Next Steps in the OECD/Inclusive Framework's Digitalization Project

Now Is the Time for Business to Engage in the Global Tax Policy Process

US – October 16, 2020

The OECD's Inclusive Framework on BEPS announced on October 12, 2020, that it will pursue its work plan on the tax challenges of digitalization until at least the middle of 2021 and probably beyond.

The work plan, which was reconfirmed by the G20 finance ministers on October 14, 2020, has two distinct parts or "pillars." Pillar One calls for the creation of a new taxing right involving reallocation of part of a multinational's profits to market countries, and expanded taxing powers for those countries at the expense of countries where production occurs. Pillar Two is a global minimum tax proposal for large multinationals.

Two "blueprints" of the pillars were published on October 12, 2020, each more than 200 pages in length. The 137 members of the Inclusive Framework have not yet agreed on all elements of the plans – hence the need to continue discussing them in 2021.

The stakes for multinational businesses are high. In particular, Pillar Two would create an elaborate new system of tax rules applicable to all multinationals with annual global sales revenue in excess of a stated threshold (€750 million in the current draft blueprint). These rules would aim to ensure that a certain minimum effective tax rate was paid on all of the group's global income. The minimum effective rate has not yet been agreed upon, but many believe that it will be at least 12.5%.

Even if this new regime did not result in a significant increase in tax payable by a given multinational group, the cost of simply determining how the Pillar Two rules apply to the group's operations and entities everywhere that it does business would be substantial, and painful. Pillar One would add another complex set of rules for groups within the scope of its allocation rules, plus additional new rules for the taxation of marketing and distribution activities in all industries. The business community has every reason to be concerned about the outcome of this process, and to do whatever is possible to try to influence the outcome.

An additional risk factor for businesses operating in Europe is the possibility of new tax measures to be initiated by the European Commission. EU officials have repeatedly stated that if agreement is not reached by the Inclusive Framework, the EU will move on its own to propose within the first half of 2021 rules similar to the Pillar One and Pillar Two proposals for all EU member states. In addition, France has announced its intention to reinstate its digital services tax by year-end 2020, a move that could deepen existing transatlantic trade tensions.

A further tax risk for multinational business lies in Africa. Recently, the African Tax Administration Forum published its "Suggested Approach to Drafting Digital Services Tax Legislation," encouraging African countries to consider proceeding unilaterally with such taxes, regardless of the multilateral Inclusive Framework process. Kenya has already passed one and other African countries may follow its lead.

The next step in the Inclusive Framework's process is a public consultation on the blueprints. A consultation document was issued along with the draft blueprints, requesting written comments on a number of issues that remain to be discussed by the Inclusive Framework's members. Comments may also address other aspects of the proposals.

The comment period will last from mid-October to December 14, 2020, and a public consultation meeting will take place in January 2021. Companies and business groups would be well advised to take advantage of the opportunity to submit written comments and speak at the meeting.

We have deep expertise in international tax policy work and have been assisting a number of global multinationals to engage with governments in relation to the Inclusive Framework's process. We would be pleased to assist in identifying the issues posed by these proposals that are of most importance to your business, and in developing and delivering your comments by the mid-December deadline.

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