Tax Policy Alert
(A supplement to Tax Policy Bulletin and Tax Insights from International Tax Services and Transfer Pricing)

OECD Secretariat seeks input on global minimum tax design

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In brief

The Organisation for Economic Co-operation and Development (OECD) Secretariat on 8 November, published *Public consultation document: Global Anti-Base Erosion Proposal ('GloBE') (Pillar Two)* ('the Consultation') which seeks stakeholders' views on the introduction of common global minimum tax rules across the more than 130 countries participating in the OECD Inclusive Framework. Such rules would operate through top up taxes and other defensive measures where a multinational group's income is not subject to sufficiently high levels of tax. Together, these rules are known as the GloBE proposal.

The Consultation is the second part of the OECD's efforts to develop a two-pronged solution (alongside 'Pillar 1' Proposals, which seek to rewrite profit allocation rules for large 'consumer facing' businesses) to the tax challenges arising as a result of globalisation and digitalisation. Unlike the Pillar 1 proposals, however, this latest consultation envisions minimum tax rules that apply to large international businesses in all sectors (subject to potential carve-outs) and could therefore significantly increase tax and compliance costs for an even wider range of businesses.

In detail

The proposal

The Consultation makes clear that it only addresses part of the Pillar 2 issues set out in the May 2019 Programme of Work, focusing primarily on the development of an 'income inclusion' rule, which would seek to top up the foreign taxes paid by a business' overseas branches or controlled entities to a minimum rate. Subject to consultation, the starting point for such a calculation appears to be financial accounts, but it is an open question whether these would be local accounts, or the consolidated accounts of the group's ultimate parent entity.

While the broader GloBE proposal also includes rules to deny tax or treaty benefits deductions where the recipient of a payment is not sufficiently taxed (the 'undertaxed payments rule' and 'subject to tax' rules), and a new treaty rule to allow residence countries to top up taxes on income attributable to foreign branches' immovable property (the 'switch-over' rule), the focus of the Consultation is primarily the income inclusion rule; where comments are made on the other elements of the GloBE proposal they are limited to enquiries on whether different approaches would need to be taken in relation to them.

Broadly, there are three key technical areas covered by the Consultation:

- *Financial accounts:* The Consultation recognises there is a balance to strike between simplicity and the accuracy of identifying truly low taxed profits, given the differences between accounting standards and tax bases. For differences that would not even out over time (e.g., non-taxable income, or non-deductible expenses), the Consultation suggests that removing certain amounts as standard could be an appropriate middle ground. For differences that would even out over time (e.g., where profits are recognised in different years for tax and accounting purposes), three options are suggested: carrying forward any excess taxes paid for offset in future years, using IFRS deferred tax accounting standards rather than the cash tax recognised in the accounts, or averaging over multiple years.
- *Blending:* The Consultation also seeks views on the degree of 'blending' that should be included, which is essentially determining whether groups could consolidate taxes at an entity, jurisdiction, or worldwide basis in order to determine whether the effective taxes paid on profits are sufficiently high. The factors under consideration in this regard include the cost of compliance, the impact on volatility, and the allocation of profits and taxes between entities and jurisdictions.
- *Carve-outs:* The Consultation recognises that carve-outs may be required, and that there is often a trade off between certainty and complexity. No industries or regimes are specifically identified as potential targets for carve-outs, but broad questions are raised for stakeholders to consider, such as whether carve-outs may be appropriate on the basis of a group's global size or industry, or the scale of local presence, as well as the potential behavioural impacts that carve-outs may have. It is worth noting that no mention is made of the rumoured carve-out for the US GILTI regime. Note that the Consultation does not mention the US GILTI regime.

Next steps

Following a period to 2 December 2019 for stakeholders to provide written comments, a public consultation meeting will take place in Paris on 9 December 2019. The OECD seeks political agreement among the members of the Inclusive Framework on the basic architecture of the proposed changes in January 2020 so that more detailed technical work on the mechanics of both Pillars can take place throughout 2020.

The takeaway

While this workstream is being delivered under the OECD's *"Tax Challenges Arising from the Digitalisation of the Economy"* project, the impact of the proposals being implemented go far beyond highly digitalised businesses; these proposals seek to address more fundamental concerns that the BEPS Project did not provide an adequate solution to the risks of activities and profits being moved to low- (or no) tax jurisdictions. The potential impact should be heeded by all international businesses - including those who do not operate in low-tax jurisdictions and those already subject to US GILTI rules.

Levels of enthusiasm for Pillar 2 appear to be mixed among the Inclusive Framework's member countries (although with clear support from some key G7 countries), but there is fairly broad political support for the wider package, and the OECD is working on the basis that both pillars would be agreed together. While some countries are keen to ensure that all income is taxed at a minimum rate, others want to take a broader view that allows countries the flexibility to set lower rates from which groups suffering otherwise higher rates could benefit. Unlike the Pillar 1 Proposals that seek to reallocate tax base between countries, elements of Pillar 2 could be implemented by a smaller group of countries.

The rate of tax to which profits in scope must be topped up remains a key challenge for the Inclusive Framework to agree (as different rates would be expected to bring different regimes within scope), but it is not being addressed as part of the current consultation. The interaction of the income inclusion rule with the other rules (and all their interactions with the Pillar 1 Proposals) is another key area that will need to be addressed but is not consulted on at this time.

There is significant complexity in each of the Pillar 1 and Pillar 2 proposals, and in their interaction with each other. Taxpayers will want to analyse the potential impact on their businesses, and the outstanding challenges outlined above - in terms of the impact of both prospective tax liability and increased compliance and filing burden. Given the wide-ranging implications of this project, taxpayers will want to make their views known to the OECD and national governments as the project moves forward in an effort to achieve a stable and sustainable consensus agreement.

Let's talk

For a deeper discussion of how these issues might affect your business, please call your usual PwC contact. If you don't have one or would otherwise prefer to speak to one of our global specialists, please contact one of the people whose details are set out below:

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