Things are changing after all

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Abstract

The global situation is getting more difficult every year. While states fortunately agreed on the SDGs and on a climate contract in New York and Paris at the end of 2015, the situation is deteriorating with a fast growing world population and increased environmental pressures. Is there still a chance for a sustainable future or will we end up in a world two-class society or an ecological disaster? At first sight, sustainability might seem a hopeless task, but there is still a chance. Because, following the world financial crisis, the coordination between states has increased considerably. This concerns the overall idea of green and inclusive economies, replacing free market and market fundamentalistic paradigms, even on the OECD level. Encouraging is a concentration on aspects of balance concerning income, and even more attacks on aggressive tax avoidance schemes and tax havens. Details are given in the paper.

1. Initial Situation

In the context of globalization and in the face of many international problems the world is not in an easy situation. With regard to global governance, in particular, progress is not as fast as we might want it to be. However, some progress has been made. Ten years ago, for example, the issue of adequate taxation of cross-border economic activities was an ongoing problem which seemed to be intractable. Not even in the EU was it possible to create change for the better, among other things because of the attitude of Luxembourg and Austria. Both normally used Switzerland and Liechtenstein as their excuse, on the grounds that for reasons of competition there was nothing they could do until these countries made some changes. In their turn Switzerland and Liechtenstein always argued that they were not prepared to do anything until the EU had clarified its internal problems with Luxembourg and Austria.

Until the global financial crisis, the standard attitude was the market-fundamentalist propaganda that the financial market was the “brain” of the world economy and that only it was capable of the optimal allocation of scarce resources.”
it was capable of the optimal allocation of scarce resources. Governments and politicians were not to interfere in this. Any kind of strict regulation and taxation of these processes would burden the intelligence of the “global financial brain”, and the free market was the solution to all problems. The IMF and the World Bank argued along the same lines. With the Washington Consensus aid to poorer countries was made conditional on them pursuing a neo-liberal course. These recipes have turned out to be disastrous in some respects. As soon as the financial crisis broke out, the rich countries, headed by the USA, took the very actions which had previously been prohibited to developing countries.

The crisis was a severe burden on many countries and put the Eurozone under extreme pressure. The crisis is not over yet, but it is remarkable how the discussion has changed during this period. This is especially true with regard to the question of tax haven and tax compliance, as well as to “harmful” competition between countries in the form of very low taxation of cross-border activities. The availability of CDs with incriminating data on systematic tax fraud has come to play a decisive role in this process, too.

Major changes have now taken place in relation to themes which we, not only in the Club of Rome, the Global Marshall Plan Initiative and the Senate of Economy, have always promoted as representatives of a global eco-social market economy. We have turned out to be right, and we should remember this with regard to other topics for the future, too.

2. The pressure on tax havens has grown enormously

What has happened? The pressure on tax havens has grown enormously. The critical attitude in the US and in Europe towards this topic has intensified significantly. Not least because, for one reason, so-called ‘tax-CDs’ smuggled out of the country have made it clear that members of the ‘elite’ and top leaders in all countries have for years and decades systematically committed tax fraud on an incredibly large scale. This was not the result of carelessness, but precisely planned and implemented with great consistency.

3. Automatic Data Exchange

As a result Switzerland has now revised its ‘business model’. As before, private investors are in part still able to avoid the consequences of this change of policy by entrusting their money to professional financial management companies, but with respect to assets in private bank accounts the situation is now very different. We are moving in the direction of automatic data exchange between the banks and financial authorities of individual states, and Switzerland is participating in this process. If it was unable to inform the persons involved about upcoming legal requirements in any other way the country recently even placed sensitive information about account data on the Internet. At an earlier stage account holders had been called on to either reveal their accounts to the finance authorities in their country of residence, or authorize the Swiss bank to do this itself. If this was not implemented, accounts were closed. In the OECD there has been significant progress towards an agreement on automatic exchange of data, and 50 states have already committed to this.

4. Austria abolishes confidentiality in banking

Austria, too, has now done away with its controversial banking confidentiality. The coalition government consisting of the Social Democratic Party of Austria (SPÖ) and the
Austrian People’s Party (ÖVP) achieved the two-thirds majority required in the Austrian Parliament with the votes of the opposition Greens.

By abolishing banking confidentiality, the Austrian government expects additional income from the taxation of capital gains of around 700 million euros per year via greater control options. A central register is to be introduced for this, in which all of the approx. 20 million accounts in financial institutions in Austria are recorded.

“We do not want banking confidentiality to be abused any longer,” was the reasoning for the reform. Tax fraud is theft from society. The requirements for account access are reasonable suspicion and the approval of a judge in the Austrian Federal Finance Court.

Part of the comprehensive reform is an increase in the top tax rate from 50 to 55 per cent for income of one million euros and above. The tax on capital gains will increase to 27.5 per cent, while it stays at 25 per cent for interest on savings accounts (see Handelsblatt, July 8, 2015 no. 128, p 9).

5. Taxation of cross-border economic activity

A second major issue is cross-border economic activity. In particular this is aimed at aggressive tax planning by companies such as Google, Amazon and Facebook, which essentially do not pay any taxes at all. Their approach takes advantage of competition between countries, the lack of transparency in the case of internal transfers within companies, and the possibility of involving intermediaries as well as the multiple transformation of legal conditions (so-called “wrapping”). The OECD is working on all these issues, together with the G20. Together both organizations are investigating the whole complex of cross-border activities and their taxation. Tangible progress is expected in this field.

6. Calling free-trade into question

In the context of the discussions on the planned trans-Atlantic free trade agreement (TTIP) it is interesting that it is now being pointed out (Handelsblatt 06.18.2015) that as early as 2004 Paul Samuelson, the late doyen of market-based economics in the United States and Nobel laureate in economics, shocked the representatives of doctrinal purity with the statement that “Free trade could cause lasting economic damage”. Recently former US Treasury Secretary Larry Summers wrote: “The era of free trade agreements in the classic sense is over. Further agreements can no longer simply be justified by the knee-jerk assumption that free trade is always a good thing.” In fact, the general preferability claimed for free trade with reference to Ricardo has never been universally applicable, and specific conditions are required for it to succeed. Ricardo himself was aware of this. However, the “free-trade fanatics” tended to ignore or conceal this aspect of the doctrine.

7. More transparency with regard to property in Switzerland

Piketty¹ and his student Zucman² address high transparency in the area of property as one of the reasons that taxation is not possible or cannot be implemented in some cases. Several thousand billion dollars have also been missing in international capital export budgets for many years. This is part of that lack of transparency. While half the world’s assets are buildings and property is largely transparent in land registry registers there, this is not true for
other types of ownership, such as shares or assets in certain foundations or trust organisations. These are all entry points for a lack of transparency with many negative consequences for enforcing what is necessary legally or warranted in itself. Piketty and Zucman argue at this point that property should in principle be registered in registers, to which public authorities have access when required. Otherwise, no legal protection for the property should be granted. The orientation of ownership on the common good and the assumption of responsibility on the part of owners should thus be fully enforced.

The following is now noteworthy*: Switzerland has recently further tightened its transparency regulations for combating money laundering on the recommendation of the Financial Action Task Force (FATF; a working group in the OECD anti-money laundering) and in response to international pressure. The change in the law for private limited companies with bearer shares, and slightly reduced for all other private limited companies and limited liability companies, is included. The new developments already came into force on July 1, 2015 with partially applicable transitional periods of 6 months. This means urgent action for all private (or non-listed) companies in order to create the necessary structures in time.

8. Why are bearer shares problematic?

While companies keep what is called a shareholders register for registered shares, in which shareholders must register in the company with each purchase of shares and do not become shareholders until it is entered in the shareholders register, there are no comparable structures for bearer shares. Because all shareholders’ rights are contained in an anonymous sheet of paper and the shareholders can pass on this paper as they like, the company does not know the holders of bearer shares.

9. What new obligations apply to bearer shares?

Bearer shares will effectively be treated as registered shares in the future. What is new is that companies must also keep registers for all their bearer shares.

10. What other obligations apply to all AGs and GmbHs?

In the future, all types of shares including ordinary shares of GmbHs will be obligated to ascertain and document the economic beneficiary for holdings of 25% and more. The economic beneficiaries are the natural persons (one or more), who are behind all holdings, interim companies, trust structures, etc. and are the actual beneficial owners of the assets.

11. Harmonization of corporate taxation in the EU

Amazingly there has been movement within Europe on another subject. Whereas so far the focus has been on the harmonization of the basis for corporate taxation in EU discussions on the topic (which, however, did not lead to any progress over the years), the much debated findings about the massive tax concessions made by Luxembourg in particular towards very large companies have meant that the subject of minimum levels of taxation in the corporate sector is now also on the table within the EU. That the BDI in Germany opposes this is difficult to understand. For every ordoliberal there should be a self-evident objective of

* urtax NEWSLETTER of 30/06/2015
ensuring fairness in a common market by comparable or agreed upon levels of taxation of all companies and of preventing “freeriding” of some companies at the expense of others. This is true so much the more, as particularly small and medium-sized companies are those that are usually disadvantaged.

12. Explicit addressing of the balance of income distribution

Another key issue in the work of the Research Institute for Application-oriented Knowledge Processing (FAW/n in Ulm), the Club of Rome and others which has been raised in books and dissertations, is the question of social balance, the so-called ‘efficient inequality range’—in other words the shaping of social differentiation within societies to ensure a positive effect. Accordingly it is a matter of achieving the golden mean between too much and too little balance. In the wake of the financial crisis, large international organizations such as the IMF and OECD have changed their economic position considerably. They are now arguing in favour of green and inclusive economies, instead of essentially unregulated market structures. This corresponds to the Senate’s position of an ecosocial market economy, an ecologically and socially regulated market economy. With its Better Life Index the OECD has also formulated an interesting list of criteria for sustainability, which includes an explicit parameter for the distribution of income. German political thinking has not yet reached this stage. The topic has currently gained importance due to the reflection of the important book by Piketty (Capital in the Twenty-First Century), as well as in continuation of relevant considerations by economic Nobel laureate Joseph Stiglitz in his book on the topic “The Price of Inequality”. The problem of increasingly input-free appropriation of ever larger parts of the annual economic output by a small group of very large asset holders and their heirs requires reforms and change, if a “productive” balance of income distribution is the goal.

The contention of the OECD corresponds to the position which the Senate has always held that the 80% with lower income levels should enjoy at least half of total income, and the 20% with higher income levels should have access at most to 50% of total income. As described, the question of distribution is today an explicit policy issue within the OECD. Unfortunately this is not yet the case in Germany and Europe as a whole. That needs to change. The Senate has always argued in this direction, and is now doing so increasingly with regard to potential massive future job losses in high skills areas resulting from the increasing technical intelligence of IT systems, from analytics, Industry 4.0 and the use of big data.

In cooperation with Denkwerk Zukunft, which shares our position on the issue we, as the Senate of the Economy, held an interesting conference on the issue of income distribution as long ago as 2012 in Hamburg. The subject of the conference was that a balancing parameter

was missing in the ‘magical quartet’ of Germany’s 1967 Stability Act, which addresses the four points of (1) price stability, (2) high employment, (3) balanced external trade and (4) adequate and steady economic growth. In the ‘affluence quintet’ of Denkwerk Zukunft the balance of income distribution is one of the 5 parameters taken into account when looking for sustainability-oriented policies.

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In a recent study entitled “Why Less Inequality Benefits All” the OECD has now once more pointed out that countries lose a lot of wealth when inequality becomes too great. This unambiguous statement is a very big step forward towards a “green and inclusive economy” philosophy. In Germany, too, at least one important step forward has been taken: the introduction of the minimum wage.

13. Towards better Corporate Law

In today’s economic system, the dominance of ownership interests towards returns on assets and capital undermine the obligation of property, within the context of the common good to at least pursue the objective of sustainable development equally. In particular, success in the market can be “sold” as a valuable contribution, even when it is ultimately based on burdening the common goods, that is, of global commons. This is a form of externalisation of costs of companies at the expense of the general public. In today’s competition law, set competitors cannot sue under competitive pressure of unfair competition but are put under pressure on the market, in the sense of a Prisoner’s Dilemma, to do the same as their competitors. The “plundering” of the commons is becoming commonplace, as can easily be observed in the climate issue, today.

To this end, there are now new scientific activities underway, intended to modify corporate and competition law, which is addressed very comprehensively in documentation from the Friedrich Ebert Foundation, “Anchoring sustainability in competition”. This goes back to the concrete formulation of the required new laws by experts from the legal sector with relevant specialisation. In particular, companies should be able to sue competitors for unfair competition if they achieve their performance in the market under false pretences, namely (only) at the expense of the burden of common goods. If their suit is successful, then the “free riders” are levied with the appropriate costs and obligations as a condition of being allowed to keep their licence to operate. In the long-term, this may be an important contribution in a world in which entrepreneurship and sustainability are better connected than today.

‡ Friedrich-Ebert-Stiftung (ed.): Anchoring sustainability in competition. Expertise on behalf of the Department for Economic and Social Policy of the Friedrich Ebert Foundation (Authors: Johannes Hoffmann, Gerhard Hofmann, Jens Lowitzsch, Christian Pitschas, Denis Suarsana and Herwig Roggemann), Bonn, June 2015
14. New Approaches to solving the Climate Problem

Interestingly, progress is also being made with respect to the climate. For too long an attempt has been made to translate an abstract idea of justice into a global compromise. This could never succeed, in view of the very different initial situations in which countries find themselves, combined with equally different notions of justice. The debate so far has only reflected the problems of justice between developed and less developed nations. In the process there has been no mention of the achievements and inventions of the developed nations—for example penicillin or the automobile—which have benefited the less developed nations. What was also lacking was the second dimension of justice, which consists of the fact that countries such as India and Brazil now contain many rich people, while there are also a lot of poor people in OECD countries. Even more significant: unemployed people in Germany cannot be expected at their own expense to solve the climate problems of Indian millionaires. As a result two dimensions of justice need to be addressed simultaneously.

15. Voluntary Carbon Neutrality on the part of the private sector

The logic of development has meant that today, since Copenhagen, a pledge-based approach is being pursued, and hopefully this will result in a new global climate treaty in Paris. This pledge-based approach, which is voluntary, not directly coordinated and not conditionally related commitments by the participating states, will only solve half of the climate problem. However, it may solve the question of justice between nations. At the same time it opens up a large window for private climate-neutrality action on the part of organizations, businesses and private individuals, which can be financed by wealthy protagonists in particular. This applies to drawing legal emission certificates out of the market as well as to afforestation and humus formation in agriculture in order to absorb CO₂ from the atmosphere (negative emissions). Such measures contribute, in particular, towards the second dimension of justice to be observed.

16. Financing the Green Climate Fund

Potentially they involve indirect co-financing of the green climate fund by the rich countries to the benefit of the less developed countries. After the preliminary agreements this fund will provide at least $100 billion a year, which the rich countries are to contribute annually from 2020 in order to support climate protection measures in poorer countries and finance measures required for adaptation to climate change. If we consider that the total budget for development cooperation (ODA) is currently (only) 135 billion dollars per year, this is an important new element in cross-financing from the fully developed countries to the remaining states. In addition, such carbon neutrality measures mean the co-financing of humus formation and in particular of afforestation in tropical countries.

This is a wealth and development programme for these countries which also promotes the environmental dimension of sustainability. It is a programme which the Economic Senate has been promoting for a long time. The World Forest Foundation of the Senate is particularly active in this field, in cooperation with the World Bank among others. Many of our senators have already adopted climate neutrality. Here, too, there is an opportunity for improved further developments.
17. Oslo Principles and an important Dutch Court Decision

It is also interesting that a group of leading philosophers and legal scholars with what are called “Oslo Principles” are developing a step towards global domestic law and global governance in a report on the position that the countries of the world are already obliged in currently valid international law to do everything possible and reasonable under fair conditions in order to solve the climate problem within the meaning of the 2 °C objective. There is a difference here between the obligations of developed countries and the least developed countries. It should be stressed that the right to impose economic sanctions on countries that fail to comply with the Oslo Principles is part of the programme. However, how this approach should be enforced is not discussed when strong nations such as the United States refuse to accept these legal principles. It is also not discussed how the relationship with WTO law may be if, for example, border adjustment tariffs are imposed on countries that do not abide by the Oslo Principles. Nevertheless, it is interesting that a legal position arises here which will possibly be confirmed again by international courts.

It is very interesting in this context that now for the first time a court, in this case the Dutch District Court of The Hague, in the Urgenda case (Urgenda is a Dutch foundation that campaigns for rapid transformation towards sustainability), has ordered the Dutch government to adopt significantly more stringent climate policies than previously planned. In addition to Urgenda, 900 Dutch citizens have also supported the suit. Specifically, the Dutch government is instructed to reduce emissions on its own territory by 25% within five years. The argument concerns the protection of Dutch citizens from the risks of climate change.

18. Europe on the road to greater unity—despite crisis

Europe is struggling to cope with the euro and the Greek crisis. But beyond Greece it is about much more—the further development of the European Union. Now an important step has been taken with the Five Presidents Report. The presidents of the five main EU institutions, Jean-Claude Juncker (European Commission), Mario Draghi (ECB), Jeroen Dijsselbloem (Euro Group), Martin Schulz (European Parliament), and Donald Tusk (European Council) have recently presented this report. The proposals for reform presented in it, which provide for more European integration in the financial sector, a more effective banking recapitalisation, and the beginning of a capital market union, among other things, are a step in the right direction. However, with respect to fiscal and structural reform they remain too vague.

In this context, Europe must especially recognise that the monetary union is a step away from fiscal sovereignty.§

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Notes

§ Handelsblatt, July 6, 2015 No. 126, p.48