New Global Tax Accord Takes Shape

After more than four years of international negotiations taking place mostly behind the scenes, 132 countries — representing more than 90% of worldwide gross domestic product (GDP) and including the Group of 20 (G20) large economies — recently agreed to a new plan to reform international tax laws in an effort to "ensure that multinational enterprises pay a fair share of tax wherever they operate."[1]

The negotiations, overseen by the Paris-based Organisation for Economic Co-operation and Development (OECD), represent the most significant attempt in over a century to overhaul the global tax system and bring international tax policy into the modern digital age. The accord has the potential to reshape global commerce.[2]

THE PROPOSED 15% GLOBAL MINIMUM CORPORATE TAX RATE IS INTENDED TO DISCOURAGE MULTINATIONAL COMPANIES FROM SETTING UP THEIR OPERATIONS IN FOREIGN COUNTRIES WITH THE LOWEST TAX RATES.

What is the crux of the new global tax agreement?

The global agreement has two main pillars. The first would require large, multinational enterprises (including digital companies) to pay taxes in countries where their goods or services are sold and where they earn profits, even if they have no physical presence there. This provision is aimed primarily at large U.S. tech companies that sell their goods and services abroad, and is intended to supercede attempted regulation by other countries that are already in the process of trying to collect taxes on these companies.[1]

The second pillar, proposed by the United States, calls for a 15% global minimum corporate tax rate in an effort to prevent multinational companies from shopping for a country or jurisdiction with the lowest tax rates, a phenomenon U.S. Treasury Secretary Janet Yellen described as a "race to the bottom."[2]

President Biden added: "With a global minimum tax in place, multinational corporations will no longer be able to pit countries against one another in a bid to push tax rates down and protect their profits at the expense of public revenue."[2]

[1] OECD.org, 2021
[2] *The New York Times*, July 8, 2021

The OECD estimated that raising the global minimum corporate tax rate to 15% would generate an estimated $150 billion in additional global tax revenues each year. It stated that the "package will provide much-needed support to governments needing to raise necessary revenues to repair their budgets and their balance sheets while investing in essential public services, infrastructure and the measures necessary to help optimize the strength and the quality of the post-COVID recovery."[1]

What countries are on board?

All the G20 economies, representing over 75% of global trade, have endorsed the deal. They include the United States, Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, Republic of Korea, Mexico, Russia, Saudi Arabia, South Africa, Turkey, the United Kingdom, and most countries of the European Union.[3] In all, 132 countries are in favor.

However, several countries with low corporate tax rates that currently operate as tax havens have not agreed to the deal, including Ireland, several Caribbean countries, Hungary, Estonia, Kenya, Nigeria, Peru, and Sri Lanka.[2] These smaller nations are attempting to secure a better deal to enable them to compete with larger countries and make up for the potential loss of any tax advantage. The refusal of Ireland, Hungary, and Estonia to sign on to a global corporate tax rate is a potential roadblock because of the European Union's requirement for unanimity on tax issues.[4]

Undoubtedly, there is a significant amount of work to be done to bring "holdout" nations on board. The Biden administration has pushed Congress to approve a new tax rule that would punish companies that operate in the United States but have headquarters in those holdout countries by significantly increasing their tax liabilities. The president has also pushed Congress to increase the minimum tax on revenue earned by U.S. companies outside the United States in an effort to help fund the $4 trillion infrastructure and economic agenda he hopes to pass this year.[2]

Has the new global tax agreement been enacted yet?

No. There are still significant, complex technical and policy details that need to be worked out, including how the plan will be executed and which U.S. multinational companies will be subject to the new rules on digital tax.

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[3] G20.org, 2021
[4] Bloomberg, July 11, 2021

In addition, the plan needs to be approved by Congress and the national legislatures of participating countries. In the United States, each pillar of the plan could be considered separately. According to Treasury Secretary Yellen, the provision for a 15% global minimum corporate tax rate could be included in a budget bill headed to Congress later in 2021, while the provision on digital taxation of multinational companies might be ready for Congress in the spring of 2022. A further wrinkle is that if the digital tax provision is considered an international treaty, it will require two-thirds approval in the Senate.[4]

In any event, the global tax accord is due to be finalized by G20 leaders at their next meeting in Rome in October 2021, with G20 finance ministers anticipating global implementation in 2023.[4]