Introducing a forward-looking component to the G20 leaders’ agenda

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The G20 leaders’ process should involve learning from the experiences of the past, dealing with the demands of today and anticipating the challenges of the future. If the G20 is to be the premier forum for international economic cooperation, it needs to focus more on likely future developments and the challenges from a rapidly changing global marketplace.

One lesson from the crisis is the close interconnectedness between financial markets. As Janet Yellen has pointed out in reflecting on the events of 2008, losses arising from leveraged investments caused a few important, but perhaps not essential, financial institutions to fail. She goes on to note, ‘At first, the damage appeared to be contained, but the resulting stresses revealed extensive interconnections among traditional banks, investment houses, and the rapidly growing and less regulated shadow banking sector.’ Of course, that interconnectedness operated globally and the events in US financial markets had worldwide ramifications.

Tax and trade are two high-profile issues on the G20 agenda. Like finance, they have a common driver: namely, the challenge policy faces in keeping up with an increasingly global and interconnected business landscape. More and more businesses operate globally.

Trade policy has to adapt to the reality that value chains are increasingly driving international trade. Goods are ‘made in the world’ rather than in one country. In such a world, the mercantilist view that exports are good and imports are bad, and the traditional trade negotiating stance that market access can only be granted as a concession for access to another country’s market, are out of date and counterproductive.

A challenge facing the G20 on tax is dealing with ‘base erosion and profit shifting’ – the ability of globally operating companies to exploit loopholes, particularly in double tax agreements, to make profits disappear for tax purposes, or shift profits to jurisdictions with little or no taxation.

The rise of global value chains has been facilitated by technological developments, particularly the digital age. The same forces have been driving financial innovation and the
interconnectedness of financial markets, along with transforming the traditional approach to corporate taxation. Goods are no longer produced in a single location in a single country, but are widely dispersed across jurisdictions. In such an environment it is increasingly difficult to determine in which jurisdiction value-adding occurs and where tax can be applied. This is even more challenging with goods and services delivered over the internet, including the challenge of imposing value-added taxes on such cross-border transactions.

Moreover, multinational companies do not organise their operations as discrete entities in specific countries who engage in arm’s-length transactions – they adopt a global approach. In such a world it is very difficult for a jurisdiction to identify where its taxing rights exist, and very easy for corporations to ensure that profits are only declared in low-tax centres.

Technological change will not stop. Financial innovation will not stop. More and more goods and services will be delivered over the internet. The advent of the 3D printer will further diffuse production and value-adding activities across many jurisdictions.

These developments will further increase integration between countries. The result will be that individual nation states will find it increasingly difficult to set laws covering globally operating businesses. Effective international cooperation will become more and more important. This is, of course, the reason for the existence of the G20, and it emphasises the necessity of ensuring that there are effective forums for international economic cooperation.

So rather than looking at such issues as financial regulation, trade and tax as discrete issues, the agenda for the G20 Brisbane summit should incorporate a specific session where leaders reflect on the future challenges of economic management from the perspective of likely corporate and technological developments. In short, G20 leaders should engage in ‘the vision thing’.

Notes

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