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## UNITARY TAXATION: THE BRITISH GOVERNMENT'S VIEWS

### A Note by the United Kingdom Government to the United States Treasury Working Group on World- wide Unitary Taxation.

The British Government has long-standing objections to the method of unitary taxation and has made these clear at the highest levels of the U.S. Administration and elsewhere on a number of occasions. Today the British Government has put a note to the U.S. Treasury Working Group on Unitary Taxation. The United States Administration has established the group under the Chairmanship of United States Treasury Secretary Regan. It is composed of representatives of the Federal Government, State Governments and the United States business community.

The note sets out the reasons why the United Kingdom Government, like many other Governments, is opposed to worldwide unitary reporting. The main points in the note are:

- "A. Her Majesty's Government is opposed to the application of the unitary method of state taxation on a worldwide reporting basis.
- "B. The worldwide unitary method of state taxation is contrary to well established international principles and practice of taxation, and imposes unreasonable tax and administrative burdens on multinational corporate groups doing business throughout the world.

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- "C. Unitary taxation is already damaging commercial and economic relations between the U.S. and the U.K. and other countries. If it continues, the damage to international trading relations will become more serious. If unitary taxation spreads, the scale of the worldwide damage will be further increased.
- "D. In particular, for U.K. companies unitary tax imposes significant additional burdens on both the companies and their shareholders. First, it produces anomalous tax liabilities, which may be considerably larger than those calculated on the internationally accepted arms'-length basis. Second the requirements of the method involve additional compliance costs. In addition the uncertainty generated by the unitary method has disruptive effects on U.K. corporations' business activities and industrial investment.
- "E. As long as the worldwide unitary method persists, it will be impossible to achieve the essential economic objectives of providing a consistent and coherent tax framework for international trade and investment. Moreover, the damage to international trade and investment would be greatly increased if foreign Governments responded by imposing retaliatory measures or introducing unitary systems of their own.

The conclusion of the British Government's note is:

"In this paper the U.K. Government has analysed the worldwide unitary system by reference of the universally-accepted criteria of a good system -- equity, certainty, simplicity and the promotion of economic efficiency. It has demonstrated that, when applied in the present international context, the worldwide unitary method inevitably produces results which are inequitable and uncertain. The method involves additional compliance costs for companies. Furthermore it is in the United Kingdom Government's view objectionable in principle that the method can require the disclosure of the records of companies outside the USA, particularly as these will often apply to transactions entirely unrelated to activities within the United States.

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"If the worldwide unitary system is allowed to persist, it will hamper rather than promote economic efficiency distorting investment patterns and inhibiting trade throughout the world. It makes it impossible to achieve the essential objective of providing a consistent and coherent international tax framework for trade and investment. This framework is particularly crucial at the present juncture in the development of the world economy, when businesses are seeking profits throughout the world without regard to national boundaries. The narrow economic standpoint of the unitary system is incompatible with the harmonious relationship that is the goal of our Governments, to the benefit of the American and British people alike.

"The British Government await with interest the conclusions of the U.S. Working Group, and the proposals that the U.S. Administration put to their international trading partners in the light of the Working Group's report."

#### Background Notes for Editors

Worldwide combined unitary taxation is a method of taxation adopted by some states of the United States for corporations operating there. It is a technique for allocating profits of multinational companies not on arms'-length principles -- which is the method adopted by Developed Countries generally, including the United States Federal Government, and recommended by the OECD Model Double Taxation Convention of 1977 and by the U.N. Model of 1980 -- but rather on a proportion of world profits. The ratios of a company's sales, payroll and fixed assets in the territory of the taxing state to the group's world sales, payroll and fixed assets are ordinarily used to determine that proportion.

The British Government has consistently urged that action be taken to prevent the application of unitary taxes to United Kingdom businesses. It first sought to do so when negotiating the current United Kingdom/United States Double Taxation Agreement, but the United States Senate attached a reservation against the provision in the draft agreement which would have prevented individual states from applying the method of United States subsidiaries of

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United Kingdom corporate groups. In agreeing to ratify the Double Taxation Agreement without this provision the United Kingdom Government was given to understand that the United States Administration would take steps to resolve the matter.

The constitutionality of unitary taxation was subsequently considered by the United States Supreme Court in the case of the Container Corporation of America v. The California Franchise Tax Board. In June 1983 the Supreme Court delivered a judgement upholding the right of a state to use this method of taxation in relations to a United States parent corporation and its foreign subsidiaries. The Court reserved the question of the position of corporations with foreign parents. In the light of this judgement the Government again urged the United States Administration to take action to resolve the position. The Chancellor and the Prime Minister wrote letters to Treasury Secretary Regan and President Reagan in August/September 1983. The Chancellor and the Prime Minister also raised the matter with Treasury Secretary Regan and the President personally in Washington in late September.

The United States Administration decided not to file for a rehearsing of the Container Case. In September the President established a working group on unitary taxation, composed of representatives of the Federal Government, State Governments and the United States business community and chaired by Treasury Secretary Regan to explore its use and 'to produce recommendations that will be conducive to harmonious international relations while respecting the fiscal rights and privileges of the individual states.'

The U.K. Government is not alone in objecting to worldwide combined unitary taxation. The European Community and the Governments of the other major OECD countries have also submitted testimony for the consideration of the working group. In addition, a number of international businesses and business organizations have given evidence to the working group, setting out the objectives to unitary tax on a worldwide reporting basis.

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