BEPS 2.0: Making the world safe for Americans

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The BEPS edifice

Buttressing a tax we are told we should be desperate to scrap

> *… Treasury research estimates that each additional $1 collected by way of company income tax reduces the living standards of Australian households by around 50 cents in the long run because of reduced investment. This impedes Australia's productivity and, in turn, reduces opportunities for better paying jobs.*
>
> *… in the long run, over half of the economic burden of corporate tax is likely to be shifted away from shareholders through lower wages for employees and higher prices for consumers.*
>
> *… Corporate tax [reduces] the return from their investments [which] reduces the level of investment in small, open, capital importing economies, such as Australia… Higher taxes on investment generally mean that fewer investments will be viable… Reducing Australia's corporate tax rate would increase Australia's appeal as a place to do business.*
>
> ReThink (2015)

Should we be worried?

Maybe Treasury doesn't need to worry / ATO shouldn't get hopes up

- Australian corporate tax won't increase under either Pillar
  - might lose some money under Pillar 1
- *compare* $3bn estimate for both Pillars in *Australian Financial Review* (July 2021)!

US probably break-even in revenue terms

- US modelling says Pillar 1 is revenue neutral for it
  - 55% of the $150bn revenue goes back to the US
  - BIG benefit of no DSTs / DPTs not quantified
- GILTI already exists; no US revenue lost from Pillar 2

But US got what they wanted

- for digital world: few affected companies, little revenue on the table, ALP lives on, one tax claim, which has to be enacted in the US, administered by IRS
- GILTI now imposed on their competitors via Pillar 2

The promise of Pillar 1 (Amount A)

Did something truly remarkable just happen?

- challenging the PE threshold
- challenging the separate entity fiction
- challenging the *TP Guidelines*

Not really, but maybe next time

- Amount A gets narrowed
  - turnover threshold ↑; number of affected groups ↓
  - 10% profitability requirement + the segmentation debate + now ‘averaging’
  - adjustments to book profitability
  - treatment of pre-regime losses
  - exclusion of deemed routine profits
  - US safe harbour proposal becomes, ALP as a cap
- Amount B gets put on hold
- Amount C disappears

Marketing and distribution profits safe harbour

Where the residual profits of an in-scope MNE are already taxed in a market jurisdiction, a marketing and distribution profits safe harbour will cap the residual profits allocated to the market jurisdiction through Amount A. Further work on the design of the safe harbour will be undertaken, including to take into account the comprehensive scope.

Will Pillar 1 cost Australia money?

Australian firms operating offshore

- no existing revenue lost to other countries because of (i) $30bn threshold + (ii) carve out for mining, financial sector [ie, no item E]
- possibility of future domestic revenue lost if DPT repealed, but maybe nothing here to lose

Foreign firms operating in Australia

- Maybe some revenue gained
  - except, ALP as marketing + distribution safe harbour excludes Apple, Microsoft, Amazon, others?
  - (remainder of) $125bn* x (26m / 7.9bn) = $411m
  - or maybe $125bn* x (1.3tr / $84.5tr) = $1.9bn

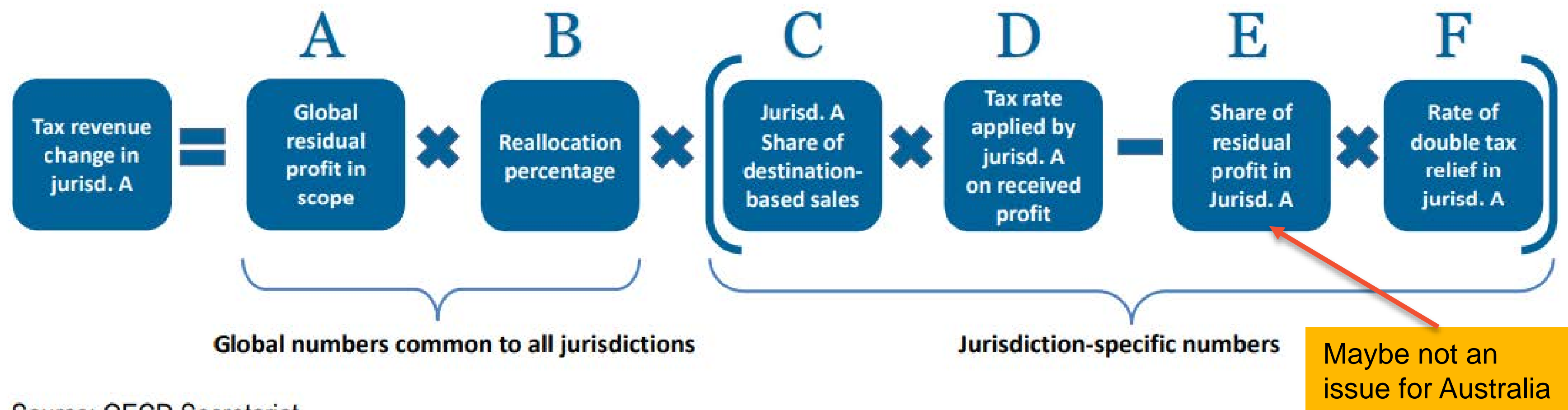
    * $100bn October 2020 → $125bn in Oct 2021???
- Maybe some revenue lost
  - MAAL (except, turns out there is no revenue here: ≈$100m tax from turnover of $8bn!)
  - DPT – no-one knows since DPT is the product of exasperation, not a serious tax rule

Other revenue loss

- FITO for tax paid by group offshore, but allocated to Australian sub

- **Step 3:** Allocate, in order of priority, the Amount A tax liability to the entities that have a connection with the market(s) where Amount A is allocated.
- **Step 4:** Allocate, on a pro-rata basis, where no sufficiently strong connection(s) is (or are) found or where those with a market connection lack the necessary amount of profit.

OECD, *Economic Impact Assessment* (October 2020)



What is missing?

- [C x D] should be capped at ALP if local presence
- [G x F] need another loss for FITO on profits never in A
- loss of MAAL / DPT

‘Two paths diverged in a yellow wood …’

Did we choose the right path?

> *A consensus-based multilateral solution involving Pillar One and Pillar Two would lead to a more favourable environment for investment and economic growth than would likely be the case in the absence of an agreement by the Inclusive Framework.*
>
> OECD, *Economic Impact Assessment* (October 2020)

- Conclusion is simply – co-ordination *beats* uncoordination
- Says nothing about co-ordination ***around what***
- Having seen Pillar 1, real question is whether OECD should have pursued coordination around
  - uniform model DST
  - UN proposed art 12B
  - uniform model DPT

Pillar 2 – taking GILTI to the world

15% tax on foreign super-profits? Not really

- industry carve out (shipping)
- entity carve-outs (super, non-profits, CIVs, SWF, etc)
- using accounting consolidation to define CFC
  - Enron / TAHE / etc
- de minimis exemption
- 'Substance Carve Out' (ie, sheltering passive behind income presumed to be non-passive)
- national blending
- profit / loss carry forward rules
- tax carry forward rules
- STTR only gets you to 9%

Pillar 2 – taking GILTI to the world

Is GloBE less ambitious than our current CFC rules?

- Part X has no industry / class of taxpayer carve outs
- 5% active income test *versus* de minimis threshold
- active v. passive income demarcation:
  - (10% x payroll + 8% x WDV) *versus*
  - income ≠ 'adjusted tainted income'
- s. 400 *versus* national blending
- no profit / loss carry forward or averaging
- no tax carry forward / averaging

Will Pillar 2 make any money for Australia?

Australian-owned firms operating offshore

- not obvious that GloBE tax base > CFC ‘attributable income’

Foreign-owned firms operating in / through Australia

- Australia isn’t going to change our tax base on local subsidiary of MNE to prevent GloBE being enlivened
- **IIR:** UPE beats IPE every time – cf. s. 456A
  - ie, US / UK / etc always wins since will be UPE (ie, foreigners don’t own other foreign things *through* Australia)
- **UTPR:** probably never gets enlivened because IIR trumps UTPR
  - ie, US / UK / etc always wins once IIR in place
- **STTR:** will STTR turn out to be effective?
  - only gets levied at maximum of 9%
  - only on interest + royalties (currently)
  - and amounts must be paid to related party
  - aren’t many situations where interest/royalty paid to associated entity can leave Aust without IWT / RWT

> *In general, no top-up tax would be imposed in circumstances in which the relevant treaty already provided for source taxation on the covered payment …*