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Double taxation still needs to be addressed following G20 meeting

Tax authorities have many questions to settle in negotiations to tackle the risk of double taxation across jurisdictions when implementing OECD's tax framework.

By **Leanna Reeves**
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Global tax policymakers must tackle the risk of double taxation

The July G20 meeting marked the endorsement of the OECD's two-pillar solution, but with over 130 jurisdictions joining the agreement, settling some of the key details remains a challenge for global tax policymakers ahead of the next G20 meeting in October 2021.

Adopting the two-pillar tax framework will require a significant level of collaboration from tax authorities to mitigate the risk of a double taxation.

"It is one thing to agree a headline approach to change the international tax regime, but a very different thing to achieve consensus on methods of calculation, apportionment, exclusions, and the like," said Matt Stringer, head of international tax at Grant Thornton.

To this date, members of the Inclusive Framework (IF) have agreed to adopt pillar one – which aims at reallocating profits of multinational enterprises (MNEs) with a global turnover over €20 billion ($23.6 billion) – and pillar two, set to impose a global minimum tax rate of at least 15% on multinationals within the €750 million threshold.

Tax policymakers are yet expected to deliver further details around the agreement, which could be critical for the final implementation of the tax framework.

“Ironing out the details – there are several make or break points in the details; marketing and distribution safe harbour, tax certainty for local subsidiaries in developing countries, tax credit mechanisms, revenue sourcing rules, computation of residual profits, carry forward of losses,” said Seema Kejriwal Jariwala, partner at BMR Legal.

The IF could adjust to design a pillar one computation around every in-scope company, according to Jariwala. Pillar two could also increase disputes across the globe, meaning further clarity will be required to prevent countries from being “over-zealous” in their attempt to apply the Subject to Tax Rule (STTR) or the Undertaxed Payments Rule (UTPR), said Jariwala.

“Substance-based carve-outs are typically very fact specific and there is no one-size fits all solution to it. Creating a long list of exceptions creates complications in understanding and implementation. Getting 130 countries to agree may be an additional challenge,” she added.

Jurisdictions will need to assess which country will lose tax revenue under pillar one and what specific rate will be applied under pillar two to determine how the rule gets implemented locally.

The EU block also encompasses another potential obstacle for tax policymakers due to holdout countries, meaning a Directive could be needed.

Taxpayers will need certainty to implement both pillars, particularly in regards to where they pay the tax and who they pay it to.

“The compliance and practicalities of how you implement some of this is going to be critical going forward, and we don’t get that from the G20. It needs to be a clear message back to the OECD to make sure they develop that for easy implementation and consistency across each of the countries who will implement the rules,” said Andrea Tolley, partner at KPMG UK.

Above all, adopting the rules will require “an unprecedented degree of cooperation and coordination among tax authorities”, according to Kate Barton, global vice chair at EY. This creates a substantial risk of increased uncertainty and complex tax controversy.

Risk of disparity

Countries demanding a higher minimum tax rate, for instance, could lead to disparities between jurisdictions, especially developing countries versus developed economies.

The African Tax Administration Forum (ATAF) has recently released a statement suggesting the minimum global tax rate should be of at least 20%. The ATAF also called for at least 35% of the profits of residuary profits, in excess of 10%, should be allocated to market jurisdictions.

Prior to the G20 meeting, US Treasury Secretary Jane Yellen also pushed for a higher global tax rate – from 15% to 20%.

Barton yet said it would be unlikely, following the July meeting, that jurisdictions demand a higher rate as they are concerned of potentially losing on a global consensus.

“I do think it would be difficult to get broad consensus on a higher minimum tax rate. It is already at a top end of what many countries are willing to agree on,” she said.

“It is unlikely that developing countries would push for a higher minimum given that in many cases their own subsidized rates hover around 15%. In India, corporate tax rate is 30, but under a production linked incentive scheme, the tax rate is 15% and under a patent box regime, the tax rate is only 10%,” added Jariwala.

James Ross, partner at McDermott Will & Emery, said countries could not risk not reaching a final agreement on the two-pillar solution. “There’s a real balancing act going here,” he said.

Most importantly, a lack of coordination amongst jurisdictions could lead to a global tax burden, in which the risk of double taxation will be enhanced. More details around pillar one and pillar two is therefore crucial to mitigate this risk, suggestedBarton.

“It is essential that the final agreement to be reached in October spells out the new rules in as much detail as possible. Beyond this, government policymakers need to give thought to the mechanisms that must be put in place to mitigate the risk of tax controversy or double taxation,” she said.

While the G20 meeting marks a significant step for tax authorities, further detail around the two pillars will be crucial in the final implementation of the tax framework.

“There have also been concerns expressed by India and China, as well as many developing countries about some of the provisions. So, while the G7, IF and now the G20 meetings, were all important steps along the road, there is still much more work to be done,” said Will Morris, PwC deputy global tax leader.

The potential disparity across jurisdictions, led by countries calling for a higher global minimum rate and changes to pillar one, will need to be tackled by tax authorities to mitigate the risk of double taxation and ensure a final consensus in October is reached.

Further negotiation and detail around the two-pillar solution can be expected, with possible challenges along the way.