FISCAL AFFAIRS

The GloBE Agreement: Opportunities and Challenges for Developing Countries

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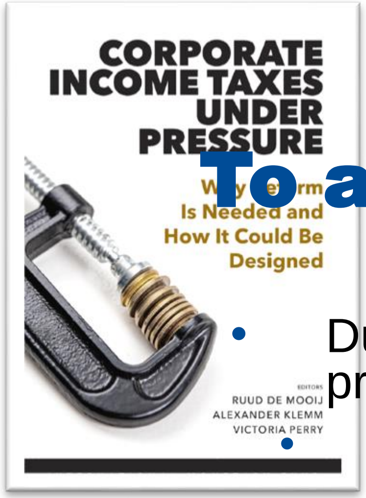
Big picture: Where are we?

- 137 countries have agreed to a two-pillar corporate tax reform

- Pillar One:
  - Revised allocation of taxing rights to market jurisdictions

- **Pillar Two**:
  - Global anti-base-erosion minimum tax (the GloBE) of 15 percent



To alleviate profit shifting and tax competition…

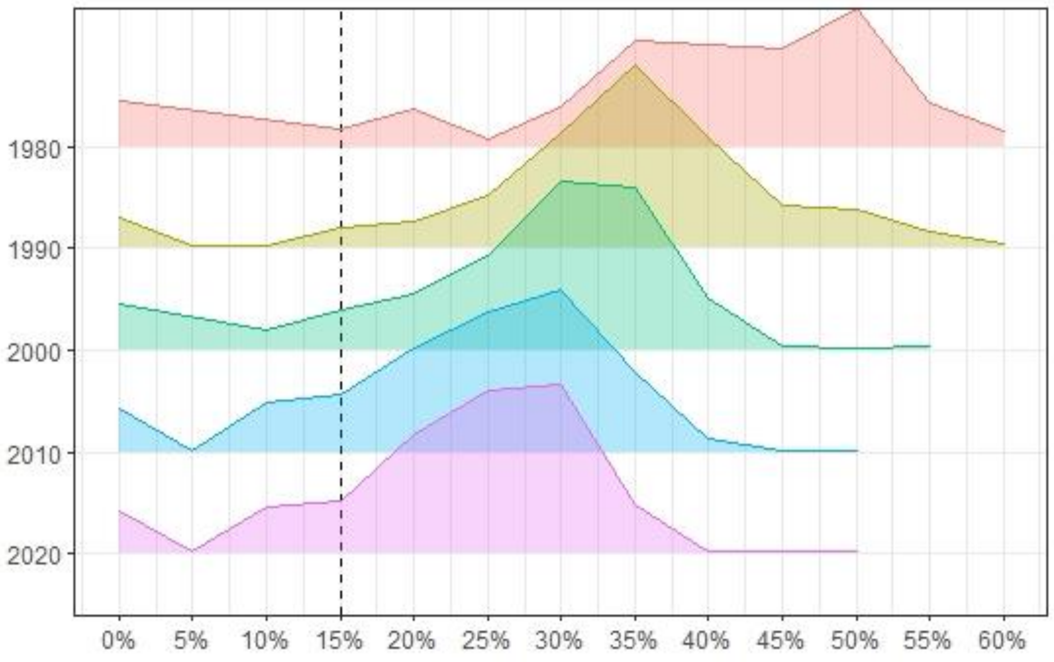
- Due to perennial problems under the prevailing source-based territorial system:
  - arm's length principle, mobility of reported profits, mobility of capital…

- A minimum tax caps the gains from profit shifting while putting a floor on tax competition (IMF 2019, 2021)

- Milestones since the global agreement: model rules for the GLoBE rules (December 2021); Commentary and Examples (March 2022); public consultation on Implementation Framework (this month)

- Aiming for coming into effect in 2023, though lots of challenges remain…

Corporate Income Tax Rate by Decade



What's in the GloBE?

- A common approach: optional; but needs to accept adoptions by others

- Applies to MNCs with consolidated revenue ≥ EUR 750 million
  - Excludes international shipping income + other entities

GloBE Top-Up Tax

- Per jurisdiction, profits of MNEs if *effectively* taxed below 15%
  - ETR: financial accounting income/tax expense with adjustments

- Top-up tax on *excess* profits to reach the minimum rate of 15%
  - Carveout: 8% of tangible assets, 10% of payroll, both falling to 5% over 10 years

and who gets to charge the GloBE?

GloBE Top-Up Tax

Resident countries, based on the Income Inclusion Rule (IIR):
- priority given to MNC’s home and intermediate parent countries

Source countries, based on the undertaxed payment rule (UTPR):
- charge mechanism to be determined
- allocated across jurisdictions based on relative employees and tangible assets

the GloBE rules: IIR + UTPR

The STTR reduces the total GloBE tax

GloBE Top-Up Tax

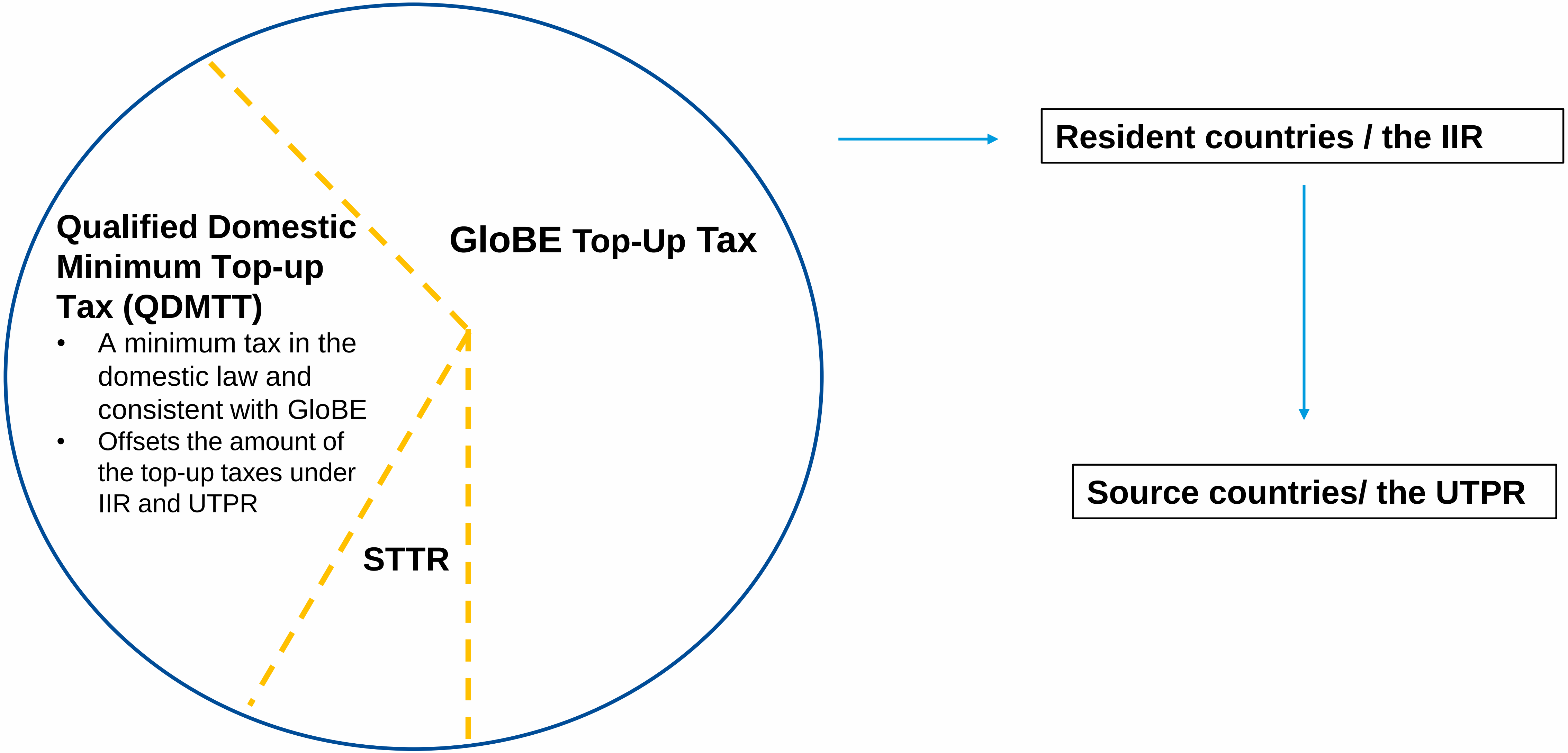
Resident countries / the IIR

Source countries/ the UTPR

Subject to Tax Rule (STTR):

- Top-up tax (e.g. via withholding) in source countries on interest, royalties and other defined payments
- 9%, reduced by current tax on the payment
- Treaty based, creditable against the GloBE tax…
- …with limited scope and revenue

and so does the QDMTT



Moving forward

GloBE

- Implementation Framework by end 2022 (detailed filing obligations, multilateral review processes and safe-harbors)
  - although GILTI co-existence remains to be addressed…
- IIR effective in 2023
- UTPR coming into effect in 2024
- Lots of actions already at the national/regional level: UK, Australia, the EU, and US

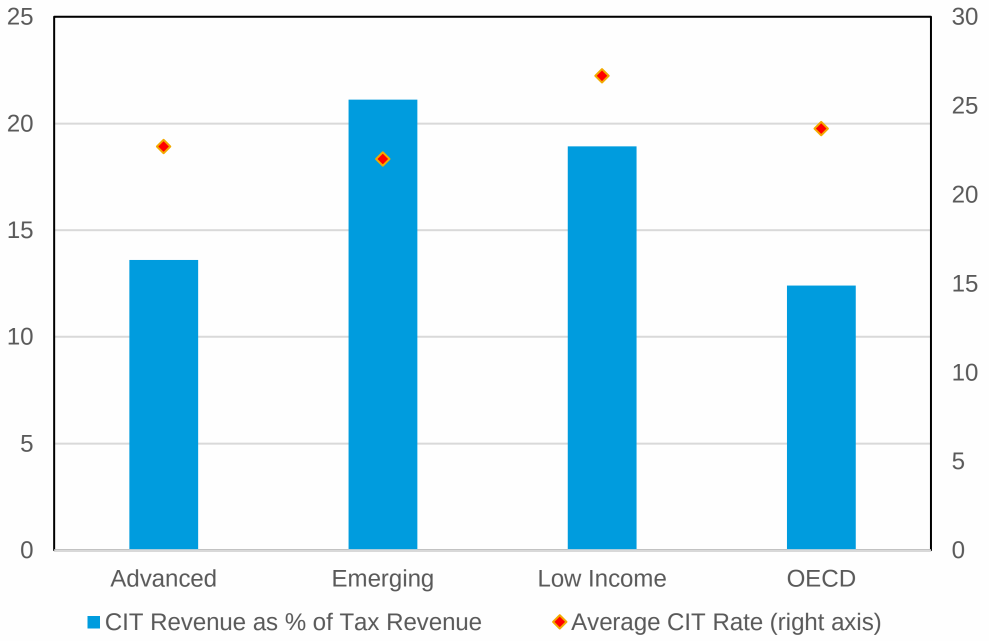
STTR

- Finalize rule extended to March(?) 2022
- “Defined set of other payments” remains to be defined…
- Public consultation once the design has been stabilized

What's in for developing countries?

Developing countries lose more %GDP to BEPS (Crivelli, de Mooij, and Keen, 2015), while relying more on CIT revenue…

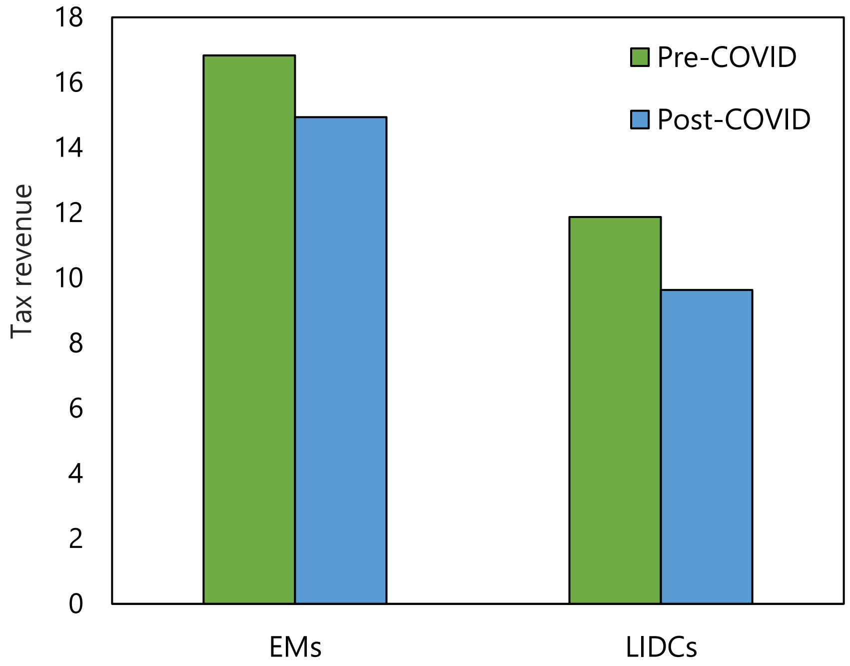
CIT Revenues as a share of Total Revenue and CIT Rates (2019)



IMF Fiscal Monitor Database

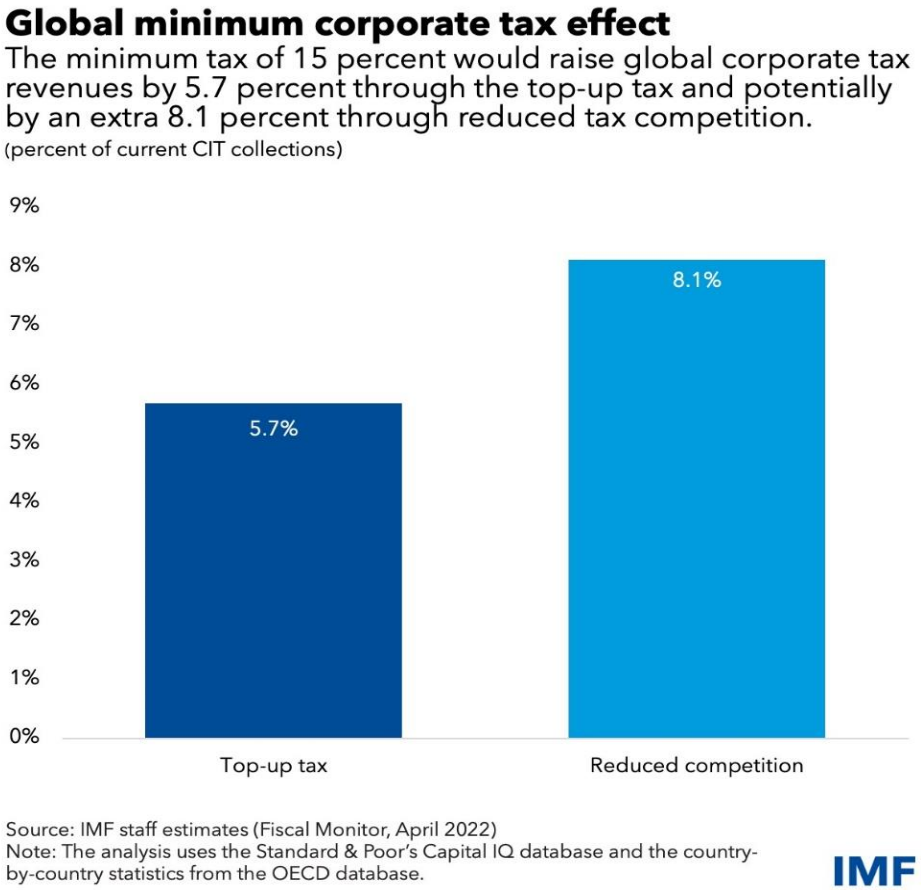
…and facing more revenue pressures post-Covid

Tax revenue projection pre- and post COVID for 2020 (% GDP)



and how to share the GloBE?

- Global: $150 billion, 6% of CIT revenue
  - and likely higher through reduced tax competition…



CHAPTER 2 COORDINATING TAXATION ACROSS BORDERS

Introduction

International coordination on tax matters is needed now more than ever. National governments share challenges in securing revenues, addressing inequalities, and curbing greenhouse gas emissions. Succeeding in these efforts increasingly requires dealing with pressures that cannot be stopped by national borders. These cross-border spillovers—the effects of one country's

The rising need for international coordination on taxation stems from three developments in the past few decades:

- *Globalization and digitalization* of the economy have created opportunities for development but have also intensified the mobility of the income tax base (profits and personal income) and factors of production (capital and, increasingly, people). Global firms draw on global supply chains to serve global markets, with increased possibilities for generating large profits without physical (taxable) presence. All of these developments have tax implications, which, without coordination, can adversely affect efficiency, distribution, and in some cases, international economic and trade relations.
- *Salience of aggressive tax avoidance and outright tax evasion* has raised demands for fairer and less unequal societies. This call is fueled not only by leaks of documents showing widespread egregious use of offshore opaque structures, but also by systematic evidence of weak tax compliance by rich individuals. As it becomes possible to transfer funds across borders through virtual assets with near anonymity, tax administrations—especially in developing countries—struggle to keep up, even as they upgrade their own use of technology to collect and process data to identify compliance risks.
- *Climate change*—a vital global challenge—demands urgent measures to curtail emissions. Carbon taxation (charges on the carbon content of fossil fuel supply) or other carbon-pricing or regulatory policies aimed at discouraging emissions can make a difference only if adopted by enough large emitters. If carbon pricing cannot be internationally coordinated, then other unilateral approaches would likewise entail international elements.

This chapter opens with brief general considerations for addressing cross-border tax spillovers. Next, the chapter addresses how international coordination can improve the taxation of multinationals and individuals and reduce greenhouse gas emissions. The discussion is framed around improving existing international coordination arrangements, with special attention to the standpoint of developing countries.

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and how to share the GloBE?

- How it will be shared by developing countries is hard to predict…
  - The rule order
  - Adoption of rules by other countries
  - MNE response: less profit shifting + changes in where to book profits + more costly investment
  - Dynamic domestic responses by others
    - low-tax countries: raise to the minimum
    - high-tax countries: halt/reverse the downward trend
    - developing countries: a strong case of reconsidering tax incentives

CHAPTER 2

COORDINATING TAXATION ACROSS BORDERS

Introduction

International coordination on tax matters is needed now more than ever. National governments share challenges in securing revenues, addressing inequalities, and curbing greenhouse gas emissions. Succeeding in these efforts increasingly requires dealing with pressures that cannot be stopped by national borders. These cross-border spillovers—the effects of one country's actions on other countries—necessitate international coordination. The most pressing areas for coordination are the taxation of multinational enterprises (multinationals) and individuals, as well as carbon pricing.

Recent achievements toward international tax coordination include the agreement in October 2021 under the Organisation for Economic Co-operation and Development (OECD)/Group of Twenty (G20) Inclusive Framework to reform the taxation of multinationals (OECD 2021d), international agreements to exchange information led by the Global Forum, and countries' pledges under the Paris Agreement and the UN Climate Change Conference at Glasgow (COP26) to reduce emissions.[1] However, much more should be done.

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Under the overall guidance of Paolo Mauro (Deputy Director) and Paulo Medas (Division Chief), this chapter was prepared by staff from the Fiscal Affairs Department (FAD) with contributions by staff from the Legal Department (LEG). The lead author of this chapter is Shafik Hebous (FAD), with contributions from Sebastian Beer (FAD), Susan Betts (FAD), Maria Coelho (FAD), Cory Hillier (LEG), Pierre Kerjean (FAD), Tamas Kulcsar (FAD), Li Liu (FAD), Jan Loeprick (FAD), Andrew Okello (FAD), Ian Parry (FAD), Roberto Piazza (FAD), Dinar Prihardini (FAD), Nate Vernon (FAD), Christophe Waerzeggers (LEG), and Karlygash Zhunussova (FAD), as well as inputs by Simon Black and the Financial Integrity Group (LEG) and research assistance by Julieta Raquel Ladronis (FAD).

[1]The OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS) was established in 2016 for countries to collaborate on implementing the initiative (it currently has 141 member countries and 14 observer organizations). The Global Forum refers to the Global Forum on Transparency and Exchange of Information for Tax Purposes, founded in 2000 (currently with 163 members). *COP26* is the 26th Conference of the Parties (the supreme decision-making body of the United Nations Framework Convention on Climate Change, or UNFCCC). The *Paris Agreement* is a treaty adopted by 196 parties at the COP21 in 2015.

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Challenges for developing countries

- To adopt, or not to adopt (the GloBE rules), for a highly diverse group…
  - do you host many MNE headquarters?
  - do you have a low effective tax?
  - do you have many treaties and what about the patterns of outbound payments?
  - and when: who are your largest investing countries and are they moving towards a GloBE?

- Challenges for implementation
  - information/data availability
  - capacity limitations…

- Simpler alternatives?
  - alternative minimum tax, raising WHT, revising existing treaties, OIT provision
  - reform tax incentives

- Building administrative capacity to enforce rules
  - for existing ones and the new rules if adopted