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Global Tax Alert

G7 Finance Ministers support OECD two-pillar project to develop new rules for taxing multinational businesses

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Executive summary

On 18 July 2019, at the conclusion of the two-day meeting in Chantilly of the G7[1] Finance Minister and Central Bank Governors group, France issued a Chair's Summary[2] of the discussion at the meeting.

The Chair's Summary includes a section on international taxation, which focuses on the Organisation for Economic Co-operation and Development (OECD)/G20 Inclusive Framework project to address the tax challenges of the digitalization of the economy through revisions to existing profit allocation and nexus rules (Pillar 1) and development of new global minimum tax rules (Pillar 2). The Chair's Summary indicates that the G7 Finance Ministers agreed that addressing these challenges is urgent and supported a two-pillar solution to be developed through the OECD workplan. The Chair's Summary reflects G7 agreement to move forward with both pillars. It also reflects G7 discussions aimed at bridging the gap between alternative proposals for new profit allocation and nexus rules that have been advanced by the United States (US) on the one hand, and the United Kingdom (UK), France and other European countries on the other hand, in order to focus the work on one proposed approach.

The Chair's Summary notes that the new rules to developed should be administrable and simple and that mandatory arbitration must be a component of this global solution.

Building a better working world

Detailed discussion

The Chantilly meeting is the latest in a series of multilateral meetings at which the OECD/G20 Inclusive Framework project on developing new international tax rules has been discussed, and the Chair's Summary notes that the G7 group "fully supported a two-pillar solution to be adopted by 2020 through the work programme endorsed by the G20 Leaders."

With respect to the Pillar 1 work on revising profit allocation and nexus rules, the Chair's Summary reflects the G7 group's discussion aimed at bridging the gap between the US "marketing intangibles" proposal and the "user participation" proposal favored by many European nations, including, in particular, the UK and France. This potential unification of these alternative proposals is reflected in the G7 group's agreement that the OECD should work on an approach under which the new taxing rights under Pillar 1 would be determined "by reference to criteria reflecting the level of businesses' active participation in a customers' or users' jurisdiction, such as valuable intangibles or employment of a highly digitalized model." The concept of highly digitalized business models is referenced twice in the Chair's Summary, underscoring the importance of this aspect of the project to some European countries.

The Chair's Summary also states that the new rules for profit allocation and nexus should be administrable and simple, further noting that the G7 group agreed that, "in order to avoid double taxation and ensure the stability of the international tax system, robust and effective tax dispute resolution through mandatory arbitration must be a component of this global solution."

With respect to the Pillar 2 work on new global minimum tax rules, the Chair's Summary states that the G7 group agreed that a minimum level of effective taxation – "such as for example the U.S. GILTI[3] regime" – would contribute to ensuring that companies pay their fair share of tax. The Chair's Summary further notes that "the tax level to be set would depend on concrete design features of the rules."

Implications

The agreement of the G7 group that the focus of revised profit allocation and nexus rules to be developed under Pillar 1 should include both highly digitalized business models and other business models involving valuable intangibles is an important step in advancing the work on the OECD/G20 Inclusive Framework project. While this conceptual consensus at the G7 level is a significant development, the proposals also require consensus among the (currently) 131-member jurisdictions of the Inclusive Framework. Reaching the high-level consensus that the OECD workplan contemplates achieving by January 2020 will require substantial work over the coming six months.

The complex issues underlying the Pillar 1 and Pillar 2 proposals will continue to be the subject of both policy and technical discussions among the Inclusive Framework jurisdictions through at least 2020 in trying to reach full consensus agreement on specific solutions. As widely noted in many EY communications, the international tax changes being contemplated will have implications well beyond digital businesses and digital business models and could lead to significant changes to the overall international tax rules under which multinational businesses operate. It is important for companies to follow these developments closely as they unfold in the coming months and to consider engaging with policymakers at both national and multilateral levels on the business implications of these proposals.

Endnotes

1. Canada, France, Germany, Japan, Italy, United Kingdom and United States.
2. http://www.g7.utoronto.ca/finance/190718-summary.html. The Chair's Summary is very similar in nature to a post-event Communiqué or Declaration.
3. Global Intangible Low-Taxed Income.

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