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Research on Tax Avoidance of Multinational Corporations in China

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Abstract: This article primarily focuses on the tax avoidance practices employed by multinational corporations. Firstly, it provides a comprehensive definition of tax avoidance behavior exhibited by these corporations and specifically highlights how such actions contravene the stipulations of tax laws. Subsequently, it delves into an analysis of commonly utilized tax avoidance methods by multinational companies, supported by real-life case studies. Finally, it examines the detrimental impact caused by the tax avoidance practices adopted by these corporations.In the latter part, in view of China's current laws, regulations and tax administrative enforcement problems on the issue of tax avoidance by multinational corporations, it puts forward suggestions on improving relevant laws and promulgating relevant legal interpretations.

Keywords: multinational corporations, tax avoidance, Chinese law

1. Introduction

Under the background of economic globalization, the rapid development of corporations has become a common phenomenon.Tax avoidance by multinational corporations is often hidden, difficult to detect and, because of its transnational nature, difficult to verify and convict. But at the same time, as a large multinational enterprise, the amount involved is often large, and the harm to the national tax revenue is great.

Accordingly, the tax regulation of multinational corporations has become a significant issue in the tax development of all countries worldwide. Many countries have conducted extensive research on this matter and implemented relevant policies to mitigate its negative impact. Most of them have established relatively comprehensive coping systems and legal frameworks to curb the tax avoidance practices of large multinational corporations within their jurisdictions. Throughout this developmental process, numerous typical cases have emerged, contributing to the government tax authorities' accumulation of valuable experience in dealing with such issues.

Turn to the situation in China. Since entering the 21st century, China has rapidly integrated into the world economy, reformed its tax system, and implemented numerous policies and regulations. However, China's multinational corporations have a relatively short development time, with only a few large multinational enterprises existing, most of which are state-owned. Private multinational enterprises are scarce as well. Additionally, China joined the World Trade Organization late and lacks experience in dealing with tax avoidance by multinational companies of foreign countries within the

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world market. Furthermore, directly transplanting the anti-tax avoidance cases in the Anglo-American law system to China also has the problem of incompatibility.

In the above context, the research of this paper mainly focuses to get the definition of tax avoidance of transnational enterprises, the harm caused by tax avoidance, and find ways to deal with China's own problems of transnational tax avoidance.

2. General Overview of Tax Avoidance Practices

2.1. Definition of Tax Avoidance

Tax avoidance by multinational corporations refers to the behavior of transnational taxpayers who take advantage of the differences, loopholes, exceptions and defects in the tax laws and international tax agreements of two or more countries to avoid or reduce their total tax obligations. It is legal for multinational companies to conduct tax planning in their operations on the basis of compliance with the tax laws of the relevant countries.This helps multinational companies reduce their tax burden. For example, transfer pricing is used for tax planning. Transfer pricing refers to the internal transaction pricing of products, services or property provided by the internal institutions of transnational management group companies or affiliated enterprises. Under the jurisdiction of high tax rate, transfer pricing is not only a way to repatriate profits that can be fully utilized, but also an important means to avoid withholding tax.

However,although the state allows companies to use legal means to save themselves taxes. However, tax avoidance is not a general sense of saving their own taxes, but to take the surface of legal, but actually contrary to the intention of the national tax law, is prohibited by various countries.

2.2. The Harm of Tax Avoidance

First of all, it disrupts the order of the international market. As multinational corporations take advantage of the differences in tax laws of different countries to transfer profits through related party transactions, which will cause some developing countries with imperfect laws to suffer huge financial losses[1].At the same time, due to the higher profits generated by large multinational enterprises in tax avoidance, some giant enterprises in developed countries will grow even stronger. This will further widen the economic development gap between countries and make the economic development of developing countries more difficult.

Secondly,tax avoidance will lead to a large imbalance in host country' international balance of payment and it would increase tax instability[2].Even further, these hazards lead to increased financial and economic and operational risks in the host country.High imports and low exports are common forms of transfer pricing.Through this mean, foreign-funded multinational enterprises can make foreign-funded enterprises import a large number of raw materials and other products that can be produced in host country, which leads to the increase of import and intangible expenditure and the decrease of export.

Thirdly,Tax fairness is an important factor to realize orderly market competition, and illegal tax avoidance will destroy orderly market competition environment. Because the actual tax burden of enterprises that avoid tax by illegal means is lower than the normal tax burden level, they can obtain a certain unfair competitive advantage, which leads to the development of vicious competition in the market. Not only that, such tax avoidance will put honest taxpayers at a long-term disadvantage and trigger the spread of tax avoidance activities. For the host country, it will not only destroy the domestic tax environment and tax system, but also make the fiscal revenue suffer long-term loss and reduce the competitiveness of the country.In addition, in international trade, some multinational companies lower export prices to transfer profits are also easy to cause foreign dumping charges

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against their own countries [3].As a result, international trade frictions will intensify, endangering the quality of global economic development.

2.3. Types of Tax Avoidance

At present, the main tax avoidance methods can be divided into two types:

2.3.1. Some Companies Use Loopholes Created By Some Legal Differences To Avoid Taxes

Tax avoidance by taking advantage of the differences in tax laws. Due to the differences in tax laws and tax policies of different countries or regions, multinational companies may choose to set up subsidiaries in countries or regions with lower tax rates

Take advantage of different international tax treaties to avoid taxes. Since the content of international tax treaties signed by countries is not the same, multinational companies may take advantage of these differences to avoid taxes.

Use preferential tax policies to avoid taxes. In order to attract foreign investment, some countries and regions will formulate some preferential tax policies, and multinational companies may take advantage of these policies to reduce tax burden.

Take Google's "Double Irish" and "Dutch Sandwich" as models: Google registers two companies in Ireland, one receives advertising revenue outside the U.S. market and transfers the revenue to another company based in Bermuda. Because the latter are registered in Ireland but headquartered abroad, they can enjoy Ireland's foreign business tax benefits. Google then uses another company set up in the Netherlands as a "middleman" to complete the funds transactions between the companies. Because all three companies are within the European Union, they are also exempt from corporate income tax.

2.3.2. Use Some Special Means To Transfer The Company's Profits Or Prices To Achieve Tax Avoidance

Use transfer pricing for tax avoidance. Transfer pricing refers to the internal transaction pricing of products, services or property provided by the internal institutions of transnational management group companies or affiliated enterprises. Under the jurisdiction of high tax rate, transfer pricing is not only a way to repatriate profits that can be fully utilized, but also an important means to avoid withholding tax.

Use bridging technology to transfer profits. The essence of bridging technology is to achieve the purpose of tax avoidance by involving third parties in cross-border transactions. There are three common forms of operation, such as using tax havens to invert acquisitions, constructing "conduit companies" or "stepping stone" companies.

Using the way of capital weakening to avoid tax. Under the influence of economic double taxation, investors are more inclined to take the way of debt financing for tax avoidance than equity capital investment. [4]This is because interest from subsidiaries can be deducted from taxable income for expenses, but dividends must be collected.In addition to that, the tax rates of interest and dividends imposed by the source countries stipulated in international tax treaties are not high, but the tax rates imposed on corporate income are relatively high.

A typical case is the related party transaction behavior of Huaying Technology Company. In Huaying Technology Company's supplier purchase amount, the related party purchase amount occupies the main part. However, it was noted in its annual report that some of these products lacked accurate market prices, so the agreed prices were formed through internal discussions. And these large numbers of internal agreement prices are very likely to deviate from the market price, forming tax risks[5].

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3. Current Legal And Regulatory Measures In China

3.1. Regarding Tax Avoidance, China's Current Legal System

With the improvement of our legal system, the state fully realizes the harm of tax avoidance, and is committed to the management of the chaos in the field of tax avoidance. After years of efforts, the tax law has also been greatly developed. The current tax avoidance regulation in China is based on the Enterprise Income Tax Law and the Tax Collection Administration Law, and is composed of the Implementation Regulations of the Income Tax Law issued by The State Council, the Implementation Rules of the Tax Collection Administration, the Special Measures and the General Measures issued by the State Administration of Taxation, etc., which provides the legal basis for regulating the tax avoidance of multinational corporations in China.

The Special Measures define and regulate advance pricing arrangements, capital depletion, controlled foreign enterprises, cost-sharing agreements. The main means used by large multinational corporations to avoid taxes are restricted.

After the promulgation of the Special Measures, the State Administration of Taxation issued the General Measures, clarifying the scope of application of the General Measures, and stipulating in detail the procedures for filing, investigating, closing cases and handling disputes for tax authorities to investigate general anti-tax avoidance enterprises, thus providing a procedural legal basis for tax investigations.

In addition, the State Administration of Taxation issued the Announcement of the State Administration of Taxation on Issues related to the Monitoring and Management of Special Tax Adjustment, which clarified the problems of the anti-tax avoidance monitoring and management. Actively promote the implementation of the Special Tax Adjustment Implementation Measures (Trial), and promote the implementation of BEPS research results[6].

In addition, China has promulgated specific laws on multinational corporations and tax avoidance. For example, the implementation measures of tax administration for business transactions of affiliated enterprises, and the implementation rules of booking pricing for business networks of affiliated enterprises. These specific laws and regulations provide the basis for combating such tactics as price shifting and capital weakening commonly used by multinational corporations to avoid taxes[5].

3.2. China's Current Regulatory Measures On Tax Avoidance By Multinational Corporations

The Chinese government has continuously improved its anti-tax avoidance regulatory measures. For example, the Chinese government has implemented an international tax collection and administration cooperation mechanism, strengthened supervision and investigation of cross-border transactions of enterprises, and imposed penalties and sanctions on enterprises that violate the law.

Strengthening information disclosure requirements: The Chinese government requires multinational companies to disclose information in accordance with regulations and submit relevant supporting documents when paying fees to overseas affiliates. This helps prevent multinationals from using fake transactions or fictitious fees to shift profits, thereby reducing tax avoidance[7].

Strengthening audit supervision: The Chinese government has strengthened supervision over accounting firms and other intermediary institutions, requiring them to strictly abide by the code of professional ethics and industry norms, and ensure the authenticity and reliability of audit reports. At the same time, the Chinese government has increased penalties for violations, raising the cost of breaking the law.

Promoting international cooperation: The Chinese government actively cooperates with governments of other countries, international organizations and non-governmental organizations to

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combat tax avoidance by multinational corporations. For example, the Chinese government has participated in the establishment of the global Anti-tax avoidance Coalition and worked with other countries to formulate and improve anti-tax avoidance laws and policies.

4. Inadequacy of China's Current Regulation And Suggestions

4.1. China's Current Inadequacy In Tackling Tax Avoidance By Multinational Corporations

From a legal standpoint,at present, the legal provisions of tax avoidance in China are at a different level. Most specific provisions of tax avoidance are scattered in departmental regulations. There are contradictions between the legal level,for example,the new law and the old law about tax avoidance identification binary standard. There is confusion in the tax avoidance legislation, which is not conducive to the tax authorities to fulfil the duty of tax collection and management and give multinationals an opportunity to use.

The tax law of our country does not clearly stipulate the criteria for the identification of tax avoidance.the provisions of the Enterprise Income Tax Law and the Special Measures on the principle of reasonable business purpose are contradictory, and domestic scholars hold different opinions on the application of the principle of economic substance and the principle of reasonable business purpose.

China's tax law does not clearly identify the burden of proof of tax avoidance, that is, it is not divided between the tax authorities and multinational companies[8].The burden of proof is assigned to each other, resulting in frequent conflicts.

The above is mainly due to China's inadequacies in law.In fact, China's shortcomings are also reflected in many other specific aspects. Here are a few important aspects.

The training and selection of tax personnel in China is an important issue. Many tax personnel do not have a deep understanding of tax avoidance. In the process of tax review, it is easy to be fooled by multinational enterprises.

China's current intelligence network on tax avoidance by multinational companies is woefully inadequate. The slow response to the frequently changing international reservation price leads to the prominent problem of information contradiction in tax review. In this regard, some developed countries have been exploring for a long time and have accumulated richer experience.

4.2. Suggestions On Improving The Legal Regulation of International Tax Avoidance By Multinational Corporations In China

The most fundamental measure to deal with the problem of tax avoidance by multinational corporations in China is to improve China's laws in this regard, form a reasonable and complete legal system, and be precise and clear in both formal laws and enforcement regulations.

Specific operations should include the following points:

4.2.1. Reform within China

Firstly,re-sort out the relationship between laws and rectify the contradictions between upper and lower technical laws. In addition, China should update laws in a timely manner and replace outdated old laws with new ones as soon as possible.China should unify the enterprise income tax law with the following administrative regulations on tax avoidance and codify the criteria for tax avoidance as soon as possible.

Secondly,provide detailed judicial interpretation of specific concepts in tax avoidance of multinational corporations , such as the principle of economic substance and the principle of reasonable business purpose, and clarify the boundaries of legal provisions. This can provide a better legal basis for the work of tax enforcement departments.

Thirdly,clearly delineate the burden of proof between tax authorities and multinational corporations. In the administrative regulations of the tax authorities, the responsibilities of the tax authorities and the boundaries of the exercise of rights should be clarified to reduce the contradictions between the tax authorities and multinational enterprises In order to better maintain the normal order of taxation,.in the tax inspection stage, tax authorities as administrative law enforcement agencies, bear the main burden of proof, taxpayers bear the burden of proof for reasonable commercial purposes.

4.2.2. Actions Outside of China

Multinational corporations operate all over the world, and it is often difficult for a country to grasp the actual situation of tax avoidance, so it needs to rely on relevant foreign tax authorities to cooperate bilaterally and multilaterally and exchange information[9].

Cooperate with developed countries to establish international anti-tax avoidance cooperation. Information sharing with more countries, thereby reducing the leeway for transfer pricing.[10]In this regard, China can learn from mature economies such as the United States, the European Union, and Japan. Learn from their laws and anti-tax avoidance mechanisms, while combining with China's specific national conditions to reform the anti-tax avoidance mechanism.

In addition, China should pay attention to the role of large accounting firms and update accounting standards in time. Apply updated international accounting standards to reduce tax conflicts. Of course, tax professionals-especially large accountancy, legal and securities firms-ought to do much more to address tax avoidance than merely comply with existing legislation[11].

5. Conclusion

Under the background of economic globalization in the 21st century, multinational corporations develop rapidly and have become an important economic component. However, multinational companies continue to seek differences between international legal provisions and economic and trade agreements, and use transfer pricing, capital weakening and other ways to avoid taxes among countries, which is extremely harmful, will reduce the tax revenue of the host country, hinder the development of other enterprises in the same field, and destroy the tax order. Because of the large size of multinational enterprises, the economic destructive power brought by them is very strong. Therefore, this problem deserves attention.

The main content of this paper is to analyze the specific definition of tax avoidance behavior of multinational corporations, and explain the specific tax avoidance means and harm. At the same time, according to the situation in China, it analyzes the deficiencies of China's current laws and tax behaviors, and gives corresponding suggestions.

Although China has made long-term efforts in tax reform, there are still self-contradictions in tax law, and the concept of responsibility is unclear. Therefore, in view of these situations, the most fundamental measure is to improve relevant laws and introduce specific legal interpretations of relevant words. At the same time, the rights and responsibilities of tax authorities should be clearly defined. In addition, China should pay attention to cooperating with other countries to fight tax avoidance by multinational companies.

China regards tax reform as an important position in its economic development strategy, so the tax law will certainly have a long-term development in the future. On the basis of this study, the future research can further explore the contradictions in China's tax law and make China's tax law more perfect.

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