Estimating bargaining-related tax advantages of multinational rms

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Abstract

The effective tax rates (ETRs) of multinational enterprises (MNEs) differ from those of national enterprises (NEs). We argue that the bargaining power of MNEs is an important factor in explaining the observed differences. First, MNEs are more profitable than NEs. This improves their bargaining position with tax authorities and they are able to negotiate greater tax deductions. Second, MNEs face lower costs to re-locate their business to a foreign country with a lower tax rate than NEs. This enhances the bargaining position of MNEs when negotiating about deductions. Both effects can explain the observed tax gap between MNEs and NEs; however, the tax gap between MNEs and NEs does not permit any immediate inference about the extent of MNEs’ tax avoidance. To decompose the two channels of the corporate profit tax gap between MNEs and NEs, it is elemental to rigorously condition on a vector of fundamentals which determine MNE status, profit taxation, as well as possible profit shifting activities. To that end we use French firm-level data and entropy balancing of the joint determinants of MNE status and a firm’s ETR. We find that the regressivity of the French ETR (due to economies of scale in tax deductions) reduces French MNEs’ ETR by 1.12 percentage points, while the relocation threat of the same firms reduces their ETR by 4.25 percentage points. The former is a tax advantage that any firm (MNE or NE) of the same size could obtain, while the latter is one that is specific to MNEs.

Keywords: both

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