



Global Minimum Tax Reform and the Future of Tax Competition

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Overview



As of 16 December 2022, 138 jurisdictions under the Base Erosion and Profit Shifting (BEPS) Inclusive Framework (IF) have committed to the Two-Pillar reform. Pillar Two introduces a global minimum tax rate of 15%, which will have a wide-reaching impact on tax competition. According to the OECD, Pillar Two ‘does not seek to eliminate tax competition, but puts multilaterally agreed limitation on it’.



Overview

- Comparison of Pillar Two with OECD's Previous Efforts to Combat Tax Competition
- The Fiscal Fail-safe of Pillar Two and Its Potential Restriction on Traditional Corporate Income Tax (CIT) Competition
- Remaining Scope for Tax Competition in the Post-Pillar Two Environment
- Towards a More Equitable and Efficient Tax Competition Landscape?

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Brief Introduction to Pillar Two

Objective: To address remaining BEPS challenges and put a floor on CIT competition

- Global anti-Base Erosion Rules (GloBE) rules
- Income Inclusion Rule (IIR)
 - Undertaxed Payment Rule (UTPR)

Subject to Tax
Rule (STTR)



Comparison of Pillar Two with OECD's Previous Efforts to Combat Tax Competition



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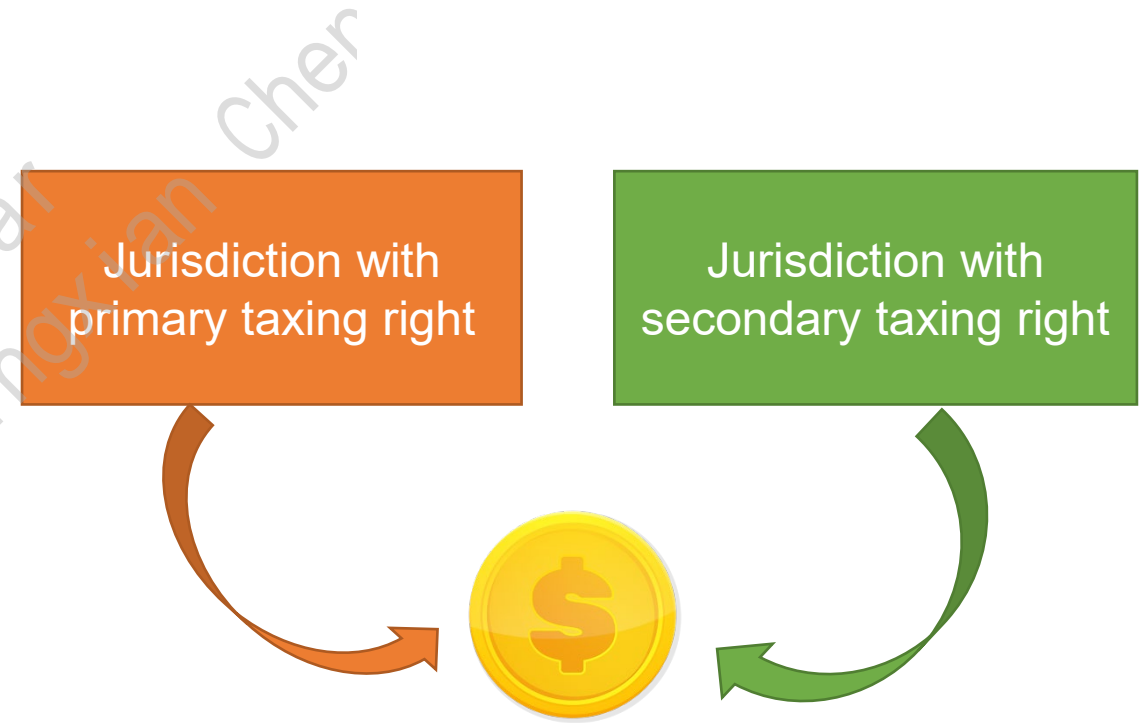
Comparison of Three Stages

	Pre-BEPS Stage	BEPS 1.0 Stage	BEPS 2.0 Stage
Main Documents	Report on Harmful Tax Competition: An Emerging Global Issue	BEPS Action 5 (and other actions)	Pillar Two
Regulatory Focus	Illegal tax evasion facilitated by tax secrecy	Harmful preferential tax regimes that lead to artificial profit shifting	CIT competition in both harmful (i.e., artificial profit shifting) and genuine (i.e., real investment shifting) cases
Regulatory Methods	List of uncooperative tax havens	Peer review mechanism	Fiscal fail-safe
Democratic Legitimacy	Significant legitimacy deficiencies	Support from 141 IF members	Support from 138 IF members

Game Theory and Fiscal Fail-safe



States are assumed to tax strategically (Tsilly Dagan, 2018)

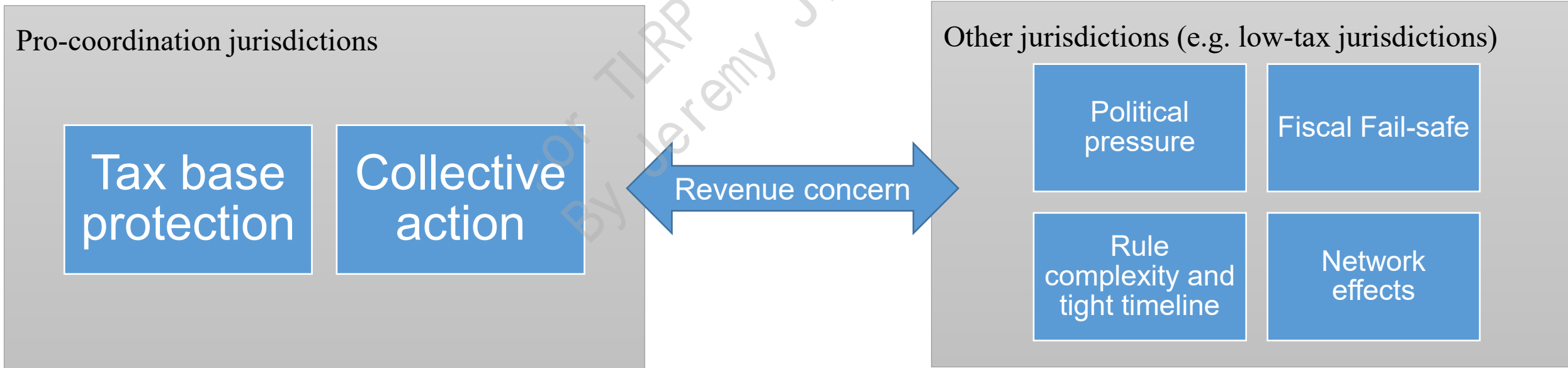


Fiscal Fail-safe (Ruth Mason, 2020)



Motivations behind the Consensus?

- Some explanations
 - Genuinely acting cooperatively to advance common interests (Wei Cui, 2022)
 - Gaining additional tax revenue (Jinyan Li, 2023)
- A more nuanced explanation?



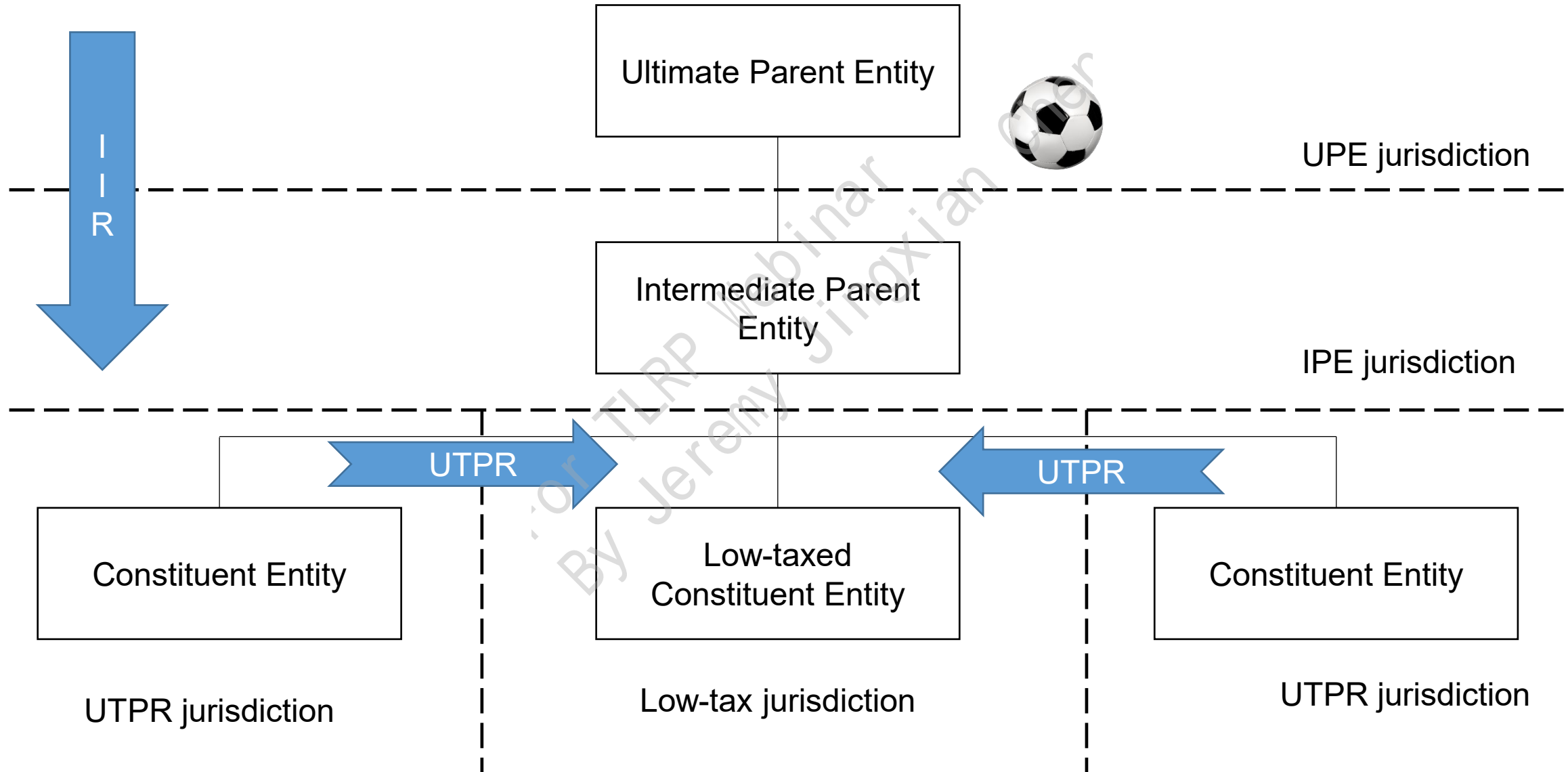


The Fiscal Fail-safe of Pillar Two and Its Potential Restriction on Traditional CIT Competition

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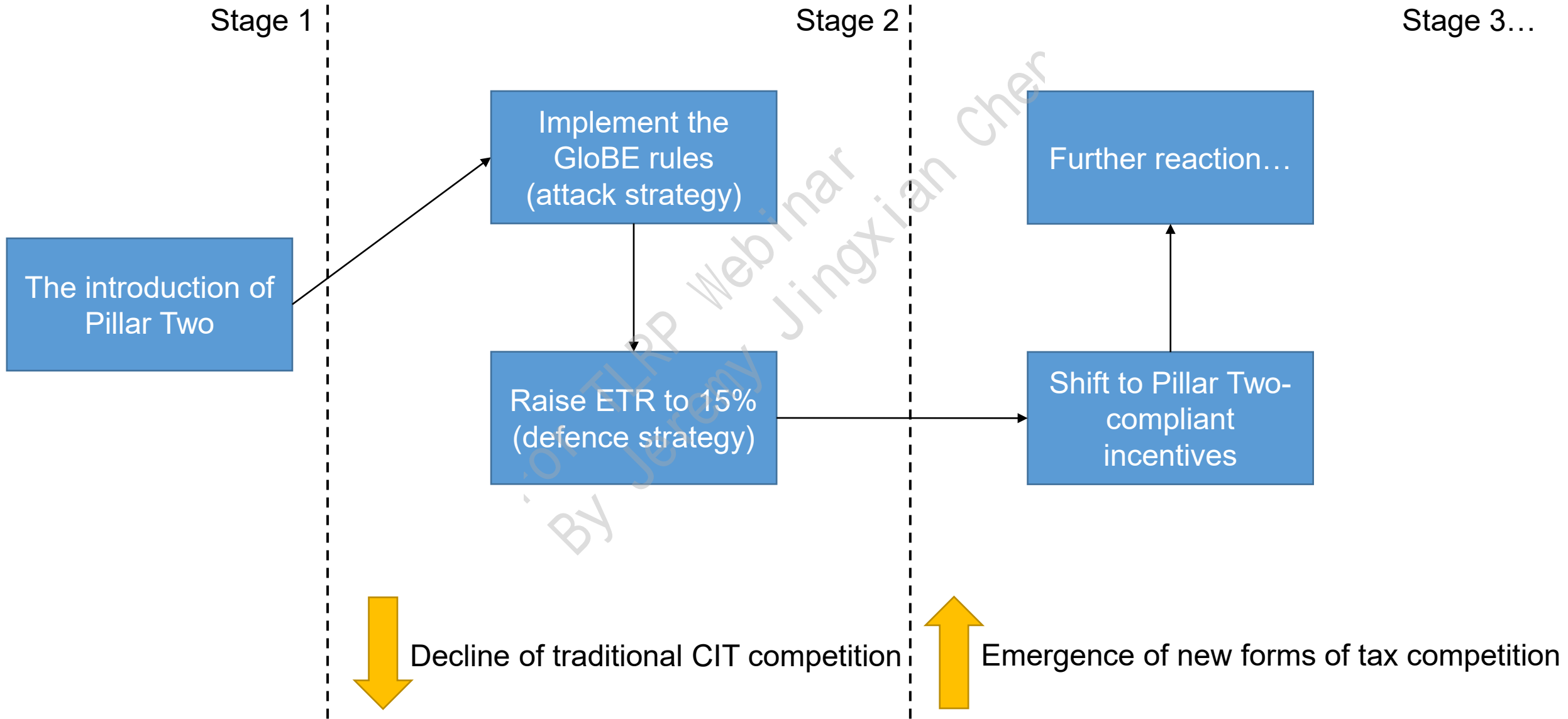


The Fiscal Fail-safe of Pillar Two





The Tax Strategic Game Created by Pillar Two





The Latest Practices of Jurisdictions

On Pillar Two, the global minimum tax is now a reality, with all 27 EU member states, as well as countries such as the United Kingdom, Switzerland, Japan, Korea, Singapore and many others moving forward with legislation. (OECD, 2023)

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“US, Europe To Go After Chinese Firms If Beijing Does Not Comply With Minimum Tax”

美国财长要抢劫中国企业？真相竟是这样！

The US Treasury Secretary wants to ‘rob’ Chinese enterprises?

原创 耿直哥 环球时报 2023-03-13 09:53 **What is the truth?**

近日，中国网络上出现了一种让许多网民相当愤怒和吃惊的说法。

该说法称，美国政府要对“明抢”了，因为美国财长耶伦近日承诺说，她要对在国际市场上有业务的中国企业追缴15%的国际业务税款。

然而，耿直哥核查后发现，此事的真相其实并不简单。

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Remaining Scope for Tax Competition in the Post-Pillar Two Environment

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Remaining Scope for Tax Competition

Multinational Small and Medium-Sized Enterprises Tax Incentives

International Shipping Tax Incentives

Incentives of Non-Covered Taxes

Qualified Refundable Tax Credits and Non-Tax Subsidy

Jurisdictional Blending Approach

Substance-based Income Exclusion

Domestic Minimum Tax



Multinational SMEs tax incentives

- The EUR€750 million threshold of Pillar Two
- 85% and 90% of MNE Groups outside the scope
- Internationalisation of SMEs
- Distortive impacts
 - Heterogeneity of SMEs
 - Complexity of tax system
 - Small-business trap



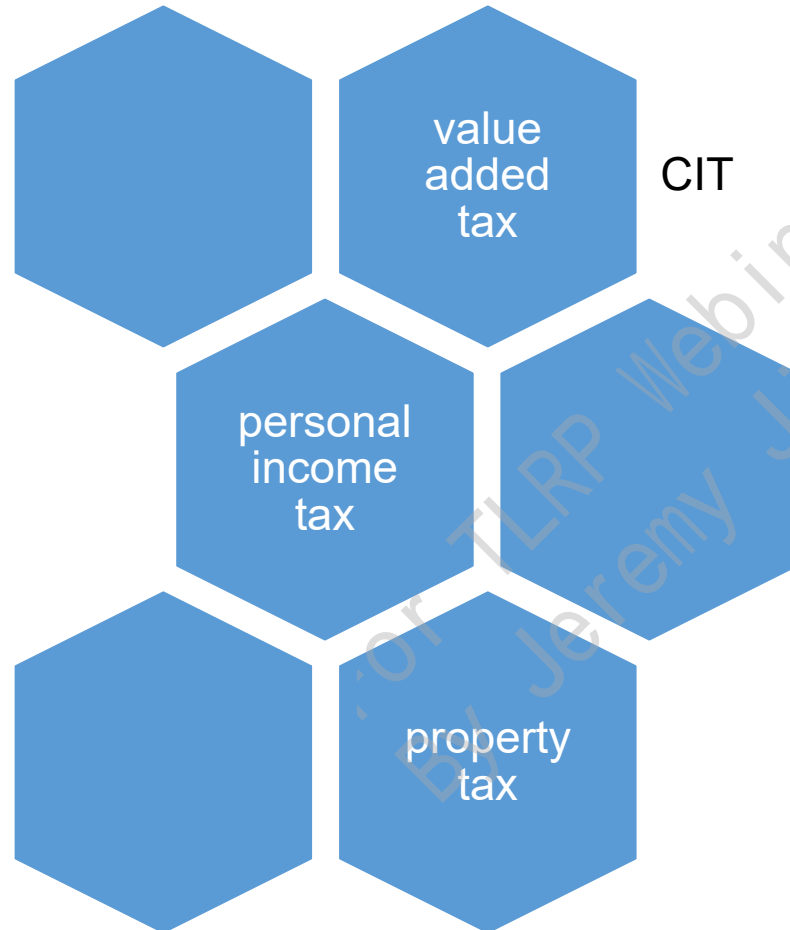


International Shipping Tax Incentives

- Special tax treatment for the shipping sector
tonnage tax regimes / shipping tax incentives
- International shipping income exclusion of Pillar Two
 - Definition of qualified activities
 - Limitation on the amount of qualified ancillary income
 - Strategic or commercial management requirement



Incentives of Non-Covered Taxes



Function of different tax types and the tax structures of different jurisdictions are highly heterogeneous



QRTC and Non-Tax Subsidy

- QRTC and cash grants as ETR Denominator

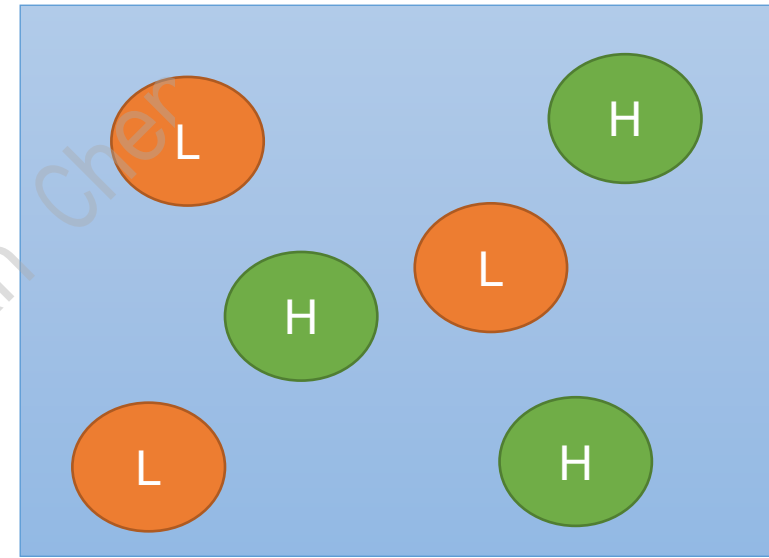
$ETR = \text{covered taxes} / \text{GloBE income}$

- Fiscal and legal challenges
 - Limited fiscal space of developing countries
 - Cost and complexity of tax administration
 - Legal constraints on direct subsidies



Mixing Effect of Jurisdictional Blending Approach

中国地图



Substance-based Income Exclusion

SBIE



5%



5%



Ring-fencing?



Domestic Minimum Tax

The GloBE Model Rules define QDMTT as a minimum tax that is included in the domestic law of a jurisdiction and meet the following three requirements: (a) determines the excess profits of the constituent entities located in the jurisdiction in a manner that is equivalent to the GloBE Rules; (b) operates to increase domestic tax liability with respect to domestic excess profits to the minimum rate for the jurisdiction and constituent entities for a fiscal year; and (c) is implemented and administered in a way that is consistent with the outcomes provided for under the GloBE Rules and the Commentary, provided that such jurisdiction **does not provide any benefits that are related to such rules.**

Provide alternative supportive measures?
Replace traditional CIT with a QDMTT?



Towards a More Equitable and Efficient Tax Competition Landscape?

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Equality

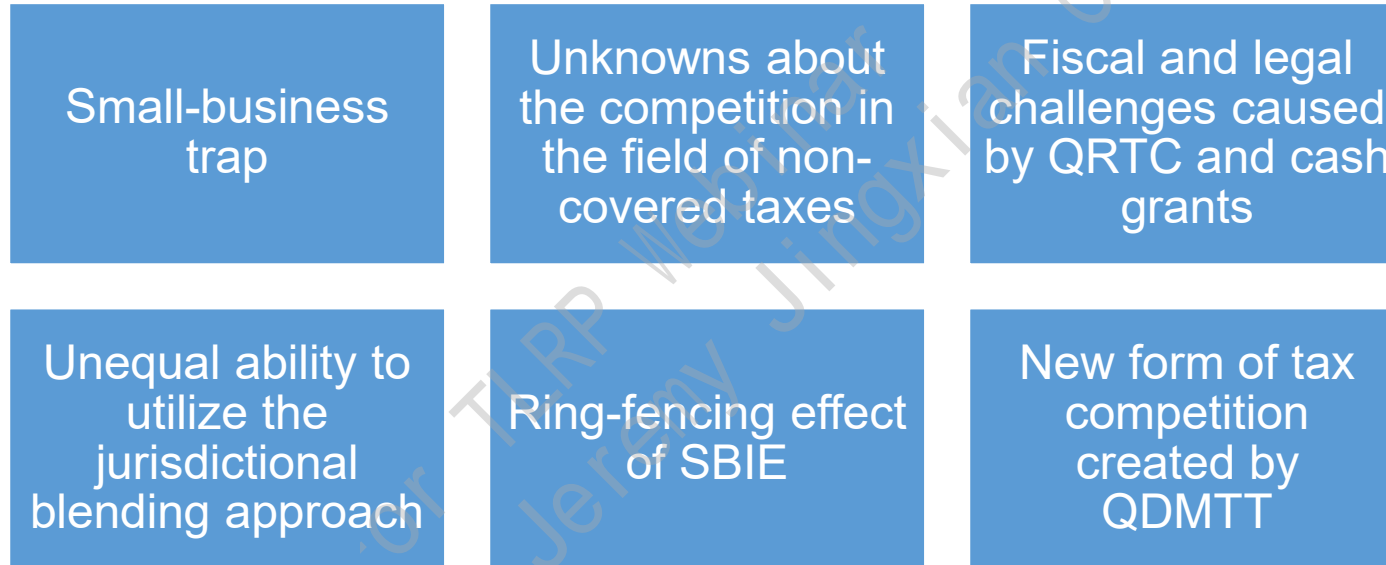
- The (questionable) ‘benefit-to-all’ narrative of Pillar Two
 - Unbalanced revenue effects
 - Limitation on tax policy space
 - STTR as a bonus?
 - Funding or technical assistance to improve the overall investment climates of developing countries?

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Efficiency

➤ The mixed effect of Pillar Two



Some new inefficiencies...

The remedy may ultimately prove to be worse than the illness. (Leopoldo Parada, 2022)



Some Preliminary Observations

- To address tax competition in a more holistic, equitable, and systematic manner
- Equality
 - Global justice principle
 - Meaningful financial or technical supports
 - Issue linkage (taxation, investment and sustainable development)
- Efficiency
 - Reports or guidelines
 - Further multilateral agreement?



Summary

- What are the differences between Pillar Two and OECD's previous efforts to combat CIT competition?
- In what way and to what extent will Pillar Two restrict CIT competition? Will there still be room for tax competition in the future, and if so, in what form? Specifically, what role can game theory play in explaining these issues?
- Will the new tax competition landscape lead to greater equality and efficiency? If not, how can the IF better address these problems in the future?



Questions and Discussions

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Thank you!



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