

Swiss Corporate Tax Reform and Mobile Firm Profits

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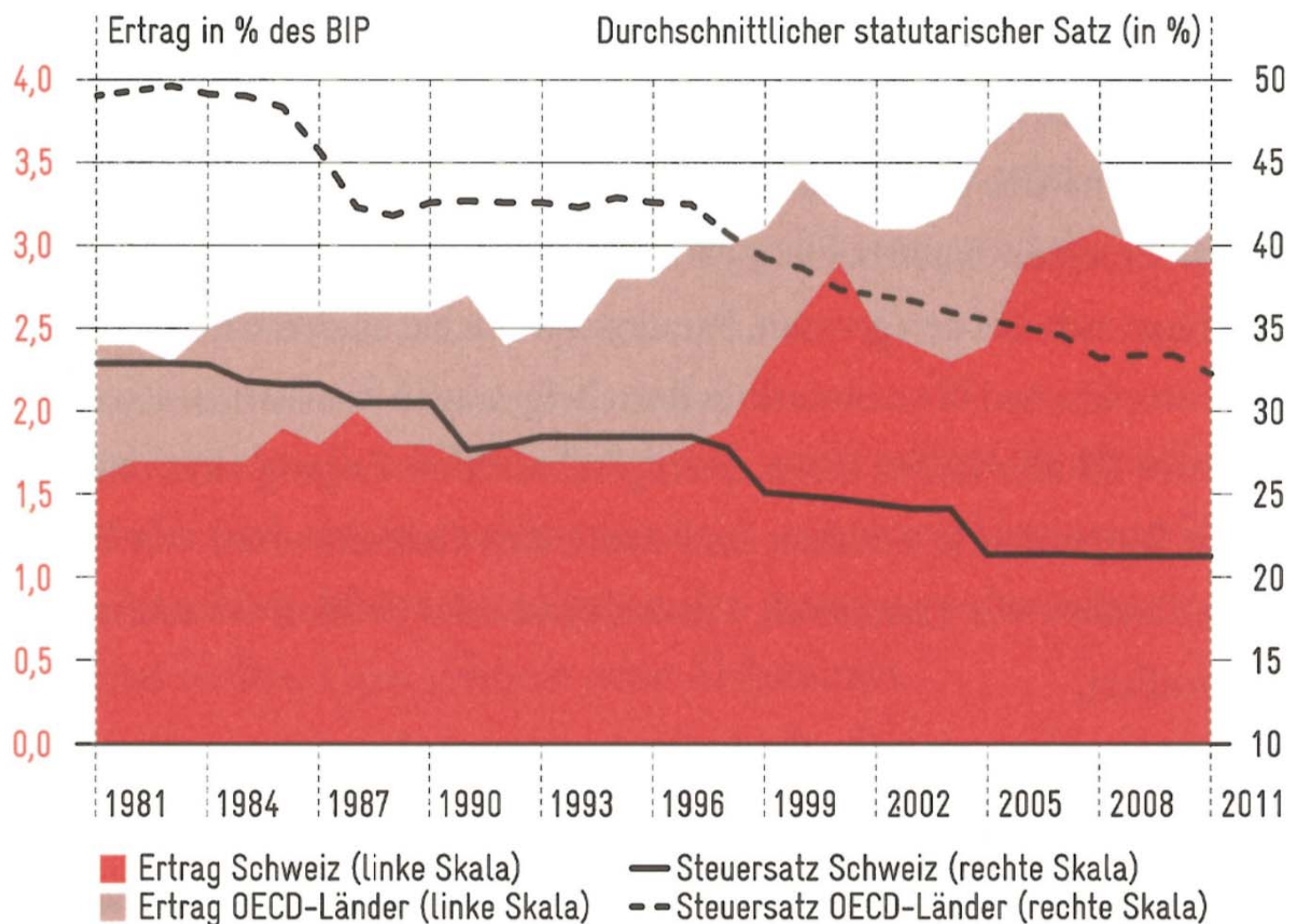
21 February 2019

The logo for UNIL, featuring the word "Unil" in a stylized, blue, cursive script.

UNIL | Université de Lausanne

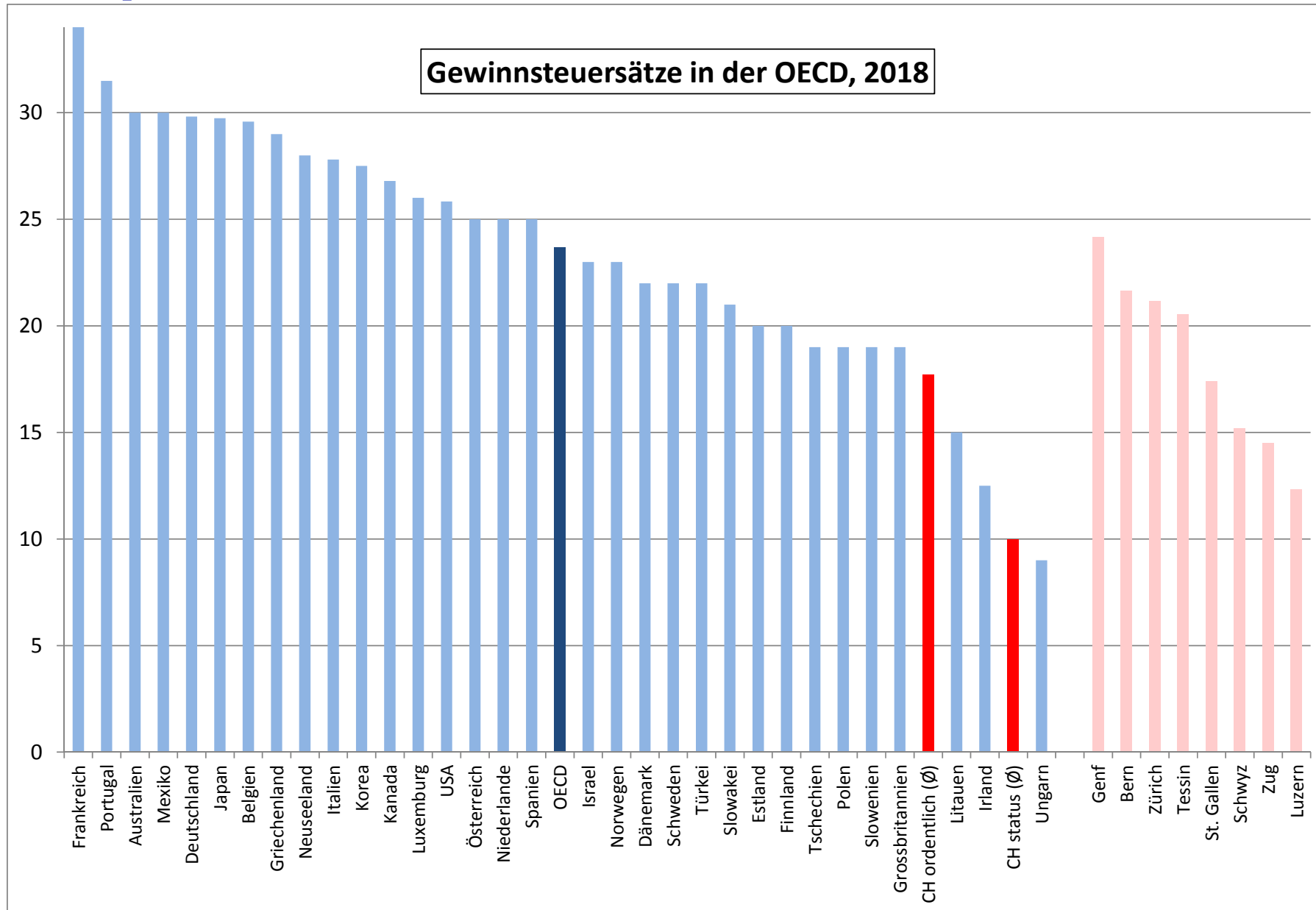
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Corporate tax around the world: Falling tax rates, rising tax revenues



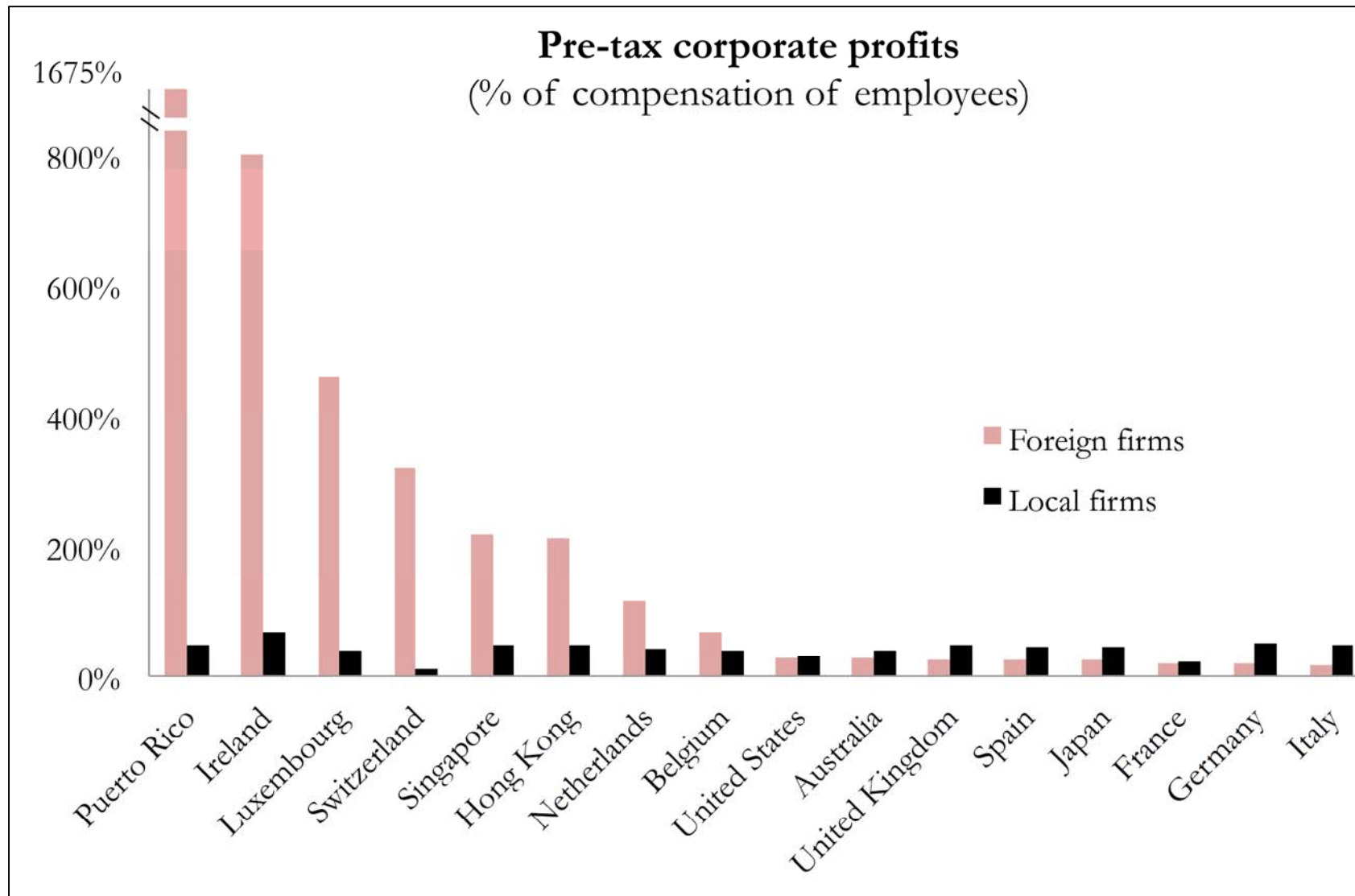
Source:
Salvi and Zobrist, Avenir Suisse, 2013

Corporate tax haven Switzerland



Sources:
OECD Tax
Database; KPMG
Swiss Tax Report
2018

Switzerland is a major beneficiary of profit shifting by multinational firms (1)



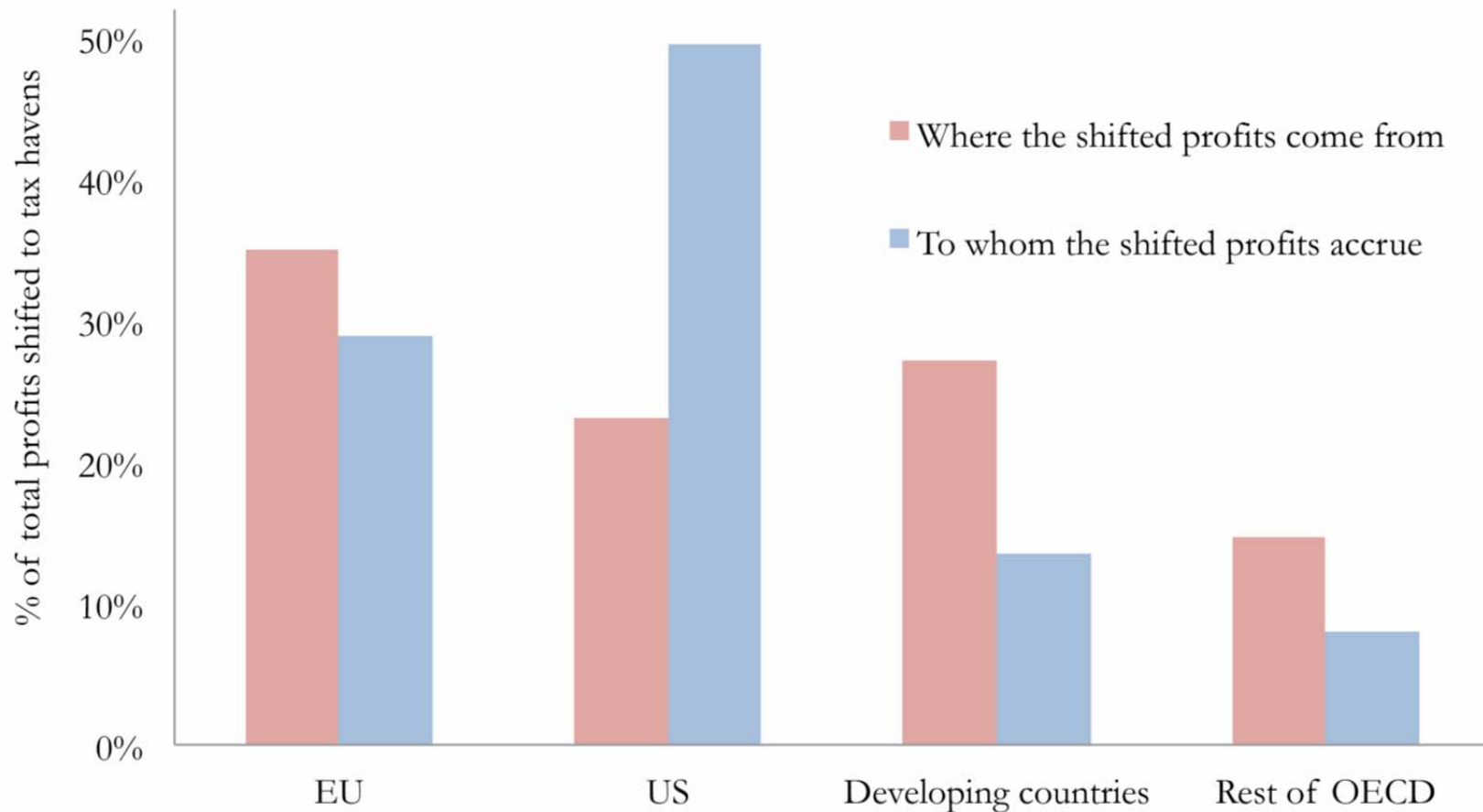
Source:
 Tørsløv, Wier &
 Zucman (2018)

Switzerland is a major beneficiary of profit shifting by multinational firms (2)

	Reported pre-tax profits	<i>Of which: Local firms</i>	<i>Of which: Foreign firms</i>	Shifted profits
Belgium	80	48	32	-13
Ireland	174	58	116	-106
Luxembourg	91	40	51	-47
Malta	14	1	13	-12
Netherlands	195	106	89	-57
Caribbean	102	4	98	-97
Bermuda	25	1	25	-24
Singapore	120	30	90	-70
Puerto Rico	53	10	43	-42
Hong Kong	95	45	50	-39
Switzerland	95	35	60	-58

Source:
Tørsløv, Wier &
Zucman (2018)

Profits shifted mainly from EU and developing countries



Source:
Tørsløv, Wier &
Zucman (2018)

The central challenge of Swiss corporate tax reform

How can canton-level corporate tax preferences for multinational firms be eliminated with a minimum of revenue loss?

New uniform corporate tax too high

⇒ revenue losses on formerly preferentially taxed profits (profit shifting away from Switzerland)

New uniform corporation tax too low

⇒ revenue losses on „normal“ firms (windfall gain for domestic firms)

The geeky approach

$$\text{Tax Revenue} = \text{Tax Rate} * \text{Profits}(\text{Tax Rate})$$

$$\Delta \text{ Tax Revenue} = \Delta \text{ Tax Rate} * (1 + (\Delta \text{ Profits} / \Delta \text{ Tax Rate}))$$

$$= \Delta \text{ Tax Rate} * (1 + e)$$

$$= \text{Share}_{\text{domestic}} * \Delta \text{ Tax Rate}_{\text{domestic}} * (1 + e_{\text{domestic}})$$

$$+ \text{Share}_{\text{multi}} * \Delta \text{ Tax Rate}_{\text{multi}} * (1 + e_{\text{multi}})$$

⇒ central importance of the *elasticity* of taxable profits

2016: Corporate Tax Reform III

No official revenue projections were published.

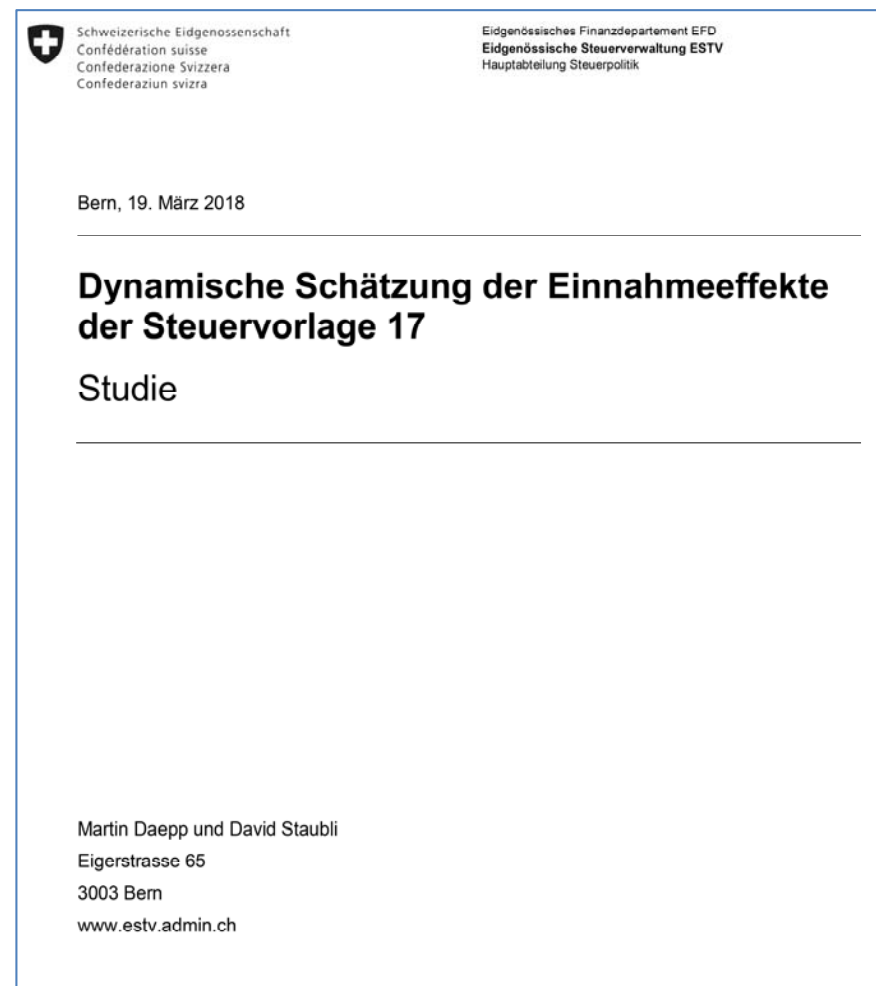
⇒ Suspicion of unnecessarily generous tax cut

⇒ rejected by 59% of voters on 12 February 2017

Revised corporate tax reform (SV17)

Detailed revenue projections by
Swiss Federal Tax Administration

- Dynamic simulations based on estimated tax-base elasticities and assumed changes in corporate tax rates abroad
- estimated Semi-elasticities:
 $e_{\text{multi}} = -10; e_{\text{domestic}} = -2$
- + « induced effects » (changes in revenue from other taxes)



Estimated revenue effects

(consolidated tax revenue confederation + cantons + municipalities; changes in CHF bn per year; scenario with social insurance contributions weighted by 10%)

	SV17		Elimination tax preferences w/o other measures		SV17 w/o patent box		SV17 w/o Δ foreign rates	
	<i>static</i>	<i>dynam.</i>	<i>static</i>	<i>dynam.</i>	<i>static</i>	<i>dynam.</i>	<i>static</i>	<i>dynam.</i>
Δ revenue:								
Domestic f.	-4.49	-3.39	-0.38	-0.78	-4.06	-3.19	-4.49	-2.76
Multinationals	+2.29	+2.66	+8.17	+0.55	+2.86	+2.60	+2.29	-0.33
...Total	-2.20	-0.73	+7.79	-0.23	-1.20	-0.59	-2.20	-3.09
Induced effects		+1.28		-0.44		+1.00		+1.94
...Total		+0.55		-0.66		+0.40		-1.15

⇒ Overall effect highly uncertain, but revised reform probably less costly than elimination of tax preferences without other measures

The parliament's proposal („STAF“)

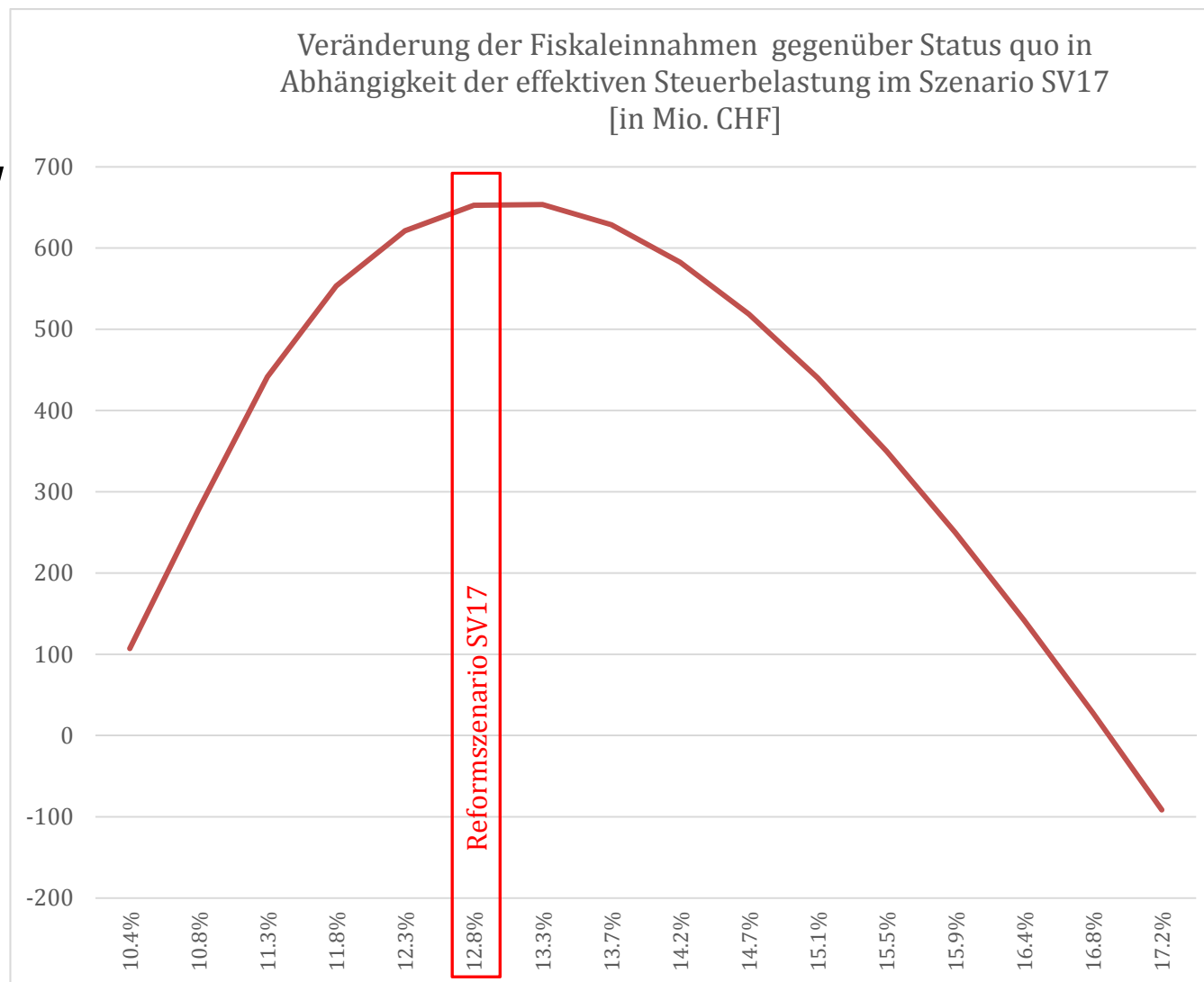
- **Federal parliament:** CHF 2 bn revenue loss through corporate tax reform compensated by CHF 2 bn for social security system („social compensation“)
- **Problem:** Social security contributions financed to a considerable extent by workers themselves
- My **back-of-the-envelope calculation of the distributional effects** within Switzerland:

	SV17		Social security reform
	static	dynamic	
Top-10%	+1.9	+0.7	-0.8
Bottom-90%	-1.9	-0.6	+0.7

in CHF bn per year, see www.batz.ch

Canton-level tax reforms (1)

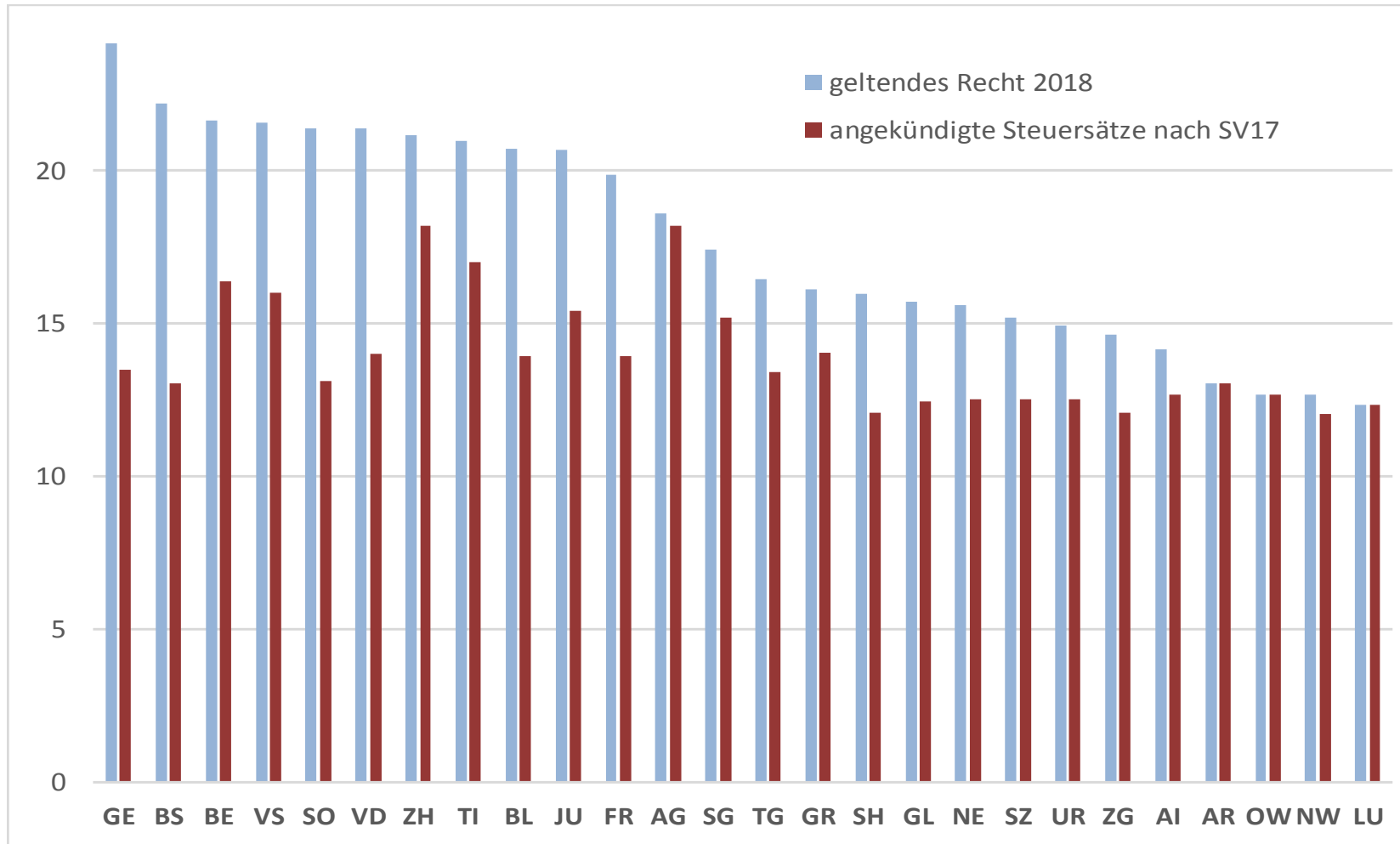
- SV17 only presents new legal framework (new preferential taxes for certain types of firms)
- Cantons have to adjust their tax rates to the new framework
- Political pressure for large tax cuts (windfall gains for domestic firms)



Source: ESTV

Canton-level tax reforms (2)

Are planned tax cuts excessive?



Source:
Botschaft zum
Steuergesetz über
die Steuervorlage
17 (EFD, March
2018)

Tax reform also affects fiscal equalisation

Source: Brühlhart and Schmidheiny (*Die Volkswirtschaft*, 2019)

Ressourcenindex



Ein-/Auszahlungen inkl. Ergänzungsbeitrag (absolut)



Ein-/Auszahlungen inkl. Ergänzungsbeitrag (pro Einwohner)



BRÜLHART UND SCHMIDHEINY (2018) / DIE VOLKSWIRTSCHAFT

Conclusions

- Reported profits of multinational firms are highly mobile and sensitive to corporate taxation
 - Employment, investment, and taxable profits of domestically oriented firms are much less mobile and sensitive to corporate taxation
- ⇒ Policy trade-off between international fiscal competitiveness and safeguarding of corporate tax revenue

The federal administration has now published careful estimates.

Corresponding analyses should be conducted by cantons for the determination of their optimal responses to the changed fiscal and legal context (including effects of fiscal equalisation).