Visualizing the minimum tax

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Navigating Global Tax Governance

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AFRICAN TAX ADMINISTRATION FORUM
FORUM SUR L'ADMINISTRATION FISCALE AFRICAINE

Global minimum tax: Open issues and questions

- How to visualize different policy choices?
- A lower or a higher minimum tax rate?
- More or less substance-based carve outs?
- Changing the rule order?

It depends, but on what?

- Two policy goals:
  - Combatting profit shifting → influencing behaviour of MNEs
  - Combatting tax competition → influencing behaviour of states
- Should both goals be pursued?
- In what priority?
- Importance of short term vs. long term impact
- What are the administrative costs of either solution?
- What are higher level goals?
  - Assumption here: A capital-importing (developing) country wants to maximize both investment and revenue
  - This assumption may not always be true

Current rule order

Capital-importing country

Headquarter country

Regular domestic tax law of source countries	Computation of tax base
	Application of tax rate

Qualified domestic top-up tax

Income-inclusion rule

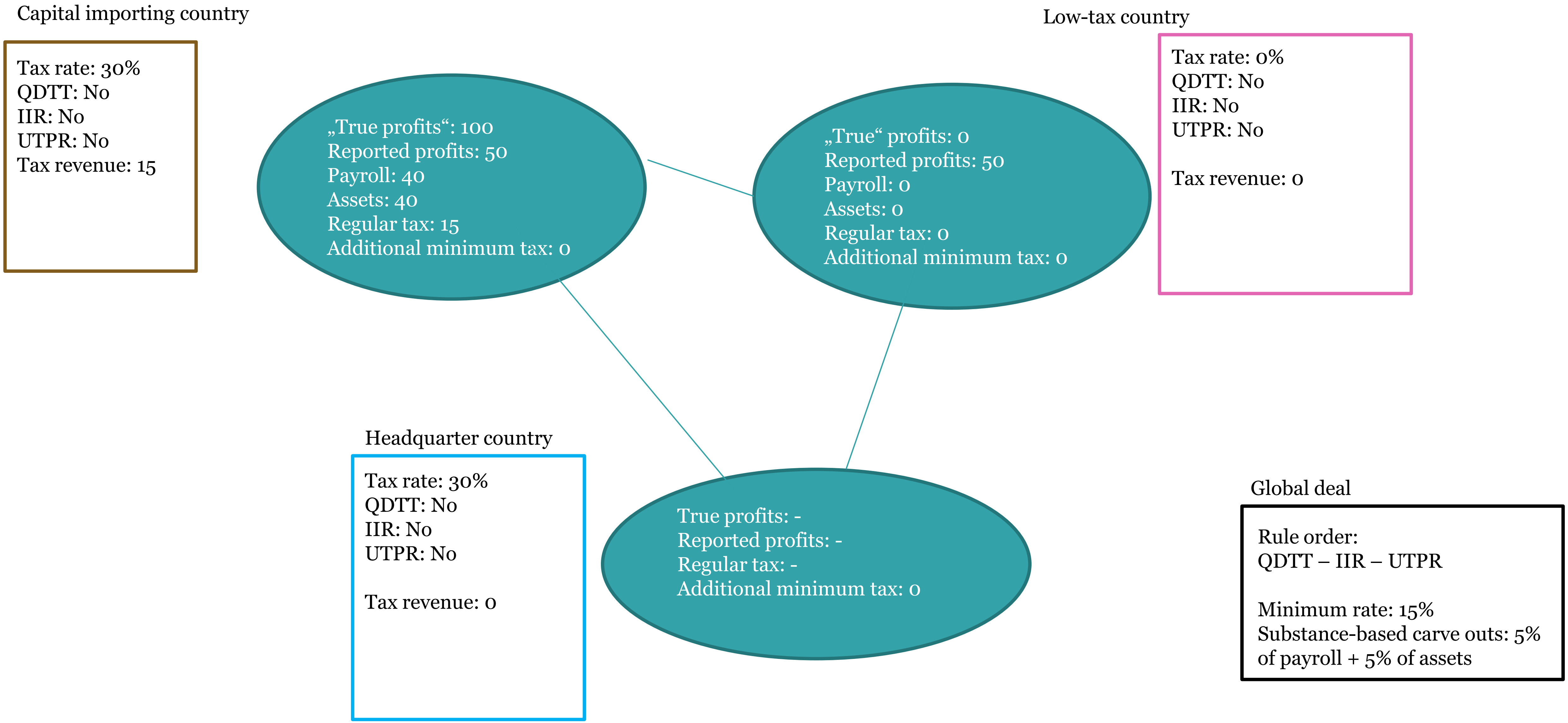
Under-taxed payments rule

Assumptions about the current reality

- Capital importing countries in Africa have statutory tax rates of around 30 to 35%
  - In some sectors (e.g. oil and gas), rates are higher (sometimes 60%)
  - Often rates are lower (often 0%), e.g. tax holidays, special economic zones, sectoral incentives
  - There are a number of jurisdictions without corporate income tax (or very low rates) available in the world
  - Some multinationals shift profits to low tax jurisdictions, especially when not benefitting from low rates

Impact of minimum tax on profit shifting

Situation 1: No minimum tax



Situation 2: Current design, short term

Capital importing country

Tax rate: 30%
QDTT: Yes
IIR: Yes
UTPR: Yes
Tax revenue: 15

„True profits“: 100
Reported profits: 50
Payroll: 40
Assets: 40
Regular tax: 15
Additional minimum tax: 0

Low-tax country

Tax rate: 0%
QDTT: No
IIR: No
UTPR: No

Tax revenue: 0

„True“ profits: 0
Reported profits: 50
Payroll: 0
Assets: 0
Regular tax: 0
Additional minimum tax: 0

Headquarter country

Tax rate: 30%
QDTT: Yes
IIR: Yes
UTPR: Yes

Tax revenue: 7.5

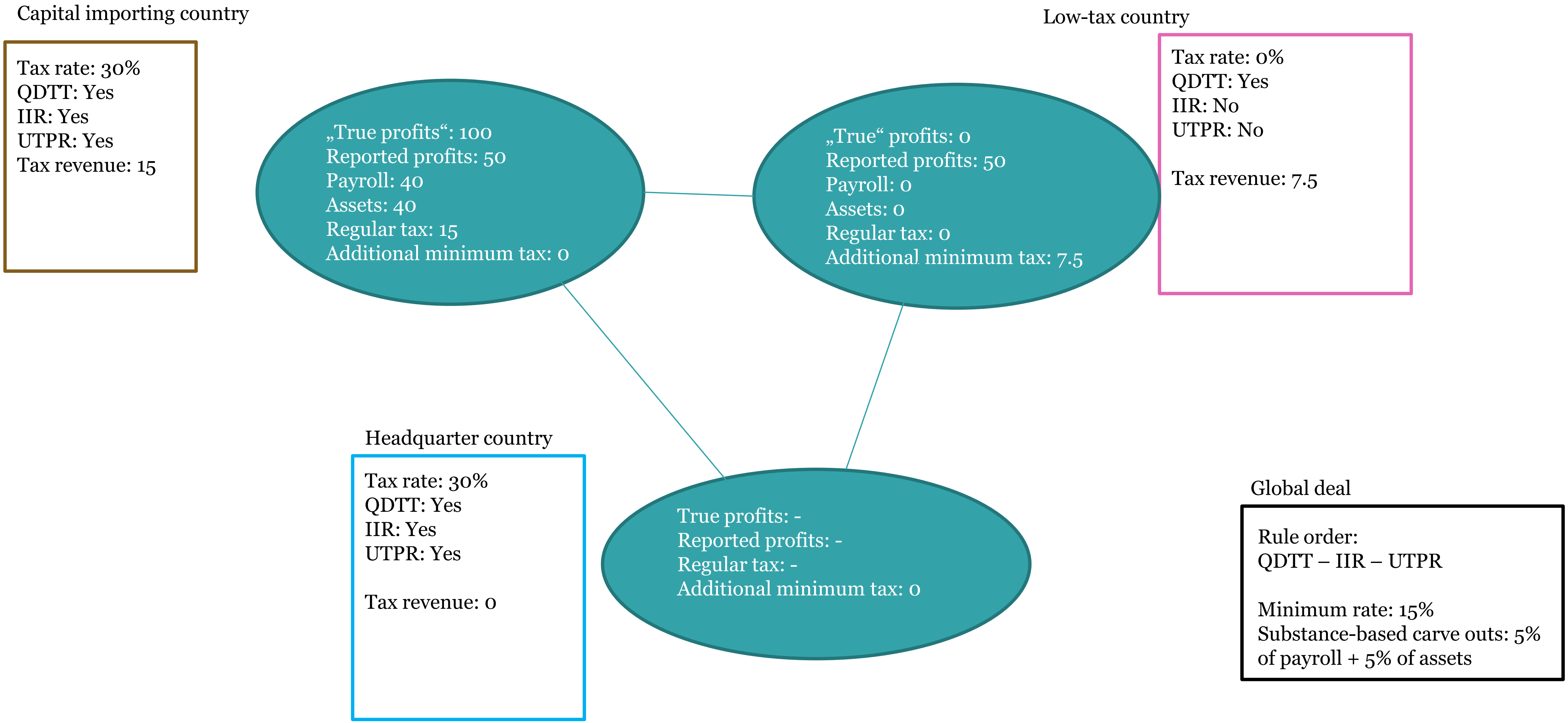
True profits: -
Reported profits: -
Regular tax: -
Additional minimum tax: 7.5

Global deal

Rule order:
QDTT – IIR – UTPR

Minimum rate: 15%
Substance-based carve outs: 5% of payroll + 5% of assets

Situation 3: Current design, participation of low tax country, short term



Situation 4: Current design, long term

Capital importing country

Tax rate: 30%
QDTT: Yes
IIR: Yes
UTPR: Yes
Tax revenue: 21

„True profits“: 100
Reported profits: 70
Payroll: 40
Assets: 40
Regular tax: 15
Additional minimum tax: 0

„True“ profits: 0
Reported profits: 30
Payroll: 0
Assets: 0
Regular tax: 0
Additional minimum tax: 4.5

Low-tax country

Tax rate: 0%
QDTT: Yes
IIR: No
UTPR: No

Tax revenue: 4.5

Headquarter country

Tax rate: 30%
QDTT: Yes
IIR: Yes
UTPR: Yes

Tax revenue: 0

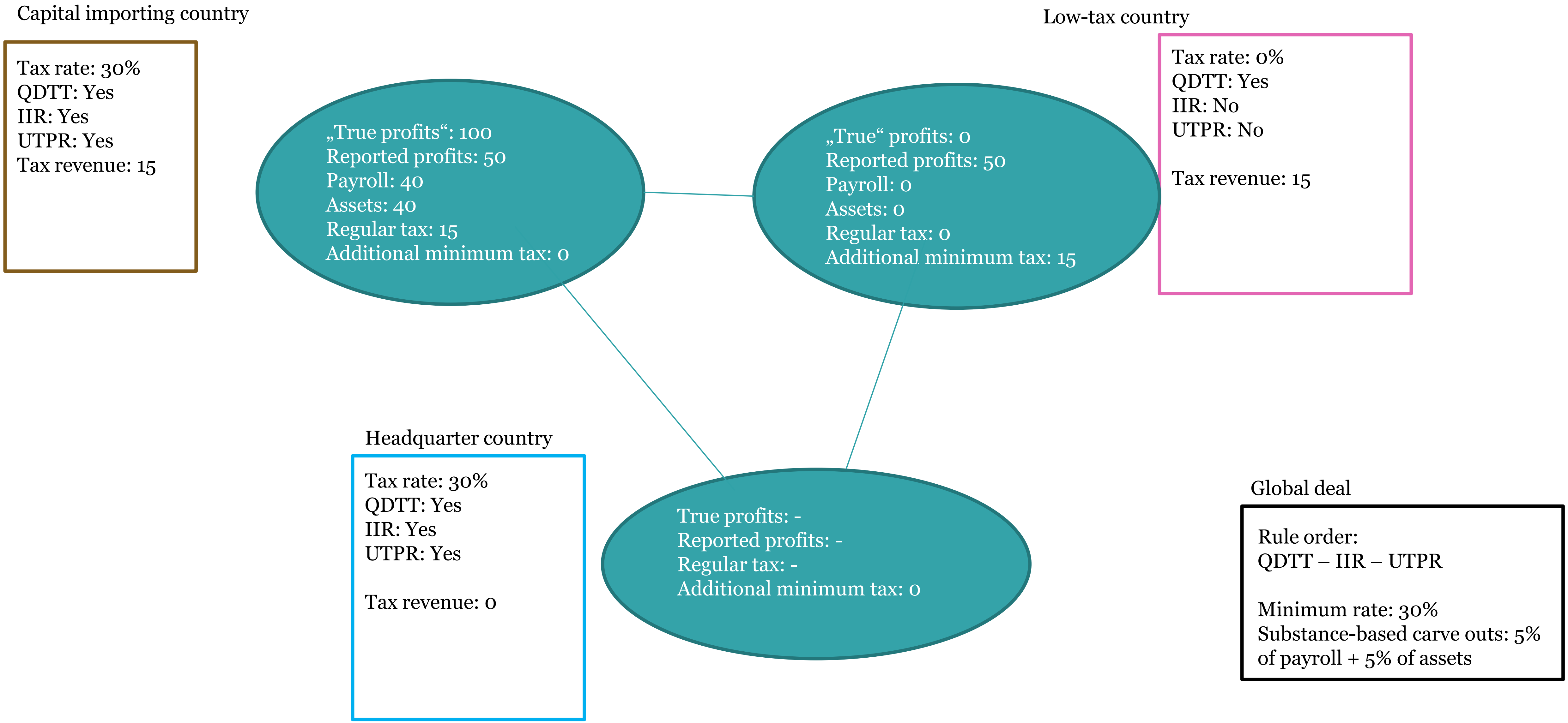
True profits: -
Reported profits: -
Regular tax: -
Additional minimum tax: 0

Global deal

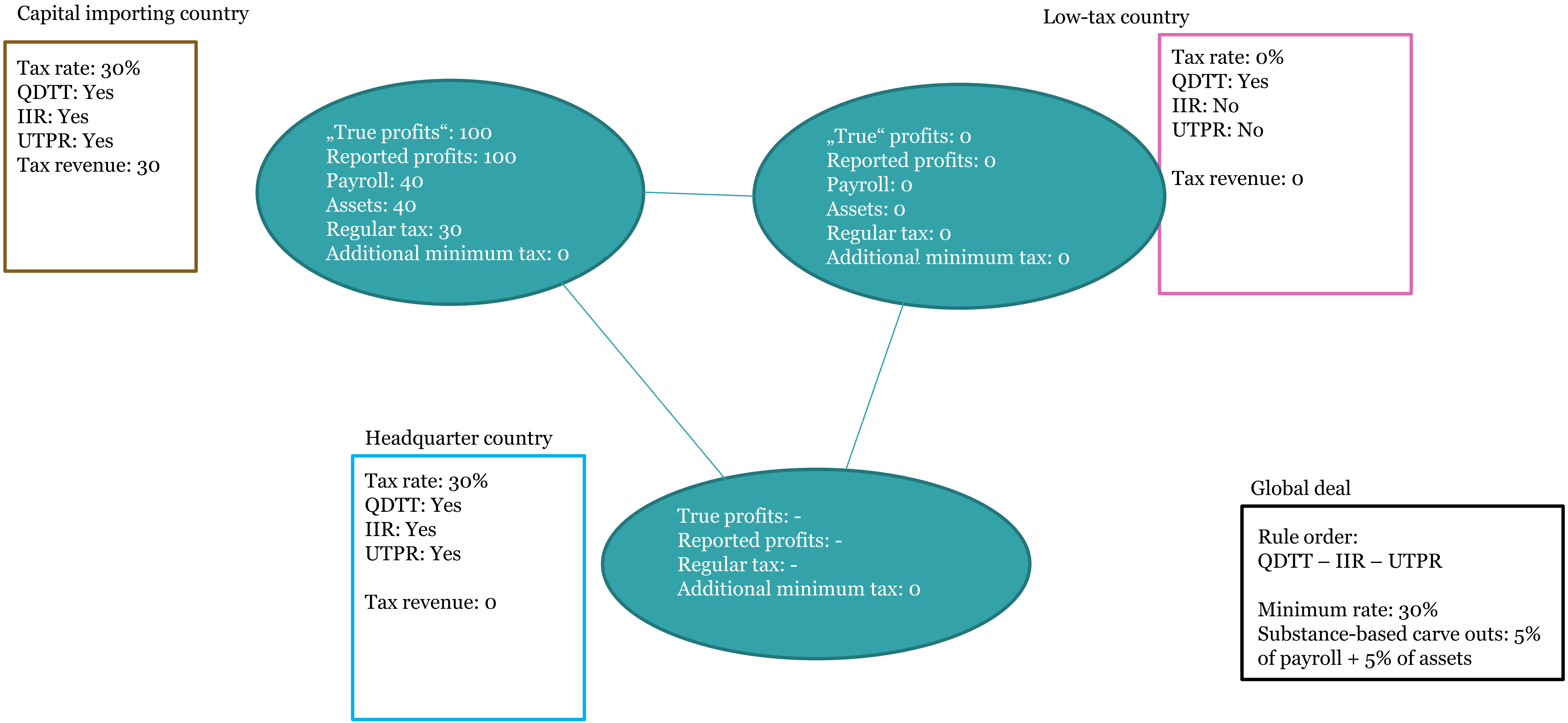
Rule order:
QDTT – IIR – UTPR

Minimum rate: 15%
Substance-based carve outs: 5% of payroll + 5% of assets

Situation 5: Higher rate (30%), short term



Situation 6: Higher rate (30%), long term



Situation 7: Rule order change, short term, no participation by low tax country

Capital importing country

Tax rate: 30%
QDTT: Yes
IIR: Yes
UTPR: Yes
Tax revenue: 22.5

„True profits“: 100
Reported profits: 50
Payroll: 40
Assets: 40
Regular tax: 15
Additional minimum tax: 7.5

„True“ profits: 0
Reported profits: 50
Payroll: 0
Assets: 0
Regular tax: 0
Additional minimum tax: 0

Low-tax country

Tax rate: 0%
QDTT: No
IIR: No
UTPR: No

Tax revenue: 0

Headquarter country

Tax rate: 30%
QDTT: Yes
IIR: Yes
UTPR: Yes

Tax revenue: 0

True profits: -
Reported profits: -
Regular tax: -
Additional minimum tax: 0

Global deal

Rule order:
QDTT - UTPR– IIR

Minimum rate: 15%
Substance-based carve outs: 5% of payroll + 5% of assets

Situation 7: Rule order change, short term, participation by low tax country

Capital importing country

Tax rate: 30%
QDTT: Yes
IIR: Yes
UTPR: Yes
Tax revenue: 15

„True profits“: 100
Reported profits: 50
Payroll: 40
Assets: 40
Regular tax: 15
Additional minimum tax: 0

„True“ profits: 0
Reported profits: 50
Payroll: 0
Assets: 0
Regular tax: 0
Additional minimum tax: 7.5

Low-tax country

Tax rate: 0%
QDTT: Yes
IIR: No
UTPR: No

Tax revenue: 7.5

Headquarter country

Tax rate: 30%
QDTT: Yes
IIR: Yes
UTPR: Yes

Tax revenue: 0

True profits: -
Reported profits: -
Regular tax: -
Additional minimum tax: 0

Global deal

Rule order:
QDTT - UTPR– IIR

Minimum rate: 15%
Substance-based carve outs: 5% of payroll + 5% of assets

Impact of minimum tax on profit shifting

- Under current design, short term revenue gains go either to headquarter or low tax jurisdiction, depending on whether low tax jurisdiction implements qualified domestic top-up tax
- In the long term, some revenue gains may go to source jurisdictions, since gains from profit shifting for MNEs are reduced (but not zero because of difference between 15% and statutory rates)
- If minimum rate is higher, in the long term, more revenue gains for source jurisdictions, in the short term no effect
- If UTPR comes before IIR, also short term gains for source jurisdictions, but only if low tax jurisdictions do not implement QDTT

Impact on tax competition

Situation 1: No minimum tax

Capital importing country 1

Tax rate: 20%
QDTT: No
IIR: No
UTPR: No
Tax revenue: 10

„True profits“: 50
Reported profits: 50
Payroll: 40
Assets: 40
Regular tax: 10
Additional minimum tax: 0

„True“ profits: 50
Reported profits: 50
Payroll: 40
Assets: 40
Regular tax: 10
Additional minimum tax: 0

Capital importing country 2

Tax rate: 20%
QDTT: No
IIR: No
UTPR: No

Tax revenue: 10

Headquarter country

Tax rate: 30%
QDTT: No
IIR: No
UTPR: No

Tax revenue: 0

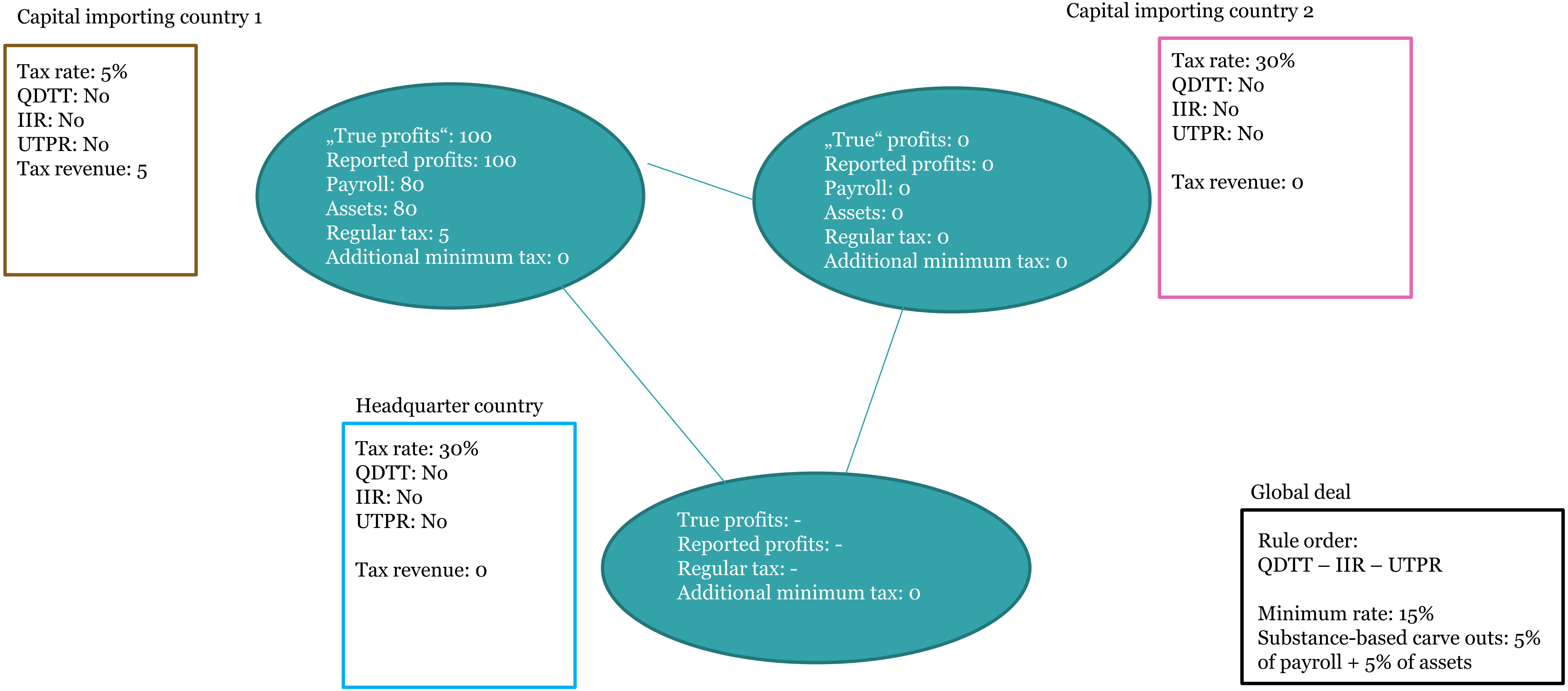
True profits: -
Reported profits: -
Regular tax: -
Additional minimum tax: 0

Global deal

Rule order:
QDTT – IIR – UTPR

Minimum rate: 15%
Substance-based carve outs: 5% of payroll + 5% of assets

Situation 2: No minimum tax, race-to-the-bottom, part 1



Situation 3: No minimum tax, race-to-the-bottom, part 2

Capital importing country 1

Tax rate: 5%
QDTT: No
IIR: No
UTPR: No
Tax revenue: 2.5

„True profits": 50
Reported profits: 50
Payroll: 40
Assets: 40
Regular tax: 2.5
Additional minimum tax: 0

„True" profits: 50
Reported profits: 50
Payroll: 40
Assets: 40
Regular tax: 2.5
Additional minimum tax: 0

Capital importing country 2

Tax rate: 5%
QDTT: No
IIR: No
UTPR: No

Tax revenue: 2.5

Headquarter country

Tax rate: 30%
QDTT: No
IIR: No
UTPR: No

Tax revenue: 0

True profits: -
Reported profits: -
Regular tax: -
Additional minimum tax: 0

Global deal

Rule order:
QDTT – IIR – UTPR

Minimum rate: 15%
Substance-based carve outs: 5% of payroll + 5% of assets

Situation 4: Minimum tax, current design, only applied by headquarter

Capital importing country 1

Tax rate: 5%
QDTT: No
IIR: No
UTPR: No
Tax revenue: 2.5

„True profits“: 50
Reported profits: 50
Payroll: 40
Assets: 40
Regular tax: 2.5
Additional minimum tax: 0

Capital importing country 2

Tax rate: 5%
QDTT: No
IIR: No
UTPR: No

Tax revenue: 2.5

„True“ profits: 50
Reported profits: 50
Payroll: 40
Assets: 40
Regular tax: 2.5
Additional minimum tax: 0

Headquarter country

Tax rate: 30%
QDTT: Yes
IIR: Yes
UTPR: Yes

Tax revenue: 2

True profits: -
Reported profits: -
Regular tax: -
Additional minimum tax: 10 – 8
(substance based carve out) = 2

Global deal

Rule order:
QDTT – IIR – UTPR

Minimum rate: 15%
Substance-based carve outs: 5% of payroll + 5% of assets

Situation 5: Minimum tax, current design, applied by all

Capital importing country 1

Tax rate: 5%
QDTT: Yes
IIR: Yes
UTPR: Yes
Tax revenue: 3.5

„True profits“: 50
Reported profits: 50
Payroll: 40
Assets: 40
Regular tax: 2.5
Additional minimum tax: 1

Capital importing country 2

Tax rate: 5%
QDTT: Yes
IIR: Yes
UTPR: Yes

Tax revenue: 3.5

„True“ profits: 50
Reported profits: 50
Payroll: 40
Assets: 40
Regular tax: 2.5
Additional minimum tax: 1

Headquarter country

Tax rate: 30%
QDTT: Yes
IIR: Yes
UTPR: Yes

Tax revenue: 0

True profits: -
Reported profits: -
Regular tax: -
Additional minimum tax: 0

Global deal

Rule order:
QDTT – IIR – UTPR

Minimum rate: 15%
Substance-based carve outs: 5% of payroll + 5% of assets

Situation 6: Minimum tax, applied by all, higher rate

Capital importing country 1

Tax rate: 5%
QDTT: Yes
IIR: Yes
UTPR: Yes
Tax revenue: 5

„True profits“: 50
Reported profits: 50
Payroll: 40
Assets: 40
Regular tax: 2.5
Additional minimum tax: 2.5

Capital importing country 2

Tax rate: 5%
QDTT: Yes
IIR: Yes
UTPR: Yes

Tax revenue: 5

„True“ profits: 50
Reported profits: 50
Payroll: 40
Assets: 40
Regular tax: 2.5
Additional minimum tax: 2.5

Headquarter country

Tax rate: 30%
QDTT: Yes
IIR: Yes
UTPR: Yes

Tax revenue: 0

True profits: -
Reported profits: -
Regular tax: -
Additional minimum tax: 0

Global deal

Rule order:
QDTT – IIR – UTPR

Minimum rate: 20%
Substance-based carve outs: 5% of payroll + 5% of assets

Situation 7: Minimum tax, applied by all, no substance carve outs

Capital importing country 1

Tax rate: 5%
QDTT: Yes
IIR: Yes
UTPR: Yes
Tax revenue: 7.5

„True profits“: 50
Reported profits: 50
Payroll: 40
Assets: 40
Regular tax: 2.5
Additional minimum tax: 5

Capital importing country 2

Tax rate: 5%
QDTT: Yes
IIR: Yes
UTPR: Yes

Tax revenue: 7.5

„True“ profits: 50
Reported profits: 50
Payroll: 40
Assets: 40
Regular tax: 2.5
Additional minimum tax: 5

Headquarter country

Tax rate: 30%
QDTT: Yes
IIR: Yes
UTPR: Yes

Tax revenue: 0

True profits: -
Reported profits: -
Regular tax: -
Additional minimum tax: 0

Global deal

Rule order:
QDTT – IIR – UTPR

Minimum rate: 15%
Substance-based carve outs: 0% of payroll + 0% of assets

Situation 8: Minimum tax, no substance carve outs, potential investment effects

Capital importing country 1

Tax rate: 5%
QDTT: Yes
IIR: Yes
UTPR: Yes
Tax revenue: 6

„True profits“: 40
Reported profits: 40
Payroll: 35
Assets: 35
Regular tax: 2
Additional minimum tax: 4

„True“ profits: 40
Reported profits: 40
Payroll: 35
Assets: 35
Regular tax: 2
Additional minimum tax: 4

Capital importing country 2

Tax rate: 5%
QDTT: Yes
IIR: Yes
UTPR: Yes

Tax revenue: 6

Headquarter country

Tax rate: 30%
QDTT: Yes
IIR: Yes
UTPR: Yes

Tax revenue: 0

True profits: 20
Reported profits: 20
Payroll: 10
Assets: 10
Regular tax: 6
Additional minimum tax: 0

Global deal

Rule order:
QDTT – IIR – UTPR

Minimum rate: 15%
Substance-based carve outs: 0% of payroll + 0% of assets

What should one do?

- Question of priorities
- Should tax systems still be used for attracting „real investment“?
  - If no: no carveouts, high rate, QDMTT important
  - If yes, carve outs important, concentration on combatting profit shifting, UTPR before QDMTT
  - Complication: Combatting profit shifting also raises the effective tax rate on „true“ profits payable in a source country and might lead to less investment
- Collect more empirical data
  - Tax sensitivities of investment

A differentiated minimum tax?

- Margalioth: “Transfers from rich to poor countries further benefit by imposing limitations on rich countries' abilities to engage in tax competition with poor countries. […] For example, Ireland would be required to raise its current corporate tax rate of 12.5% in order to decrease the relative disadvantage that developing countries have when competing with Ireland for FDI. […] With the application of anti-tax competition rules to developing countries, we establish two different harmonized tax levels - one for developed countries and the other for developing countries.” (p. 194 – 195)

Thank you!

Questions?
Comments?

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