
STEP JOURNAL

# From Pillars to post

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**Can jurisdictions reach a tax agreement that works internationally? Helen Swire looks at the progress the OECD has made in this arena and asks what happens next**

With an ever-increasing move towards global solutions in transparency and cross-border cooperation in reporting standards, it seems a foregone conclusion that jurisdictions around the world will take steps to achieve an equitable international taxation system.

Such a system has been the focus of the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (the Framework), which has been working on the implementation of global corporate tax fairness for some years. In 2021, the Framework announced that it, with the cooperation of 134 jurisdictions, had reached a two-pillar solution to address the ‘tax challenges arising from the digitalisation of the economy’: Pillar One dealing with revised profit allocation and nexus rules and Pillar Two relating to global minimum tax rules.

Pillar One aims to ensure a fairer distribution of taxing rights among countries with respect to the largest and most profitable multinational enterprises. ‘If Pillar One is not implemented effectively, this is likely to lead to a proliferation of uncoordinated unilateral tax measures, including unilateral digital services taxes,’ explains Grace Perez-Navarro, Director of the OECD Centre for Tax Policy and Administration. ‘This could lead to an escalation in damaging trade disputes, which could reduce global GDP by more than 1 per cent annually. Failure to implement Pillar One would also lead to much greater complexity and cost for businesses and would reduce tax certainty.’

The 15 per cent global minimum corporation tax under Pillar Two will put multilaterally agreed limitations on tax competition, halting the so-called ‘race to the bottom’ that has seen countries compete to lower statutory corporate tax rates. This approach aims to protect countries’ corporate tax revenues and will allow countries to collect around USD150 billion in new revenues annually.

‘Updating international tax policies is especially important today considering the nature of modern business practices and sometimes entire industries’, says Craig Redler TEP,[1] Branch Chair of STEP Orange County. ‘Most existing tax laws were written to largely rely on a taxable entity’s physical presence in a country and a lot of business today is conducted with no such presence. Most of the world’s largest corporations, at least to some extent, are digitally managed and can easily operate in a jurisdiction without a physical presence there. The existing framework is ill-equipped to address more recent business models arising from digitalisation and globalisation.’

## Roadblocks and renegotiations

While for many this seems a logical next piece in the puzzle of global taxation, the progression of the OECD proposals has not been altogether smooth sailing. Since the conception of the idea, jurisdictions have negotiated strenuously on the finer details and timelines of implementation of both Pillars. Countries including Estonia, France, Ireland, Malta, Poland, Sweden and the US have all raised concerns and it was only in December 2022 that Hungary agreed to lift its veto on the EU directive to implement the Pillar Two global minimum tax.

‘The biggest roadblocks are still at the level of geopolitical ones rather than technical implementation ones,’ comments Mark Summers TEP,[2] Deputy Chair of the STEP Public Policy Committee. ‘The potential for a transatlantic “turf war” for slices of tax on corporate profits remains, even if profit shifting into low- or no-tax jurisdictions is now, by and large, at an end. However, the main challenge identified by the OECD for Pillar One was the digitalised economy and over the past two years most of the technical work to address that challenge has been undertaken.’

‘The OECD knows that there are sometimes serious divergences between how the rules are designed and how they operate in practice,’ adds Redler. ‘The challenge is always going to be the equitable application of any new rules at the same time as ensuring compliance. It is difficult to come up with appropriate ways to coordinate the application of international tax rules with a jurisdiction’s local rules: the balance of accuracy and simplicity.’

## Forward momentum

Despite the challenges faced, however, the OECD remains positive about the forward direction of the proposals. Various specialist technical committees are striving to iron out the complexities associated with the two Pillars and the OECD is continuing to consult on the practical details with stakeholders including professional organisations, businesses and parliamentary bodies.

In July 2022, the OECD revised implementation timelines for the Pillars, saying: ‘These are complex and very technical negotiations in relation to some new concepts that fundamentally reform international tax arrangements. We will keep working as quickly as possible to get this work finalised, but we will also take as much time as necessary to get the rules right. These rules will shape our international tax arrangements for decades to come.’[3]

‘The Inclusive Framework has been able to make strong progress towards implementing the two-pillar solution,’ says Perez-Navarro. ‘Thanks to these consultations, including most recently, a consultation on “Amount A”, the administration and tax certainty aspects of the profits to be reallocated across jurisdictions under Pillar One, we have made significant progress in the technical design of various different elements.'

On this basis, she says, the terms of the multilateral convention for Pillar One's Amount A are now being developed, with the aim of the signing ceremony of the multilateral convention taking place by mid-2023. As a result, it is expected that Pillar One as a whole will come into force from January 2024.

Technical work for Pillar Two, meanwhile, is largely complete. The implementation framework, which facilitates coordination between tax administrations and taxpayers and institutes a peer-review process to assist countries to apply the rules consistently, is also working towards a 2024 implementation date.

Perez-Navarro is positive about this progress: 'Countries are now moving ahead to incorporate the global anti-base erosion rules to implement the global minimum tax into their domestic frameworks. Many countries have already started this process and our sense is that momentum is now building.'

## The start of the journey

Although there is still much crucial development to be done on the two-pillar solution, from the technical consultation to the wider engagement piece, the speed of change in the world of finance means that the work is far from over.

Part of the OECD's ongoing work is examining the international tax system's ability to deal with new forms of financial technology, including digital assets. There is a risk that such assets can be used for tax evasion, undermining the current tax transparency framework and so, in October 2022, the OECD released a new Crypto-Asset Reporting Framework (CARF). The CARF provides for the automatic exchange of information about crypto-asset transactions and applies to entities or individuals providing exchange services in crypto-assets.

Perez-Navarro notes that professional bodies such as STEP play a vital role in ongoing consultations and stakeholder conversations about how the industry can make the international taxation system transparent, effective and equitable.

It is important, too, that practitioners keep their clients informed about the ongoing developments and implementation timelines. Summers points out that although the two Pillars may currently focus particularly on the world's largest companies, having an international standard of taxation across jurisdictions will by no means apply restrictively to those companies in the long term.

'What will start at the level of the largest, largely tech, companies will establish a new international framework for corporate taxation that may well be with us for the next 100 years,' he cautions. 'The framework is bound to transform and adapt over time and come to affect smaller active and passive enterprises. Families and their businesses are more global too than they have ever been: these measures are going to touch on many practitioners in the long term.'

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[1] Craig Redler TEP is Partner at Redler Law.
[2] Mark Summers TEP is Partner at Charles Russell Speechlys.
[3] bit.ly/3iN8wED

https://www.step.org/step-journal/step-journal-issue-1-2023/pillars-post


## Helen Swire

Helen Swire is News Editor at STEP.