



FACTCOALITION

Financial Accountability & Corporate Transparency

December 14, 2020

Mr. Angel Gurría
Secretary-General, OECD
c/o International Co-operation and Tax Administration Division
Centre for Tax Policy and Administration
2, rue André Pascal
75016 Paris, France

Re: Comment on the Pillar Two Blueprint

Dear Secretary-General Gurría,

On behalf of the Financial Accountability and Corporate Transparency (FACT) Coalition, we appreciate the opportunity to comment on the BEPS Pillar Two Blueprint. The FACT Coalition is a non-partisan alliance of more than 100 state, national, and international organizations in the United States working toward a fair tax system that addresses the challenges of a global economy and promoting policies to combat the harmful impacts of corrupt financial practices.¹

The FACT Coalition welcomes the progress made on the technical details of Pillar Two, and we strongly support the twin aims of the Global Anti-Base Erosion (GloBE) proposal: to curb tax avoidance and tax competition. To uphold these aims, the FACT Coalition urges negotiators to reach political agreement on a strongly designed global minimum tax framework, as outlined hereunder.

The current negotiations are an historic opportunity to establish a global minimum tax, given the growing consensus around Pillar Two relative to Pillar One. Pillar Two may also generate more revenue than Pillar One, and may do more to curb tax avoidance and tax competition. Progress on Pillar Two must be allowed to advance independently of negotiations on Pillar One.

The FACT Coalition makes the following recommendations regarding the Pillar Two Blueprint.

The GloBE Rate Should Not Be Less than 21 Percent.

Labor income and consumption are taxed at rates well above capital income throughout the world: not because this practice is more efficient or equitable, but in large part because capital is mobile. Pillar Two is meant to address that problem and help level the global playing field when it comes to corporate tax.

But the 12.5 percent minimum corporate tax rate suggested in the Pillar Two Blueprint is far too low to stave off either corporate tax avoidance or tax competition. As the global average statutory corporate tax rate is close to 25 percent, such a low minimum rate would leave plenty of room for corporations to

¹ For a full list of members, see here: <https://thefactcoalition.org/about-us/coalition-members-and-supporters>.

shift profits to low-tax countries, accountants to design mechanisms to recharacterize domestic income as offshore; and countries to lower their rates in a race to the minimum.

The existing political momentum behind Pillar Two will be exceedingly difficult to replicate in the future. It is therefore imperative to seize the moment and avoid setting a low minimum rate that will drag down corporate taxation far into the future. Corporations have for too long failed to contribute a reasonable share of tax revenue in the countries where they do business; GloBE offers a rare opportunity to redress years of corporate tax dodging.

The Pillar Two Blueprint should also be explicit that countries retain the right to unilaterally adopt a higher rate for both their income inclusion rule (IIR) and undertaxed payments rule (UTPR), with the understanding that the UTPR would not apply to corporations that pay the IIR to another country at the globally agreed minimum rate. The Blueprint is currently silent on this point, perhaps because it is taken for granted that sovereign states can set their own tax rates. The Blueprint should state explicitly that GloBE merely sets a minimum rate, which countries can choose to top up unilaterally, lest it be interpreted as an international agreement to constrain higher corporate rates.

GloBE should apply to all corporations.

It is not usual to apply taxes only to very large corporations. For example, the US GILTI does not have a size threshold. The proposed €750 million threshold for GloBE would exclude most corporations and result in a loss of revenue. It would also enable tax avoidance by entities below the threshold. While large corporations have more capacity to comply with GloBE's complexity, smaller corporations are less likely to have complex structures.

GloBE Should Be Designed with Jurisdictional Blending.

Jurisdictional blending is clearly more effective to fight tax avoidance and tax competition. The FACT Coalition therefore welcomes this important element of the Pillar Two Blueprint.

GloBE Should Not Have a Substance Carve-out.

The FACT Coalition opposes the proposed GloBE substance carve-out. There is no sound policy rationale for it and multiple arguments against it:

- (i) a carve-out will decrease revenue,
- (ii) it will blunt GloBE's protection against tax competition, and
- (iii) it will increase complexity and, hence, administrative costs.

We reject the misguided notion that GloBE should exclusively aim to counter profit shifting rather than also discourage tax competition. Both are problems; both needed to be addressed. That said, tax competition aimed at attracting real economic activities will still be possible, even with a strong GloBE that excludes any substance carve-out. GloBE will simply elevate the floor of that competition. That is, it will allow countries to raise their statutory rate while offering targeted tax incentives to reduce the effective tax rate to the GloBE rate. The substance carve-out simply lowers that initial floor with no real gain for tax authorities or civil society.

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GloBE Must Be Tweaked to Prevent Inversion Risks.

GloBE needs to be protected against inversions. Pillar Two should only allow countries to benefit from the IIR in cases where the country of registration of the ultimate parent is the same as that of the majority of the ultimate parent's beneficial owners. However, in the event of divergence, Pillar Two must prohibit the country benefiting from the IIR from being the country of registration of the ultimate parent corporation, and instead reward the country of residence of a majority of the ultimate parent's beneficial owners. If no country hosts at least 50% of the beneficial owners, the country collecting GloBE under the IIR should be the country from which the company is effectively managed.

The UTPR is supposed to protect countries from the risk of inversion (i.e., multinational corporations shifting their registration to a country that does not adopt GloBE). However, that protection may be too weak if the GloBE rate is insufficiently high or if a country unilaterally increases its rate above the global minimum.

Moreover, avoiding tax is only one motivation for registering in a tax haven. Corporations, particularly those of developing countries, may choose to register in countries with stronger legal systems; alternatively, corporations from more regulated countries may choose to register in a country that favors weaker regulations, thereby depriving their true home country from GloBE revenue. There is also a network effect, by which businesses tend to register in jurisdictions that can have already attracted other corporations whether due to their stronger legal systems or weaker regulations. While it is fair for investment hubs to attract a lot of business registrations, it would be unfair if they also capture a large share of GloBE revenue as a result.

GILTI Should Not Be Grandfathered into GloBE.

Finally, Pillar Two needs to address the GILTI problem. Clearly, it is best to have a single global standard, rather than two different systems – that's the whole point of the OECD effort. For that reason alone, GILTI should not be incorporated into the Pillar Two approach. In addition, GILTI has flaws that some U.S. policymakers intend to address domestically. Rather than enshrining a flawed structure within the Pillar Two process, it's better to have a strong, rational, unified global system. A global agreement that builds upon the stronger aspects of GILTI while strengthening the weaker ones (e.g., with jurisdictional blending, a higher rate, and no carve out), could serve as a template for U.S. policymakers.

Thank you very much for considering the Coalition's thoughts on this topic. Should you have any questions, please feel free to contact Erica Hanichak at ehanichak@thefactcoalition.org.

Sincerely,

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