What is a global minimum tax and what will it mean?

Time to fix how multinationals are taxed

Brenda Bloch-Young, OLLI Forum June 16, 2021

Why a global minimum tax?

Yellen: “time to end the race to the bottom”

- Major economies are aiming to discourage multinational corporations from shifting profits and tax revenues to low tax jurisdictions regardless of where the revenue is earned.
- The idea is twofold: reallocating taxing rights to countries where the economic activity takes place (rather than where firms choose to book profits) and setting a global minimum tax rate.
- The goal is a 15% tax rate, but that is still being discussed.
- US desire to defuse a transatlantic row over the taxation of digital services of large US tech firms

Remember the Tax Cuts and Jobs Act?

The intent was to lessen the benefit of shifting revenue

- Base erosion and profiting shifting refers to tax strategies used by multinational companies to exploit the mismatches in tax rules by shifting profits to low tax or no-tax locations where there is little or no economic activity. The OECD has been studying this issue since 2012.

- Transfer pricing is the setting of the price for goods and services sold between controlled entities. For example, if a subsidiary sells goods to a parent company, the cost of those goods is the transfer price. This is used to shift revenue and expenses.

- GILTI (Global Intangible Low-Taxed Income) provision was intended to establish a minimum tax to offset this practice of 10.5%. The question was would it be by country or in the aggregate.

The end of the tax havens?

2018 study concluded 40% of multinational overseas profits are artificially shifted to low tax countries

- Bermuda, British Virgin Islands, and the Cayman Islands are zero tax but rely on fees from large corps and lawyers, accountants, and service providers to insurance and financial services corporations.

- EU countries - Ireland and Cyprus at 12.5% as well as Luxembourg, the Netherlands, and Switzerland have individual arrangements with multinationals.

- Hong Kong has several corporate tax rates with the highest being 15% and Singapore is at 17%

Public sentiment

Both in the US and the EU

- This OECD plan puts Ireland and a few other EU countries in a bind yet there is over whelming support for some minimum tax rate.
- In the US, we already have a minimum tax on intangible assets offshore - GILTI rate is 10.5%
- Biden's plan would be apply it on a country by country basis rather than in the aggregate.

How would a global minimum tax work?

There are still many open issues

- The 15% rate would apply to overseas profits
- This would allow each country flexibility in the home country corporate tax rate
- OECD stated that there is broad agreement in the framework but the 15% rate remains open for further discussion
- Other open topics are whether it would apply to investment funds and real estate investment trusts.

What’s next?

This will not happen soon

- The G20 meets in Venice next month to continue discussions
- The OECD is much larger but the G20 is the place to gain acceptance
- The G7 did not comment on the proposed EU digital services tax on big tech companies (the US is pushing for this to be scrapped as part of the deal)
- A global minimum tax impacts tax treaties (tax treaty approval requires a 2/3 majority.)

Conclusion

A good or bad idea? Either, it will take time

- OECD estimates that $240B of tax revenue is currently avoided
- US taxpayers should care that tech or pharma income is magically swept away to Ireland or a shell company in the Caribbean
- Allocating taxing rights according to where corporations operate would be much harder to steer away to tax havens
- Without reform, distortion and disorder will continue
- WSJ Editorial Board views it solely as an attack on large US tech firms