate will always be lower than the statutory rate due to various tax minimisation schemes, such as double taxation relief, and the research and development tax rebate (Revenue Commissioners, 2021).

A significant example of the level of tax relief offered to multinationals is that, in 2015, 13 of the top 100 companies with the highest taxable income had an effective rate of less than 1%. Among this cohort, eight had an effective tax rate of 0% and a further five had an effective rate of less than 1% (Office of the Comptroller and Auditor General, 2017). A more recent example is a subsidiary of Microsoft in Ireland, which recorded a profit of $315bn and paid zero corporate tax in 2020 (Microsoft Round Island One, 2021). This was possible because of the Irish tax arrangement in which companies were allowed to be incorporated in Ireland but tax resident in a low-tax jurisdiction, such as Bermuda. This loophole permitted corporations to reduce (or eliminate) their tax liabilities.[1]

Despite calls from international organisations for transparency on tax transactions, the Irish government has defended its corporation tax rate, arguing that the competitive corporate tax system in Ireland plays a key role in attracting foreign direct investment and, as a small EU country, it needs this fiscal support to remain relevant in the global economy. The report 'A Road Map for Ireland's Tax Competitiveness', published in 2014, is a key document in understanding Ireland's tax policy objectives.[2]

Tax Haven Determinants

But what are the determinants of tax havens in the actual economic context? There is little consensus on a definition of a tax haven and several tax haven lists have been compiled to date by international watchdogs, NGOs and academic researchers. Common features around those lists are that they try to specify criteria, such as practices considered to be unfair, levels of transparency and tax cooperation (European Commission, 2017). While it has been found that low taxation is not enough for a country to receive tax haven status (Mara, 2015), other practices including tax-free profits, high levels of FDI, a large discrepancy between the nominal and average tax rates, tax confidentiality and tax secrecy, have placed Ireland on the majority of tax haven lists. The country is not considered a tax haven by OECD criteria or the European Union list of non-cooperative jurisdictions for tax purposes. Table 2 presents the EU tax blacklist as of 2020.

Table 2 - The EU tax blacklist in 2020

American Samoa	Panama
Anguilla	Samoa
Barbados	Trinidad and Tobago
Fiji	US Virgin Islands
Guam	Vanuatu
Palau	Seychelles

Source: Official Journal of the European Union, The EU list of non-cooperative jurisdictions for tax purposes (2020/C331/03)

While the EU have publicly pushed for increased transparency and exchange of information by applying minimum standards of corporate governance and accountability, they have also been criticised for failing to include notorious jurisdictions such as Hong Kong or Switzerland on the EU tax haven list, as well as completely excluding EU Member States from the list (Transparency International, 2020; Tax Justice Network, 2020). In fact, the EU blacklist focuses on some developing countries 'for not living up to international standards despite them not being at the negotiating table and not having the capacity to implement these standards' (Oxfam International, 2021, p.3). In addition, the EU criteria for blacklisting countries seem to be linked to the commitment of countries to international standards (such as adherence to the Global Forum on Transparency and Exchange of Information for Tax Purposes)[3] rather than to actual harmful tax practices that avoid tax.

However, it is important to note that a report by the European Parliament in 2019 on financial crime called on the European Commission to identify five Member States as EU tax havens: Cyprus, Ireland, Luxembourg, Malta and the Netherlands (European Parliament, 2019). The report underlined the particularly high share of inward and outward FDI as a percentage of the GDP, noting that such high FDI is usually held by special purpose entities (SPEs) that frequently exploit loopholes, and that those countries are facilitating aggressive tax planning globally with a view to reducing the tax burden for companies, and that this could harm the integrity of the European single market (European Parliament, 2019, p. 57). According to Oxfam International (2021), a very high inward FDI relative to a country's economy is usually related to offshore structures.

Despite noting some improvement in terms of the increase in revenue as well as the implementation of measures to limit the scope for tax avoidance in Ireland, a previous report from the European Commission suggests that the country's tax rules are used by companies that engage in aggressive tax planning. In practice, aggressive tax planning means exemptions from withholding taxes on dividend payments made by companies based in Ireland, which may lead to companies evading tax altogether if they are also not subject to tax in the recipient jurisdiction (European Commission, 2018, p.22).

Public Funding Lost to Tax Evasion

Table 3 – Tax losses in Ireland (2020 estimation)

Total annual tax loss	$14,462,658,146
Tax loss per collected tax revenue (%)	22.26%
Annual tax loss due to corporate tax avoidance	$199,121,037
Annual tax loss due to offshore tax evasion	$14,263,537,109
Total tax loss as percent of public health expenditure	73.01%
Total tax loss as percent of education expenditure	93.13%
Effective tax rate	7.76%
Most vulnerable trading channel	Inward foreign direct investments
Trading partner most responsible for vulnerability	Luxembourg, U.S., Netherlands
Corporate tax haven score (2019)	76
Financial secrecy index	24
Share of global offshore wealth	5.6%
Share of global tax loss inflicted on other countries	3.7%
Tax loss inflicted on other countries	$15,830,940,779

Source: Tax Justice Network (2020).

Corporate tax is an important revenue for government finance and is responsible for a large share of total tax revenues in several countries (Cobham and Janský, 2018). International corporations often implement aggressive tax planning in order to avoid tax on investments, going beyond avoidance to the point where a firm evades their tax obligations through violations of tax laws and related regulations (Wang et al., 2019).

The State of Tax Justice 2020 report by Tax Justice Network estimates direct corporate tax losses by analysing the misalignment between the location of profits and the location of productive economic activity revealed in the published aggregated country-by-country reporting data for OECD members. Table 3 presents a summary of Ireland's tax losses. It is important to stress that the data analysis carried out by Tax Justice Network does not clarify whether these taxes would accrue to Ireland if the corporate taxation rate were to be raised.

According to Tax Justice Network (2020), Ireland loses $14,462,658,146 in tax every year to global tax avoidance - which is equivalent to 22% of its tax revenue (tax revenue: $65 billion) - while being responsible for 3.7% of the total global tax loss ($15,830,940,779) of other countries (see further details in Table 3). The social impact of lost tax is also high. The loss is equivalent to 73.01% of spending on health and to 97.13% of education spending. The breakdown of tax avoidance losses shows that $199 million is lost to global tax avoidance carried out by multinational corporations and $14 billion is lost to global tax evasion carried out by private individuals. The country is also vulnerable to illicit financial flows (especially inward FDI) and was given a vulnerability score of 60 (100 is the worst possible score). The report also pointed out that the trading partners most responsible for the vulnerability were Luxembourg, the United States and the Netherlands. The effective tax rate claimed in the report is significantly lower than the one reported by the Revenue, at 7.6%. Table 4 presents the top 10 countries most responsible for global tax losses according to the Tax Justice Network Report (2020).

Table 4 - Top 10 countries most responsible for global tax losses

Country	Tax loss inflicted on other countries	Tax loss inflicted by enabling corporate tax abuse	Tax loss inflicted by enabling private tax evasion	Share of global tax loss responsible for
Cayman Islands	$70,441,676,611	$22,819,899,267	$47,621,777,344	16.47%
United Kingdom	$42,464,646,560	$13,671,390,701	$28,793,255,859	9.93%
Netherlands	$36,371,503,832	$26,593,707,934	$9,777,795,898	8.50%
Luxembourg	$27,607,634,145	$9,283,427,114	$18,324,207,031	6.45%
United States	$23,635,935,547	$0	$23,635,935,547	5.53%
Hong Kong	$21,047,358,012	$16,331,010,356	$4,716,347,656	4.92%
China	$20,045,803,268	$20,045,803,268	$0	4.69%
British Virgin Islands	$16,295,774,429	$10,405,615,250	$5,890,159,180	3.81%
Ireland	$15,830,940,779	$6,068,846,053	$9,762,094,727	3.70%
Singapore	$14,633,842,974	$12,221,060,747	$2,412,782,227	3.42%

Source: Tax Justice Network (2020).

Regarding the corporation tax haven score, which measures how much countries enable corporations in avoiding tax, Ireland is 11th in the ranking, with a score of 76 out of 100. This relatively high score is likely due to the several tax exemptions offered to corporations that do not pay tax or pay a tax rate far lower than the country's standard, a factor that greatly increases a country's score. REITs (Real Estate Investment Trusts), for example, are generally exempt from income tax on their property rental business and from chargeable gains in Ireland (Revenue, 2021). In relation to banking secrecy (i.e. laws that allow bankers to withhold information about the financial affairs of clients under criminal investigation), Ireland ranks 29th (first is the worst), with a financial secrecy score of 48 out of 100. This relatively high level of confidentiality to bank customers - including both natural and legal persons - is likely connected to bank secrecy requirements as established in Irish common law.[4] However, previous research has found that Ireland has a fair degree of financial transparency in other areas, which are important steps towards improving transparency (Cobham and Janský, 2018).

Steps Towards Transparency and Good Tax Governance

Recent steps towards more transparency and good tax governance include the creation of frameworks to increase tax transparency at the international level. The EU has focused, for example, on transparency as a core objective of its tax policies and something that can allow public scrutiny. This aligns with the international tax reform led by the OECD, which is divided into two pillars: 1) the re-allocation of taxing rights to ensure the fairer distribution of profits among countries and 2) minimum effective taxation of the profits of multinationals. In July 2021, 130 countries agreed upon a 15% minimum corporate tax rate (OECD, 2021). Now signatory countries require multinational corporations with revenue over €750 million to provide country-by-country reporting on their profits, numbers of employees, net turnover and corporate taxes paid. Three EU members did not sign the tax deal: Ireland, Hungary and Estonia.

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[1] The ‘double Irish’ tax arrangement finished at the end of 2020

[2] Link to ‘A Road Map for Ireland’s Tax Competitiveness’ report: http://budget.gov.ie/budgets/2015/documents/competing_changing_world_tax_road_map_final.pdf

[3] The Global Forum on Transparency and Exchange of Information for Tax Purposes, created in 2000, is a multilateral agreement for tax transparency and information sharing, involving OECD countries and other jurisdictions.

[4] See an analysis of the Banking Regulation 2021: https://practiceguides.chambers.com/practice-guides/banking-regulation-2021/ireland