Global Minimum Corporate Income Tax: Challenges and Prospects in Uganda

Corti Paul Lakuma and Rehema Kahunde

Introduction

- Uganda charges a corporate income tax (CIT) rate of 30 percent. However, CIT collection has been consistently below 1 percent of GDP.

✓Lakuma (2019) suggests Average Effective Tax Rate (AETR) is between 4% and 5%,

✓Koivisto, Musoke, Nakyambadde, & Schimanski (2021) Suggest that MNCs in Uganda deduct 20 percentage points more than their large domestic counterparts.

- This could be evidence of profit shifting

Introduction (cont'd)

- Therefore, Uganda has a significant need for stronger CIT reforms.
- An ambitious reform, agreed upon by 138 jurisdictions, proposes a Global Minimum Corporate Tax rate (GMCTR)
- However, little empirical work has been able to estimate the effects of GMCTR on MNCs.

Introduction (cont’d)

- GMCTR has important implications for different countries;
  - ✓Revenue effects of the GMCTR could be large as incentives are eliminated (IMF, 2023).
  - ✓GMCTR may reduce profit shifting and tax competition and generate positive spillovers for jurisdictions with high CIT rate (IMF, 2019).
  - ✓Conversely, GMCTR is attractive to jurisdictions with low taxes but may be hard to administer (ibid).
  - ✓Yet, most developing countries expect to be losers (Hebous & Keen, 2021).

Introduction (cont'd)

- Broadly, there is need to examine whether the GMCTR does not affect tax collection.

- For a country with low AETR like Uganda, GMCTR is expected to raise AETR of MNCs.

- This may provide opportunities for tax evasion and avoidance that raises elasticities of taxable income, which would imply lower revenue (Klemm, Liu, Mylonas, & Wingender, 2018).

- A significant number of papers have used elasticities as a measure of marginal excess burden

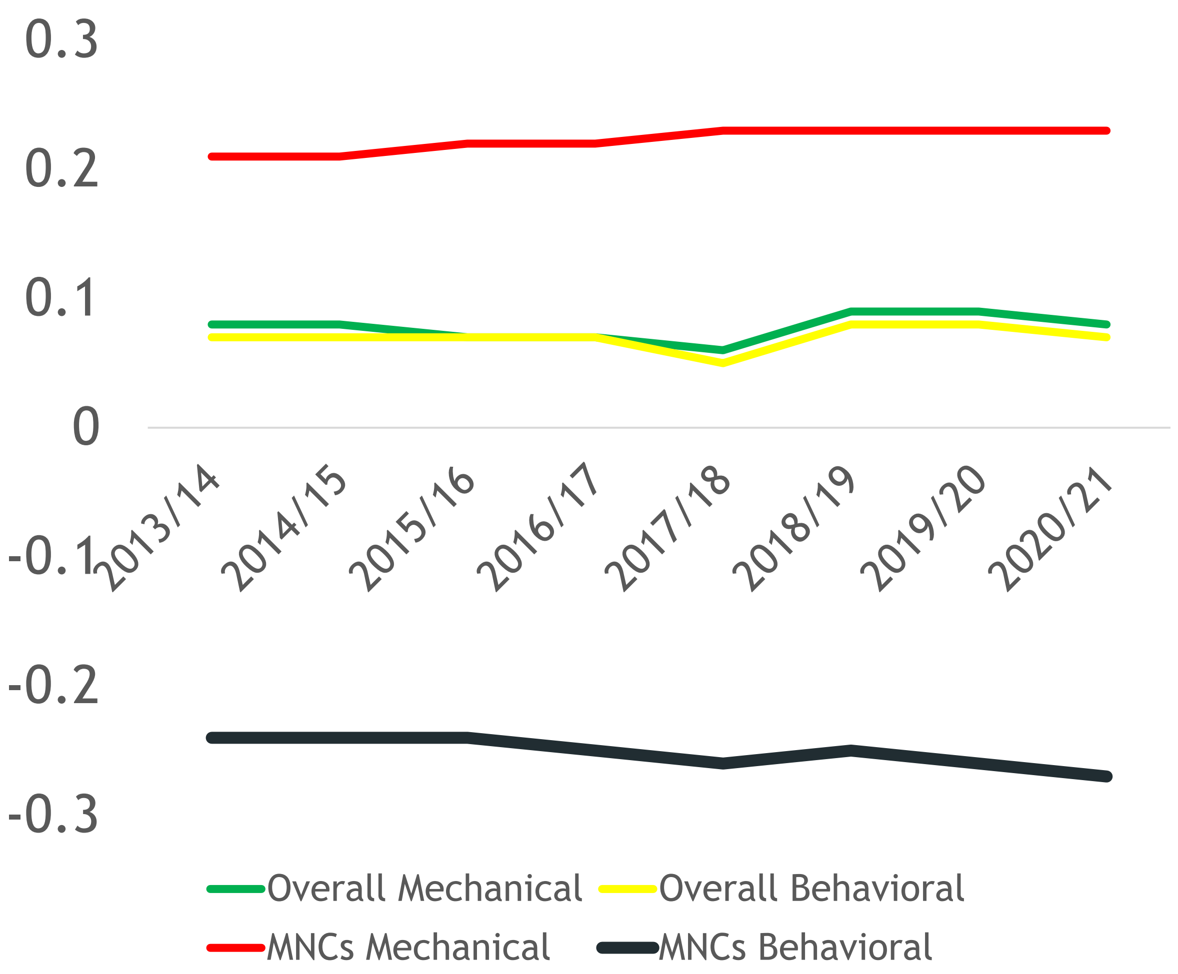
Methods and Data

- Estimate the mechanical revenue gain from moving from current effective tax rates by firms to a 15% minimum tax for firms exceeding the threshold
- Reviewed international literature on how elastic corporate income tax base or investment are to changes in tax rates
- Elasticities grouped into percentiles (25^{th}, median and 75^{th})
- Used the estimates and the changes in the tax rate to estimate the likely reduction in tax base as a reaction to the GMCTR.
- Calculate and report the total change, which is the mechanical gain minus the behavioral reaction
- Data: URA firm panel curated by URA and UNUWIDER and documented in McNabb, Nakyambadde, Jouste, & Kavuma (2022).

Methods and Data

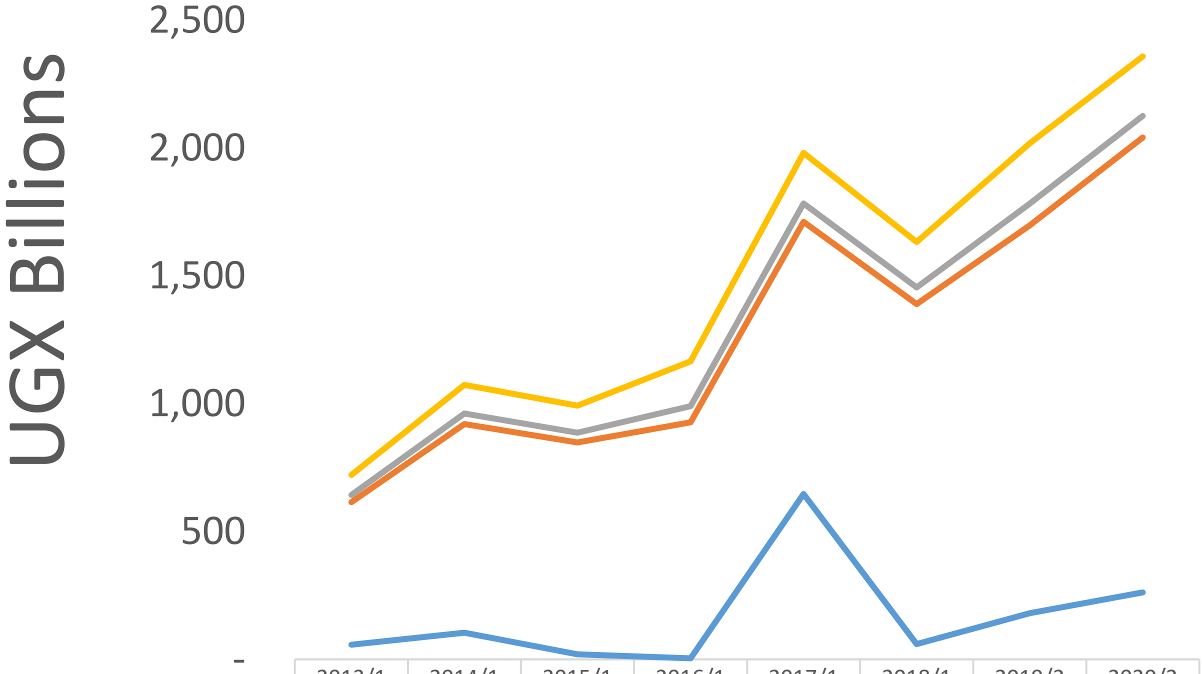
Variable	Observations	Mean (Millions)	Std. dev. (Millions)	Min. (Millions)	Max. (Millions)
Provision for Taxes	10,798	93	2,030.0	0.2	167,000
Profit before Taxes	10,798	858	24.3	1,680.0	2,400,000
Total Assets	8,465	7,530	188,000	- 12,500.0	15,500,000
Gross Profit	10,798	1,130	15,100	- 23.5	1,210,000
Profit before Taxes	10,798	858	24.3	1,680.0	2,400,000
AETR*	10,798	0.133	0.087	0.0	0.30
MNCs*	10,798	.018	0.135	0	1
Sectors*	10,416	2	3	1	4

Distribution of AETR



- AETR of MNCs increase with introduction of GMCTR
- However, MNCs respond by disproportionately hiding output
- The Overall (by both MNCs and DCs) response to GMCTR is not far from the behavioral change

Overall response to GMCTR



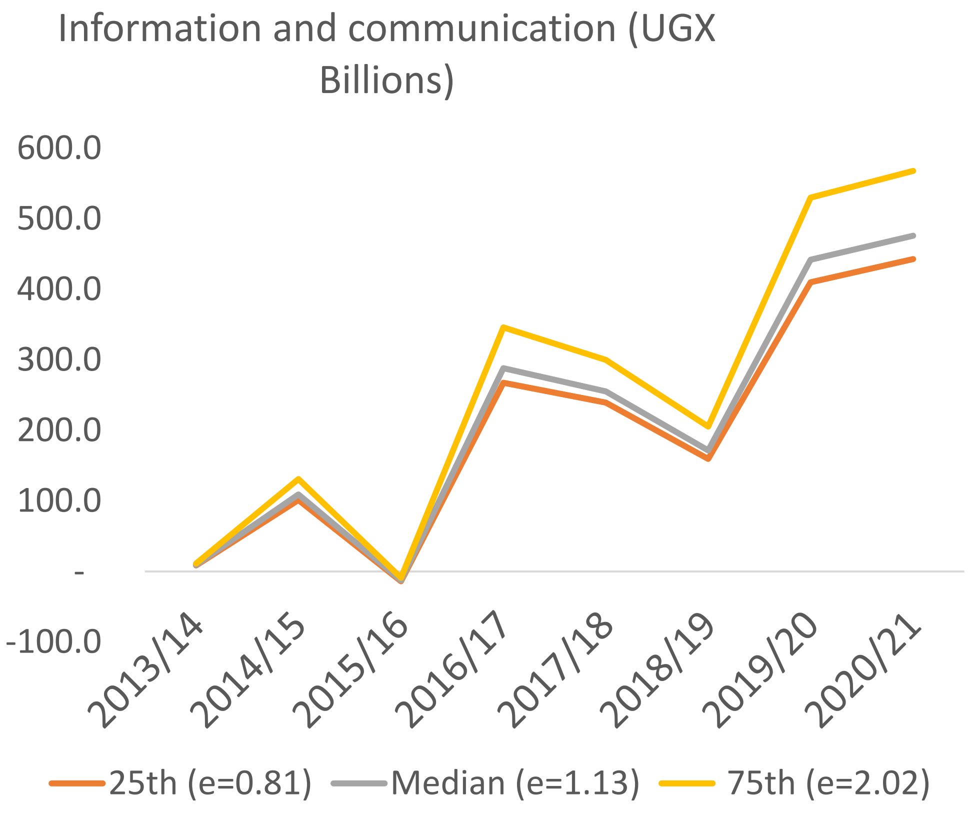
	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21
25th (e=0.81)	615	921	849	928	1,712	1,390	1,698	2,042
Median (e=1.13)	644	962	887	991	1,784	1,455	1,783	2,126
75th (e=2.02)	722	1,074	993	1,166	1,982	1,633	2,019	2,359
Reported Revenue(URA)	57	104	20	5	647	60	181	262

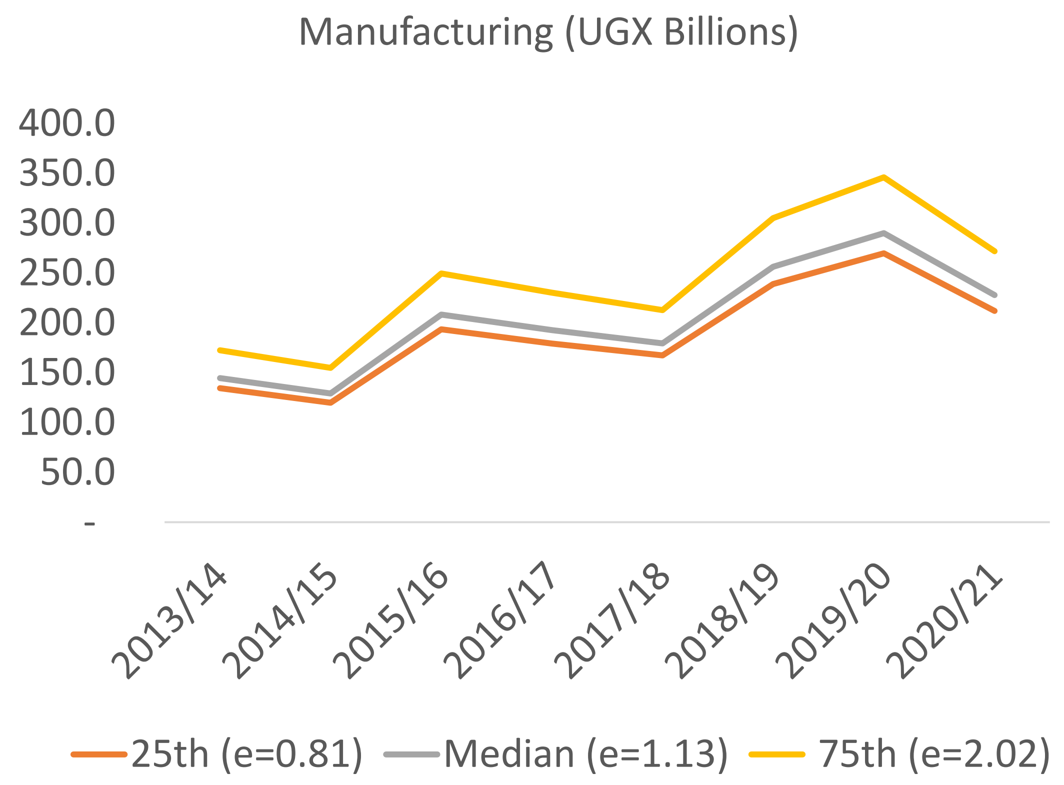
25th (e=0.81) Median (e=1.13)
75th (e=2.02) Reported Revenue(URA)

- Overall revenue gain, regardless of elasticity
- The elasticity is proportional to the revenue gain
- The gain in revenue is higher than the current collection

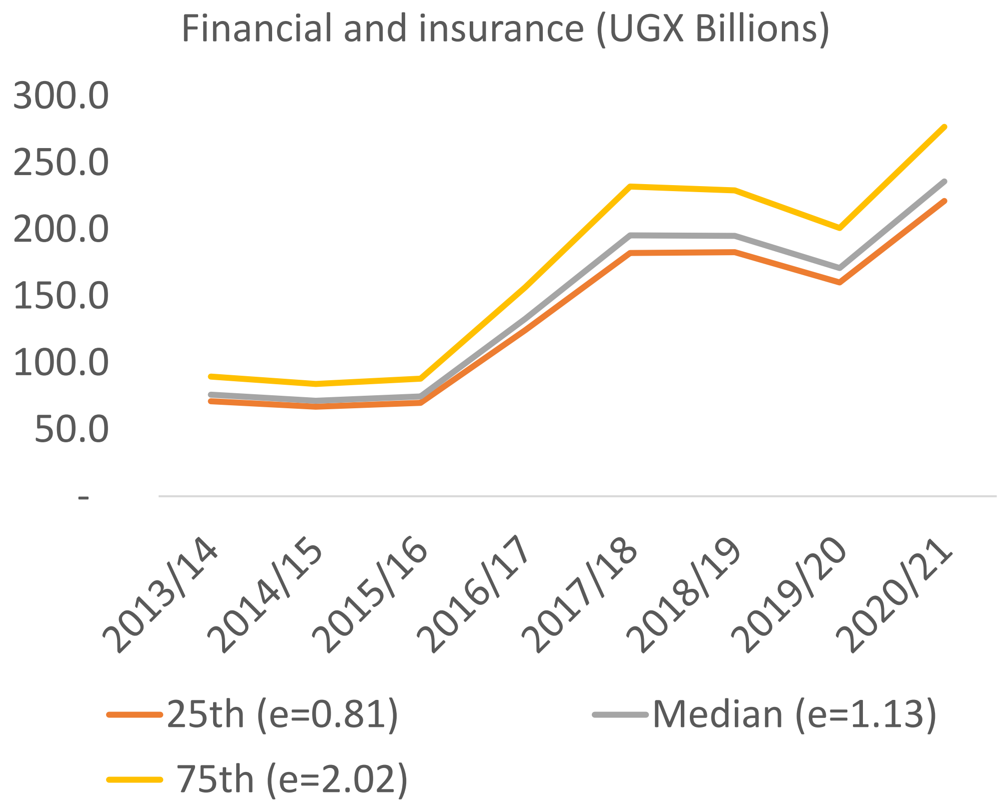
Sector response

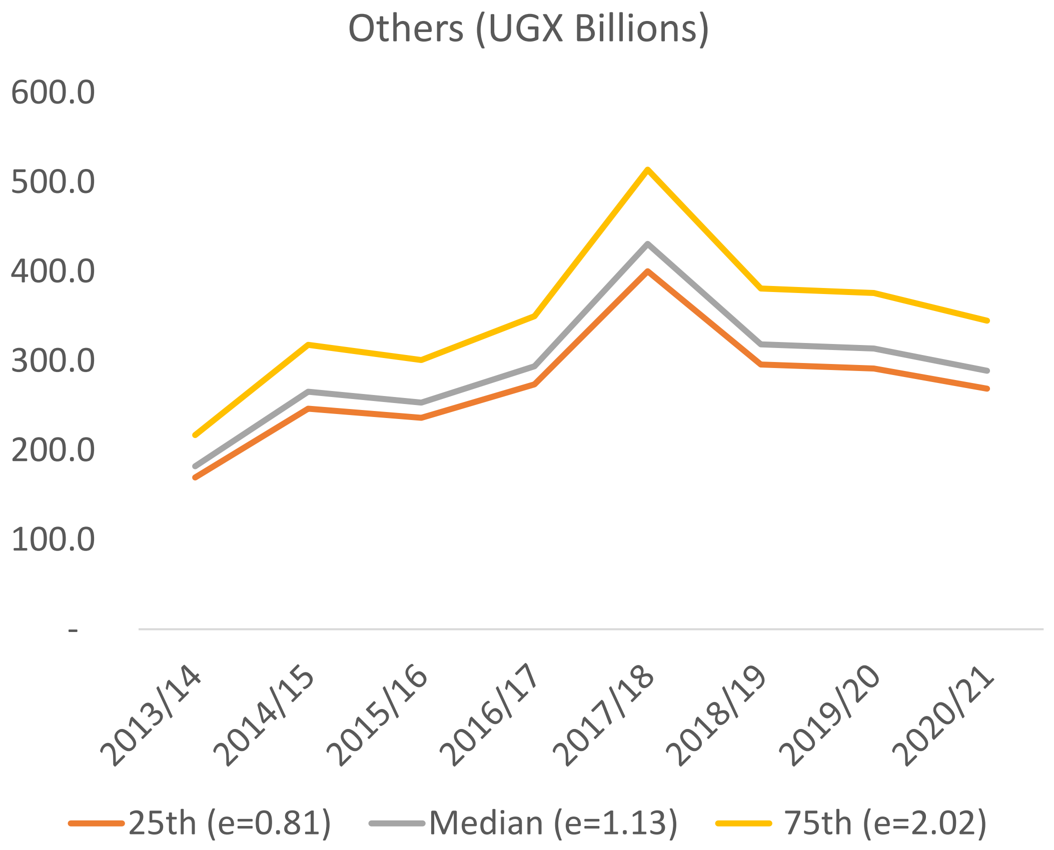
❖ Information and comm. And manufacturing Sector have the highest gain





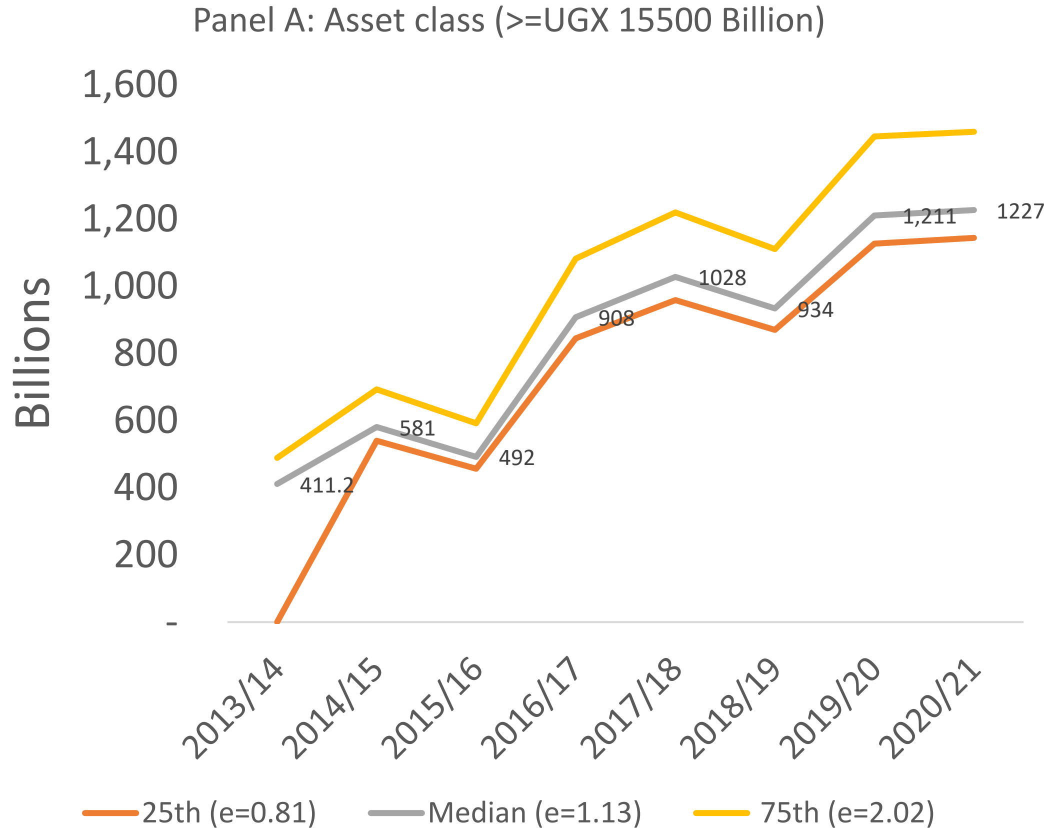
Sector Responses
Finacial sector sensitive to tax tax changes

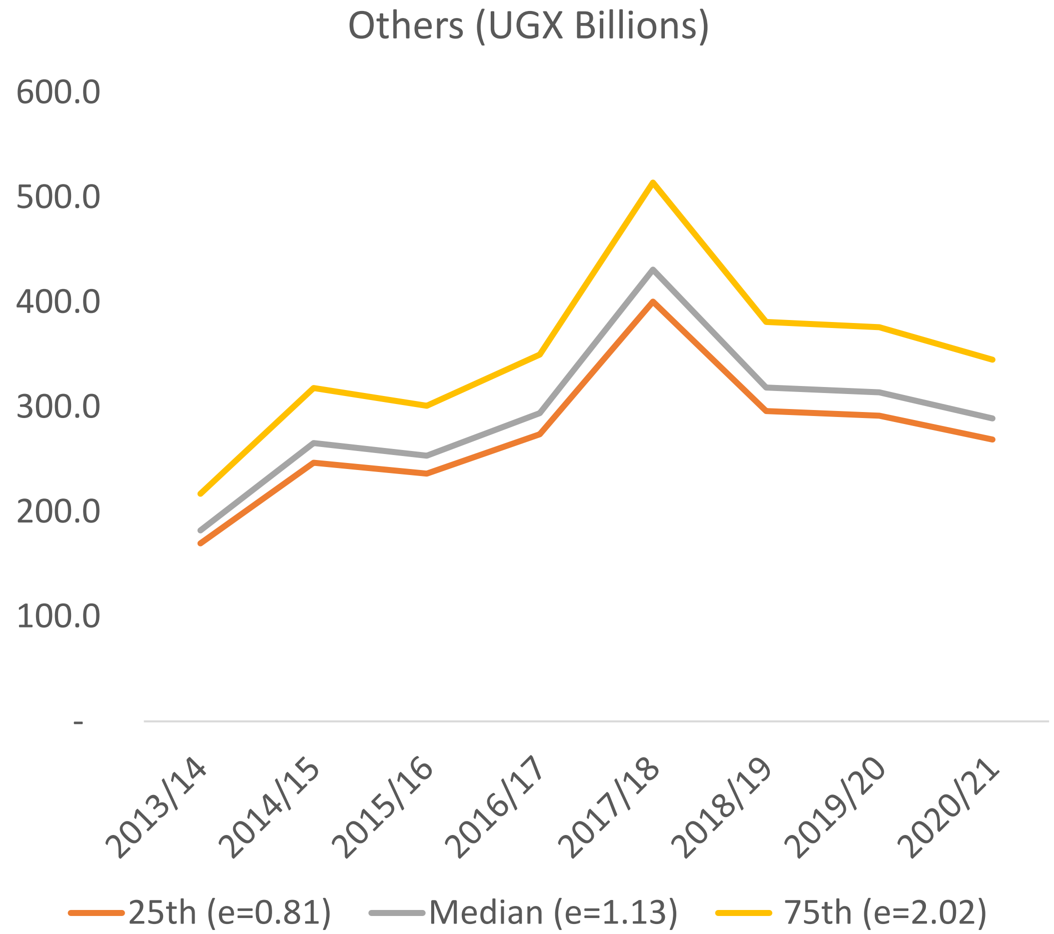




Asset Class Responses

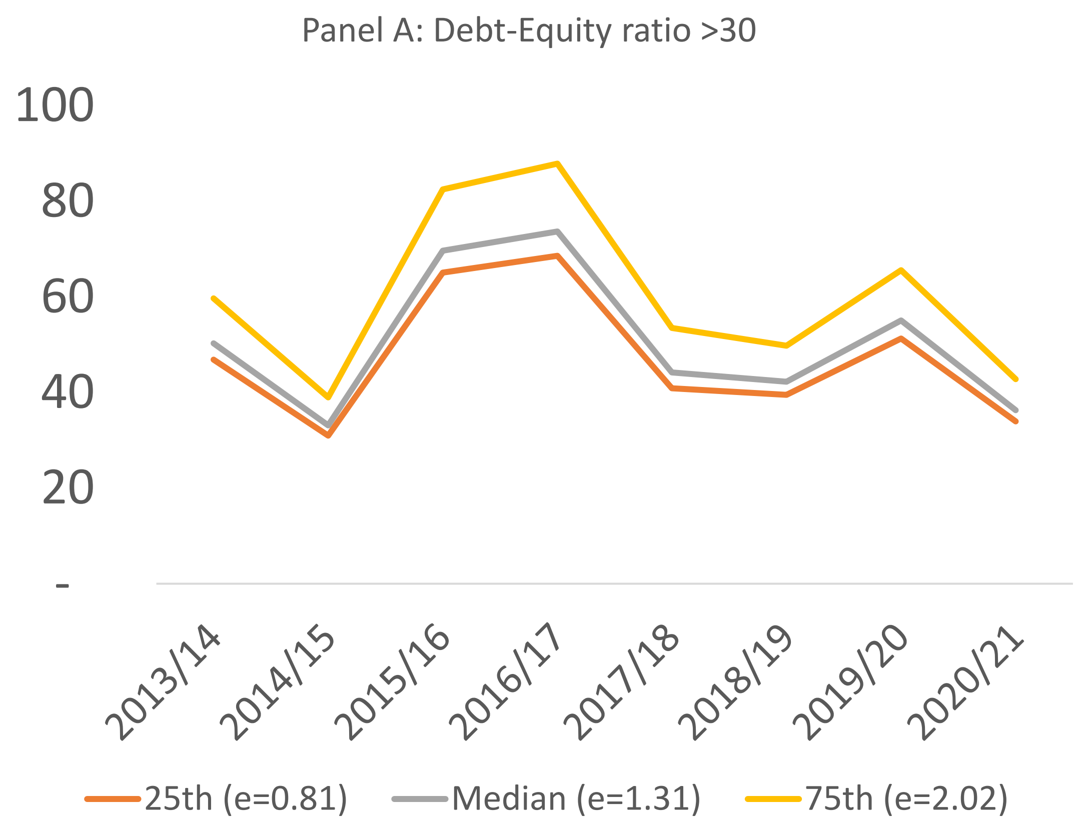
❖ Larger business produce larger revenue gain

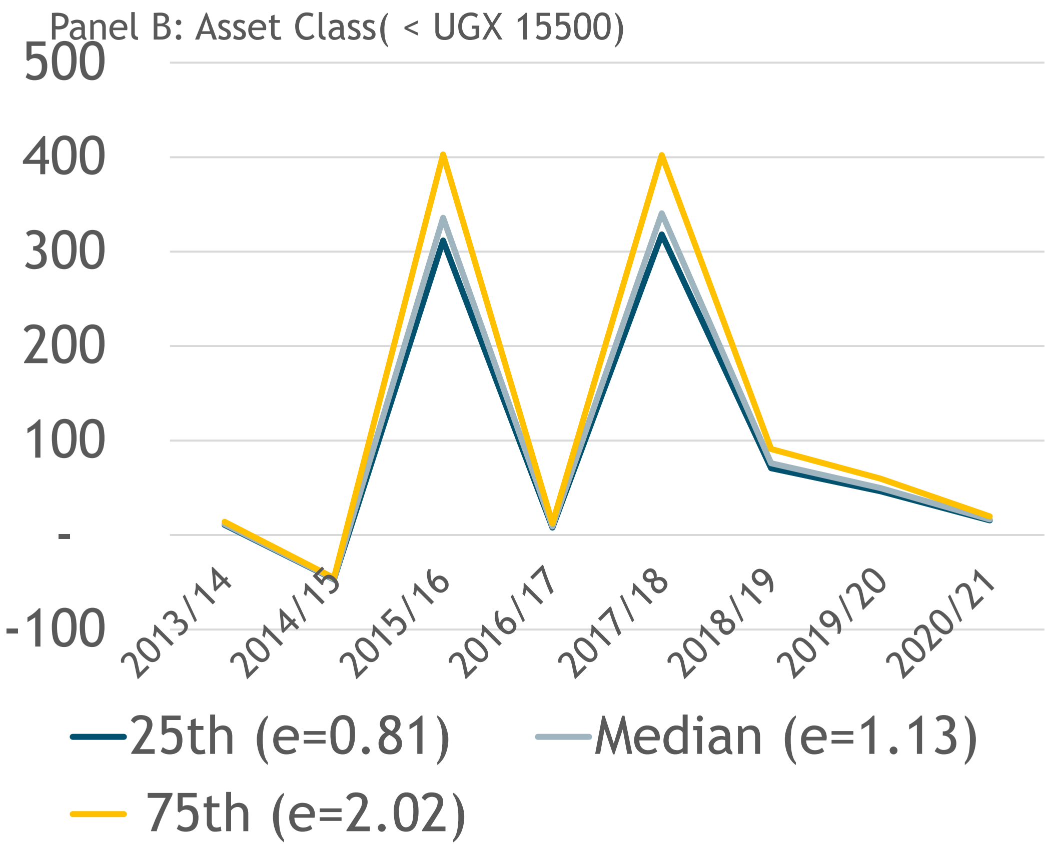




Capitalization Responses

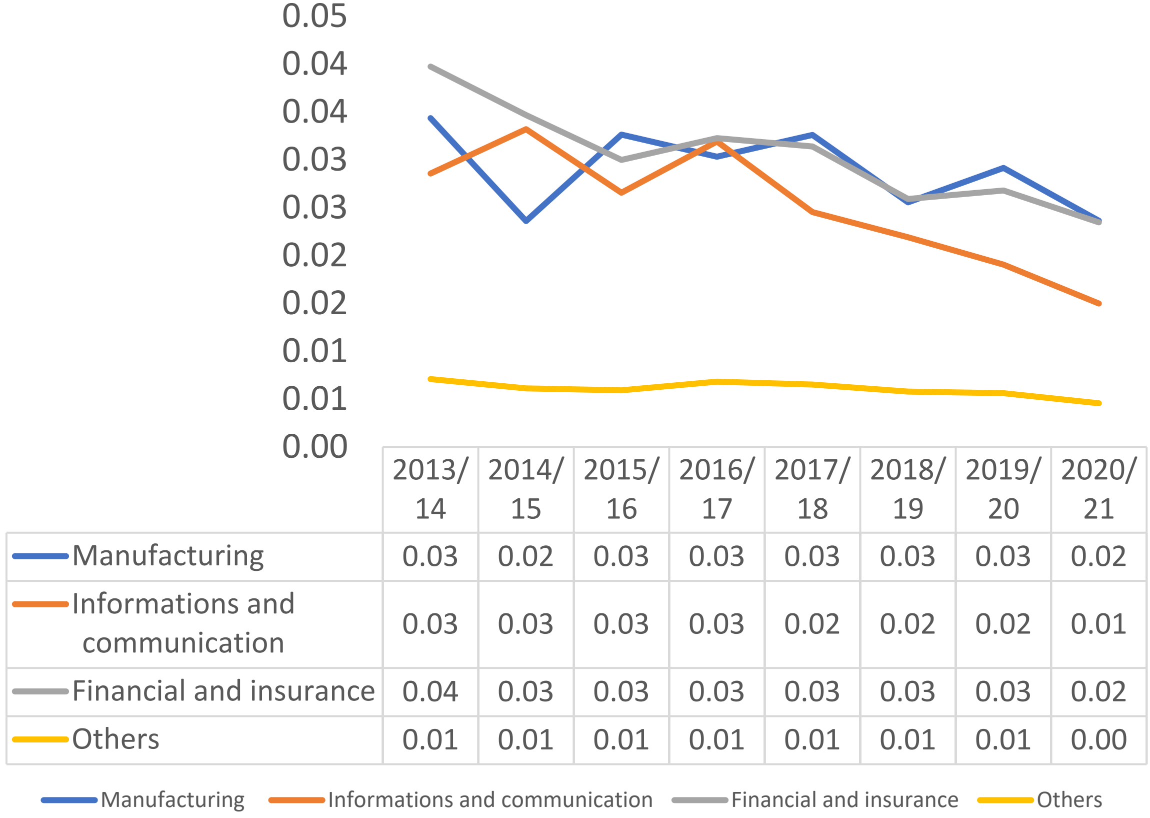
❖ Thinly capitalized MNCs produce higher and more stable revenue gain



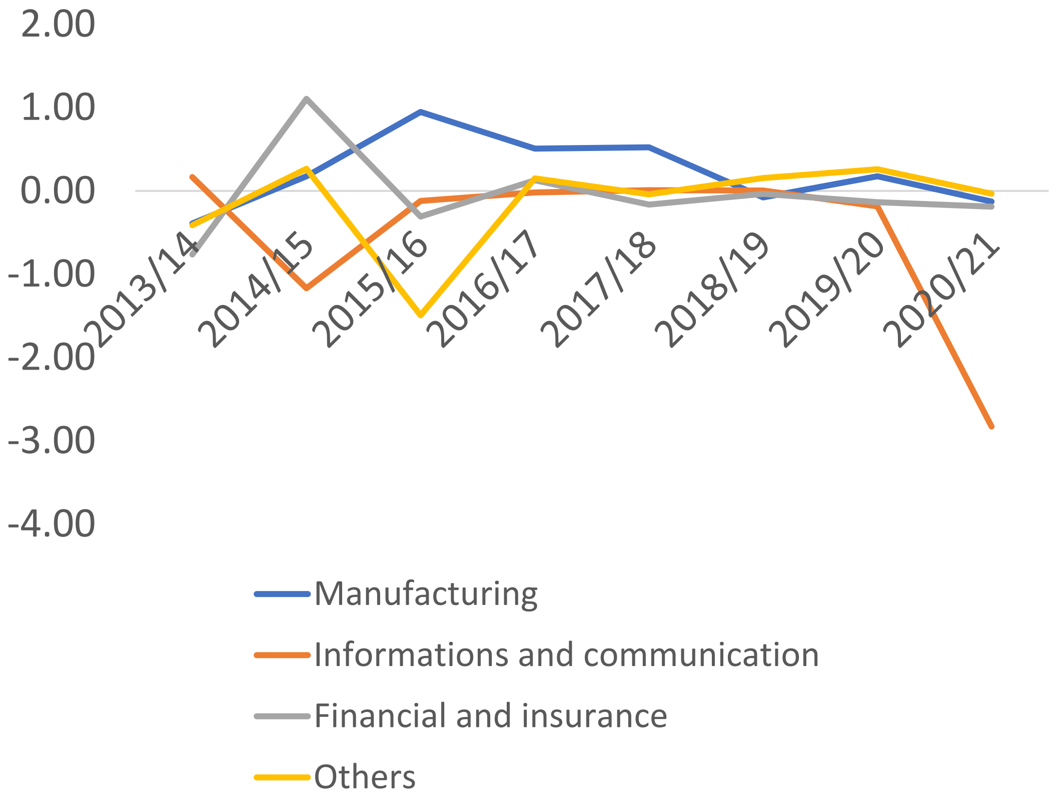


Reported and Real Response by sector

Information and communication sector evade the most taxes and Manufacturing sector invest the most



	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21
Manufacturing	0.03	0.02	0.03	0.03	0.03	0.03	0.03	0.02
Informations and communication	0.03	0.03	0.03	0.03	0.02	0.02	0.02	0.01
Financial and insurance	0.04	0.03	0.03	0.03	0.03	0.03	0.03	0.02
Others	0.01	0.01	0.01	0.01	0.01	0.01	0.01	0.00



❖Conclusions

- The are size variations regarding response to GMCTR: Large firms provide more revenue gain
- There are sector variations in response to GMCTR: Information and comm. Provide the highest revenue gain; but also has the least AETR (evades most taxes). The Financial sector is sensitive to tax changes. While the manufacturing sector invest the most
- Thinly capitalized MNCs provide the largest revenue gain. GMCTR is able to curtail BEPS

❖Policy recommendations

- Regional cooperation and Enhance administrative capacity to implement GMCTR
- Adopt safe harbor rules to simplify and prescribing expected returns for specific sectors and firm sizes.
- Limitations of mechanical deduction for potentially base-eroding payments for interest deductions