CFOC Policy Proposal

CFOC RELEASE AND COMMENT ON THE UK GOVERNMENT'S HISTORIC G7 FINANCIAL MINISTERS AGREEMENT

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Conservative Friends of the Commonwealth
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Following the recent UK led G7 summit, the CFOC policy team, lead by Policy Director Noah Khogali, have written an official CFOC response to the groundbreaking agreement in relation to the introduction of the 15% tax rate for international corporations.

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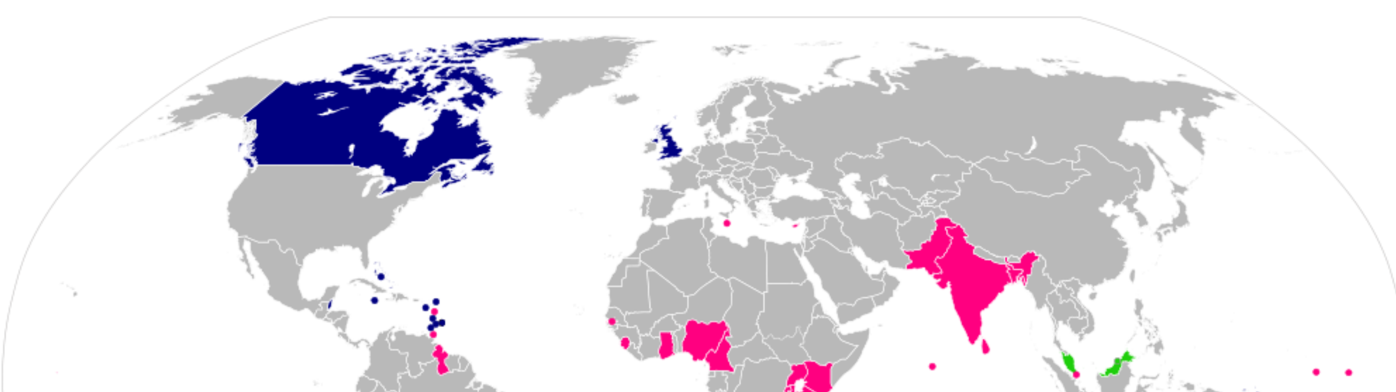

Introduction

CFOC acknowledges and commends the UK Government's efforts to lead the G7 in meaningful reform of the international economic system that has come under huge stress over the past year. It is clear that the sentiment behind these efforts have been overwhelmingly positive, progressive, and forward thinking. However, there are some parts within the policy positions adopted that we at CFOC believe have some scope for improvement in regard to the long-term economic security and prosperity of the UK, with impacts across the Commonwealth as a whole. As highlighted in our contents page above, this paper will provide analysis, critiques and commendations for each of those four main pillars. Below are listed the relevant UK Government releases on the policy concerned:

https://www.gov.uk/government/news/g7-finance-ministers-agree-historic-global-tax-agreement
https://www.gov.uk/government/publications/g7-finance-ministers-meeting-june-2021-communique

Global Tax Reform

The agreements on global tax reform reached at the G7 Finance Ministers meeting consist of two "Pillars" which aim to "tackle the tax challenges arising from an increasingly globalised and digital global economy".

The first "Pillar" is a commitment to ensure that the most profitable multinational organisations pay tax in countries where they operate, rather than simply where their headquarters are based. It would apply to international firms with a 10%+ profit margin, with 20% of income above this 10% margin taxed and split between countries where said organisation operates. The UK Government believes this will provide a valuable boost to UK Government finances, allowing further investment in UK public services.

The second "Pillar" agrees in principle a minimum corporation tax of 15% in all G7 states to ensure "a more level playing field for UK firms and cracking down on tax avoidance". This "Pillar" will be discussed in further detail at the G20 summit in July.

In addition to these main pillars, the G7 discussions also addressed the prospect of Central Bank Digital Currencies (CBDCs), reaffirming that although they have potential to become key parts of the global economic system in the future, that at present, no global project should begin operation until the policy, and most specifically, security implications have been properly assessed.

Overall, the proposed policy seems broadly positive and appeasable.

The first "Pillar" seems a sensible step in the right direction to modernize a tax system which for too long has been unable to properly deal with the realities of a modern international economic system. It will ensure that companies are less able to practice tax avoidance methods, and contribute fairly to the economies in which they operate. One Irish subsidiary of Microsoft is a good example of this, as they paid a total of $0 tax on $315bn of profits. This initiative is a meaningful step in regards to ensuring fairness across the international system and maintaining accountability for "Big Tech" and other large corporations. It prevents corporations from being able to "game the system", moving customers around to avoid paying taxes in many countries.

The second "Pillar" seems less of a positive step. It should be noted here that UK Government documents and publications at present do suggest further development of this policy, so any critiques are purely based on the information currently at hand. It does seem that, beyond the G7, it would not be in the interests of many G20 and developing countries to adopt a minimum corporate tax rate set by the G7 and spearheaded by Washington. If this comes to be the reality, it will greatly hamstring the UK's long term development post Brexit, especially in contrast with the economic opportunities and investments that will likely find their way into countries with a malleable corporate tax rate. It would greatly increase the challenge already faced by the UK Government to encourage international investment and business opportunities if the ability to undercut competitors is removed / limited. This being said, credit must be given to the UK Government especially, that the minimum rate has seemingly been negotiated down from the 21% proposed by President Biden down to 15%. If the UK Government lowers the corporate tax rate to match this 15% figure, then the negative effects of this wider policy position could be mitigated - making the UK the most favourable of the G7 states in terms of attracting international investment. In a similar vein, this could provide an opportunity for developing Commonwealth states who resist becoming signatories to this particular Pillar, allowing them to undercut G7 tax rates and coax investment into their burgeoning economies. Time will tell, but the immediate influx of cash potentially secured by both pillars of tax reform may not sustain that level of income in the long term as companies look to relocate to the likely large number of countries who look to non-agreement as a larger economic opportunity than becoming signatories. It should also be noted that it would be unsurprising, and likely a positive decision, if this pillar was dropped if/when there is not unanimous consensus over it at the G20.

The final discussion on international tax reform featured a brief mention of CBDCs and the potential of a globalised digital currency. The G7 were right to cast the possibility of a global digital currency project out of hand for the time being. At present, the security and privacy concerns are simply too great for such a project to be considered on a global scale - and there are serious concerns about a CBDC project at even a domestic level. Until these concerns are controlled legally and within policy making, there should be no attempt to introduce such a project either internationally or domestically.

Improving Climate Disclosures

G7 finance ministers committed, for the first time, to properly embed mandatory climate change and biodiversity loss considerations, previously voluntary, into corporate decision-making. The UK has already led the way in this area, already committing to do so in November 2020, and by persuading other G7 countries to do the same, this is a major step towards ensuring that the global financial system plays its part transition to net zero as investors better understand how firms are managing climate risks and can allocate finance accordingly.

Using the G7 as the conduit for such a policy was certainly commendable in decreasing inconsistent information across markets, as the Finance Ministers also supported work by the International Financial Reporting Standards Foundation to develop a baseline global standard for high-quality, granular sustainability reporting. By establishing a firm baseline of reporting for climate disclosures, the G7 has, hopefully, overcome the peril of nebulous, substance-lacking reporting which would immediately demolish the objective of setting clear climate considerations for economic decision-making.

Central Banks, the communique outlines, will share learnings on taking climate-related risks into account in their own operations and balance sheets as appropriate, and also calls for further consultation on a final proposal leading to the establishment of an International Sustainability Standards Board ahead of COP26. The establishment of such a board is to be encouraged in its reinforcement of a framework to provide investors with standardised, comparable, and reliable information on climate risks. #

The entire proposal currently lacks a timeframe, which is understandable given its recent genesis, however, there is potential for this to be agreed at the G20 summit in October or COP26 in November. This would be in line with the ambition of Yi Gang, governor of China's central bank.

Supporting Nature and Tackling Environmental Crime

In the vein of adapting the modern international economy for the 21st Century political and social arena, it was of the utmost importance that the G7 take meaningful steps to both support nature and tackle environmental crime. The decision was taken to launch a task force, mirroring the already existing TCFD who would be given the power and resources "to crack down on the proceeds of environmental crimes by introducing and strengthening central company beneficial ownership registries". The UK currently operates with a public beneficial ownership registry and has done so since 2016.

This agreement seems overwhelmingly positive - it extends a key facet of UK policy across the rest of the G7 and will be instrumental in both ensuring transparency and accountability for not only environmental crimes, but other criminal enterprises. It ensures that investors, the public and the government are kept informed and educated on key sustainability issues. This will be taken to the G20 in due course, but it is also the opinion of CFOC that there should be considerations given as to the possibility of such a program being extended across the Commonwealth as well.

Support for Vulnerable Countries

The G7 nations boast 40% of the world's GDP, making it one of, if not the most, significant international groups in the world in relation to how much real power it wields when acting unanimously. In relation to support for vulnerable countries in recovering from Covid-19, SDR's (Special Drawing Rights) have already been provided with a $650 Billion budget, and this most recent G7 has stated they will look to channel some of this money into supporting health needs; specifically vaccinations, and other means of promoting a more green and sustainable way to grow vulnerable national economies post pandemic. Debt vulnerabilities were also outlined as a key point of the G7 summit as an issue for vulnerable nations. The G7 have stated they want to establish a 'loan by loan' basis of lending to vulnerable economies and promote greater transparency in lending; something the G7 will take to the G20 and seek to get greater support in implementing. The G7 also called on the world's bank and the IMF to use their economic capital to help poorer nations attain Covid vaccinations, in addition to stating they would ask the private sector to play their part also. Finally, the finance ministers of the G7 have agreed that more must be done now in relation to investment against health risks, such as preventing antimicrobial resistance to antibiotics. The issue of 'loan by loan' is clearly a tightening of the money supply to vulnerable nations, with each loan needing to be justified and ratified by the lenders before it is issued. Although this will prevent debt being accumulated through higher risk spending, it will naturally provide more red tape for these vulnerable nations in their access to loans. A possible consequence of this could be that vulnerable nations turn to private investors that are willing to accept higher risk if they get better returns, meaning G7 and private sector partners that instigate 'Loan by Loan' red tape could lose influence and actually lead to vulnerable nations becoming indebted to private sector lenders taking higher returns for their acceptance of their higher risk; a possible result of vulnerable nations being in need for money and not being able to wait for the 'Loan by Loan' process due to time constraints and other issues this process would possibly introduce. That said, it is a preempted issue and one that could be easily adapted to if it proves to be an issue, with efficacy of the system being able to be improved as it becomes implemented.

Closing Remarks

Overall, CFOC welcomes much of the sentiment behind the agreements made at the G7 and believes that, broadly, the agreements represent a positive step in the right direction to modernize the international economy, readying it for not only a post-Covid world, but an increasingly digitized and environmentally aware one.

Nevertheless, we express some concerns on the topic of long term globalised CBDCs and the long-term implications of a minimum corporate tax rate of 15%, especially if takeup outwith of the G7 isn't unanimous. If this turns out to be the case, it would likely not be in the best interest of the UK to continue with that minimum rate.

Nevertheless, the agreement as a whole should serve as a strong indication that the UK Government has the best interests of the international community in mind, representing a commitment to fairness and justice internationally.