OXFORD UNIVERSITY CENTRE FOR BUSINESS TAXATION

1^{st} SUMMER SYMPOSIUM 2007

PROGRAMME

Saïd Business School
25^{th} to 27^{th} June 2007

Monday 25 June

8.30 -9.00	**Registration**	Reception area

Session 1 Chair: **Michael Devereux** (Centre for Business Taxation)

9.00 – 10.00	**Peter Egger** (Munich and IFO), *Saving taxes through plant ownership* with Wolfgang Eggert (Paderborn) and Hannes Winner (Innsbruck) Discussant: **Julian Alworth**	Edmund Safra Lecture Theatre
10.00 – 11.00	**Alfons Weichenreider (**Frankfurt**),** *What determines the use of holding companies and ownership claims?* with Jack Mintz (Toronto) Discussant: **Harry Grubert** (US Treasury)	Edmund Safra Lecture Theatre
11.00	**Coffee**	Seminar Room A
1.00	**Lunch**	Seminar room A
3.30	**Tea**	Seminar Room A

Session 2 Chair: **Peter Birch Sorensen** (Copenhagen)

4.00 – 5.00	**Roger Gordon** (San Diego) *An Agency-Cost Model of Dividends, Repurchases and New Equity Issues*, with Martin Dietz Discussant: **Soren Bo Nielsen** (Copenhagen)	Edmund Safra Lecture Theatre
5.00 – 6.00	**Douglas A. Shackelford** (North Carolina) *Capital gains taxes and stock return volatility* with Zhonglan Dai (Texas), Harold H. Zhang (Texas) Discussant: **Harry Huizinga** (Tilburg)	Edmund Safra Lecture Theatre
7.30	**Dinner – St Edmund Hall**	St Edmund Hall, Queens Lane

Tuesday 26 June

Session 3 Chair: **Chris Evans** (ATAX, New South Wales)

9.00 – 10.00	**Rosanne Altshuler** (Rutgers), **Harry Grubert** (US Treasury) *Corporate taxes in the world economy: reforming the taxation of cross-border income* Discussant: **Reuven Avi-Yonah** (Michigan)	Edmund Safra Lecture Theatre
10.00 – 11.00	**Richard Vann** (Sydney) *Problems in international division of the business income tax base* Discussant: **George Zodrow** (Rice)	Edmund Safra Lecture Theatre
11.00	**Coffee**	Seminar Room A
1.00	**Lunch**	Seminar Room A
3.00	**Tea**	Seminar Room A

Session 4 Chair: Julian Alworth

3.30 – 4.30	**Ron Davies** (Oregon) *Tax Competition for International Producers and the Mode of Foreign Market Entry* with Helmut Egger (Zurich), Peter Egger (Munich, IFO) Discussant: **Christian Keuschnigg** (St Gallen)	Edmund Safra Lecture Theatre
4.30 – 5.30	**Clemens Fuest** (Cologne) *Corporate tax policy and international mergers and acquisitions – is the tax exemption system superior?* with Johannes Becker (Cologne) Discussant: **David Weisbach** (Chicago)	Edmund Safra Lecture Theatre
6.00pm	**Punting on River Cherwell** (not compulsory)	
7.30pm	**Barbecue, Cherwell Boathouse**	

Wednesday 27 June

Session 5 Chair: **Judith Freedman** (Oxford)

9.00 – 10.00	**Eckhard Janeba** (Mannheim) *The globalization of tax policy: what German politician believe* with Friedrich Heinemann (ZEW Mannheim) Discussant: **Michael Devereux** (Centre for Business Taxation)	Edmund Safra Lecture Theatre
10.00 – 11.00	**Miranda Stewart** (Melbourne) *Tax Law and Political Institutions* Discussant: **David Wildasin** (Kentucky)	Edmund Safra Lecture Theatre
11.00	**Coffee**	Seminar Room A
1.00	**Lunch**	Seminar Room A
3.30	**Tea**	Seminar Room A

Session 6 **Chair: Christian Keuschnigg** (St Gallen)

4.00 – 5.00	**Alan Auerbach** (UC Berkeley), **Rosanne Altshuler** (Rutgers) *The sources of US corporate net operating losses* with Michael Cooper and Matthew Knittel (US Treasury) Discussant: **Thiess Buettner** (Munich)	Edmund Safra Lecture Theatre
5.00 – 6.00	**Ruud de Mooij** (Erasmus, Rotterdam and CPB) *Corporate tax policy, entrepreneurship and incorporation in the EU* with Gaëtan Nicodème (European Commission) Discussant: **Peter Birch Sorensen** (Copenhagen)	Edmund Safra Lecture Theatre

ABSTRACTS

Session 1

Peter Egger (Munich and IFO), Wolfgang Eggert (Paderborn), Hannes Winner (Innsbruck)
Saving taxes through plant ownership

This paper analyzes to which extent foreign plant ownership involves lower tax payments than domestic plant ownership. We employ a model of endogenous foreign subsidiary ownership to derive a set of empirically testable hypotheses about the differential taxation of foreign- and domestically-owned subsidiaries. We assess these hypotheses in a data- set of 33,577 European foreign- and domestically-owned manufacturing plants. We identify a significant tax-saving of endogenous foreign owner- ship. On average, foreign owners pay 594 Euros per employee or about 56 percent less than domestic owners of similar subsidiaries. This effect is larger in thinner markets with fewer plants, in markets with a greater relative presence of foreign owners, and for foreign owners of larger plants.

Alfons Weichenreider (Frankfurt), Jack Mintz (Toronto)
What determines the use of holding companies and ownership claims?

The paper investigates the role of holding companies and conduit entities in German inbound and outbound FDI. It identifies the relevant conduit countries that act as stepping stones. Several tax and non-tax factors for the set-up of indirect structures are empirically identified. Withholding taxes, credit systems in capital exporting countries and the possibility of group consolidation are shown to be empirically important for the design of ownership chains in foreign direct investment.

Session 2

Roger Gordon (San Diego), Martin Dietz
An Agency-Cost Model of Dividends, Repurchases and New Equity Issues

This paper develops an agency-cost model of firm financial policies, building on the intuition in Easterbrook (1984) and Jensen (1986). Agency costs arise when managers gain by investing available cash even when doing so lowers share values. Dividends then restrict the cash available to managers. While there is empirical evidence linking free cash flow and dividends, a formal model is missing. We show that an agency-cost model can explain not only the use of dividends but also a long list of other stylized facts about firm financial policy. Even under the most optimistic assumptions, however, capital investment remains inefficient, and is sensitive to free cash flow.

Zhonglan Dai (Texas), Douglas A. Shackelford (North Carolina), Harold H. Zhang (Texas)
Capital gains taxes and stock return volatility

We demonstrate that capital gains tax changes inversely affect stock return volatility. A capital gains tax cut reduces the risk sharing between investors and the government and increases stock return volatility. The tax effect on return volatility also differs depending upon the characteristics of stocks such as dividend distribution and embedded capital gains and losses. Using the Tax Relief Act of 1997, we empirically show that the return volatility of the market index, industry portfolios, and individual stocks increases after the capital gains tax cut. Furthermore, higher dividend-paying stocks experience smaller increase in return volatility than lower dividend-paying stocks and stocks with large embedded capital gains and losses see larger increase in return volatility than stocks with small embedded capital gains and losses.

Session 3

Rosanne Altshuler (Rutgers), Harry Grubert (US Treasury)
Corporate taxes in the world economy: reforming the taxation of cross-border income

Proposals for the reform of the taxation of cross-border income are evaluated within the general context of the corporate tax in an open economy. We focus on the various behavioral decisions that can be affected such as the location of income and its repatriation. The two income tax proposals considered are: (1) dividend exemption and (2) burden neutral worldwide taxation in which all foreign subsidiary income is included currently in the U.S. worldwide tax base, and at the same time the corporate tax rate is lowered and overhead allocations to foreign income are eliminated so as to keep the overall U.S. tax burden on foreign income the same. We also consider the attractiveness of destination-based and origin-based consumption taxes. Our evaluation of reform options makes use of the best available information. We also present new information on the burden of the current system. However, there are many important unknown behavioral parameters required to judge international tax systems and this missing information, some of which may ultimately be unknowable, makes it difficult to make definitive recommendations.

The burden neutral worldwide option seems to offer greater efficiency gains among the two income tax options, particularly because of reduced incentives for income shifting which wastes resources and distorts effective tax rates on investment. To be sure, the burden neutral worldwide option would increase effective tax rates on investment in low-tax countries while not increasing the average U.S. tax rate on foreign source income. The option requires a substantial reduction in the U.S. corporate tax rate. We suggest that increased capital mobility makes changing the mix of corporate and personal level taxation of business income appropriate even apart from the special issues of cross-border taxation such as repatriation taxes and income shifting opportunities that are the main subject of the paper.

Richard Vann (Sydney)
Problems in international division of the business income tax base

This article seeks to assess why current transfer pricing rules are the source of tax avoidance and to explore some possible remedies. To do this the article first places transfer pricing rules in the overall context of the international division of the income tax base in the common situation where a widely held corporate group operating in several countries derives business income. The purpose is to show why transfer pricing is the dominant international issue as compared to corporation and shareholder or residence and source taxation. The article then identifies that it is structural issues in transfer pricing rules which are the main drivers of tax planning, not difficulties of finding appropriate prices. Identifying the causes of tax planning in turn suggests possible solutions. The theory, or rather theories, of the firm stemming from the work of Coase provide the backdrop to the analysis.

Session 4

Ron Davies (Oregon), Helmut Egger (Zurich), Peter Egger (Munich, IFO)
Tax Competition for International Producers and the Mode of Foreign Market Entry

This paper studies tax competition between two countries for an international producer. The international producer chooses where to locate its headquarters and whether to serve the overseas market through exports or foreign direct investment (FDI) and local supply. We show that, in the absence of tax competition, the international firm may choose FDI even though this has welfare costs from a global point of view. With tax competition, the parent country's tax is pinned down, allowing the host country to use its tax rate to enforce exporting instead of FDI. This leads to a Nash equilibrium in the tax setting game which is associated with higher world welfare than the no-tax situation. Thus, because of the effect on entry mode, tax competition provides heretofore unexplored benefits.

Clemens Fuest (Cologne) and Johannes Becker (Cologne)
Corporate tax policy and international mergers and acquisitions – is the tax exemption system superior?

In this paper we ask whether recent claims that the US government should switch from the tax credit system to the exemption system are justified. We study corporate taxation in a model where international capital flows are either greenfield investment projects or acquisitions of existing firms, and where investment is motivated by either cost reduction or market entry reasons. The paper asks how corporate taxation affects the international allocation of capital under different double taxation regimes. We find that the standard view on international taxation only prevails in the case of cost driven greenfield investment. In all other cases the deduction system is no longer optimal from a national perspective and the foreign tax credit system fails to ensure neutrality. However, the desirability of the tax exemption system has to be qualified. We show that the cross border cash flow tax system dominates the exemption system in terms of optimality properties.

Session 5

Eckhard Janeba (Mannheim)
The globalization of tax policy: what German politicians believe

The process of globalization has an important impact on national tax policies. The large (theoretical and empirical) literature on taxation of capital in open economies attests to this. For the most part the literature does not focus directly on the political decision making process and assumes that the desired and implemented tax policy is responding to objective underlying tradeoffs. Based on a survey of members of German national parliament we challenge this notion. In fact we uncover systematic differences in the perceived international mobility of tax bases (real and paper profits), which are correlated with party affiliation, education and parliamentary committee membership. A preference for redistribution correlates with the perceived efficiency costs of taxation. These observations suggest that observed tax policy choices do not allow us to easily deduce the preferences of the median voter in the population or parliament and empirical tests of tax competition may need to be reevaluated.

Miranda Stewart (Melbourne)
Tax Law and Political Institutions

Tax law and politics are intimately connected. For centuries, theorists of the state have observed that the power to collect revenues is a central feature of sovereignty or statehood. Since Schumpeter's theory of the *TaxState* (1918, 1954), a body of literature that has been termed fiscal sociology, or fiscal politics, has considered the need for revenues as being a central and defining feature of the state and raising taxes as the most basic task of the state (Campbell, 1993; Gould and Baker, 2002).

Theorists have posed two main questions: first, what is the impact of attempts to impose, or reform, taxation on the development of political institutions; and, second, what is the impact of political and other state institutions on attempts to reform taxation? A third question is: how to improve tax policy and law-making, with the goals of improving both tax law and governance outcomes? A significant international body of historical, legal, political and economic research produced in the past few decades has sought to answer these questions (Levi, 1988; Peters, 1991; Steinmo, 1993; Sandford, 1993; Hale, 2002; Eccleston, 2004). This volume presents new research that contributes to our understanding of all three questions.

Session 6

Rosanne Altshuler (Rutgers), Alan Auerbach (UC Berkeley), Michael Cooper and Matthew Knittel (US Treasury)
The sources of US corporate net operating losses

Recent evidence has shown that the U.S. corporate sector experienced a sharp increase in the magnitude of non-deductible tax losses beginning in the 1990s, a development that, in the aggregate, cannot be explained by cyclical factors or by the overall level of profitability. Using panel data on the actual tax returns of U.S. corporations, we investigate the sources of this surprising trend and relate it to alternative possible explanations, including shifts in industrial composition, the rise in multinational activity, changes in the age structure and size distribution of firms, and increases in the volatility of corporate returns and corporate growth rates.

Ruud de Mooij (Erasmus, Rotterdam and CPB), Gaëtan Nicodème (European Commission)
Corporate tax policy, entrepreneurship and incorporation in the EU

In Europe, declining corporate tax rates have come along with rising tax-to-GDP ratios. This paper explores to what extent income shifting from the personal to the corporate tax base can explain these diverging developments. We exploit a panel of European data on firm births and legal form of business to analyze income shifting via increased entrepreneurship and incorporation. The results suggest that lower corporate taxes exert an ambiguous effect on entrepreneurship. The effect on incorporation is significant and large. It implies that the revenue effects of lower corporate tax rates –

possibly induced by tax competition – partly show up in lower personal tax revenues rather than lower corporate tax revenues. Simulations suggest that between 10% and 17% of corporate tax revenue can be attributed to income shifting. Income shifting is found to have raised the corporate tax-to-GDP ratio by some 0.2%-points since the early 1990s.

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