Global Minimum Tax

This article is based on **"Illusion of redistributive justice"** which was published in The Indian Express on 15/06/2021. It talks about the issues associated with the proposed global minimum tax.

The recent G7 meeting saw the finance ministers of the seven nations communicating their commitment to a **global minimum tax** (GMT) of at least 15 per cent and sharing the excess profits of the 100 largest companies with the countries where they operate.

Since the inception of the **Base Erosion and Profit Shifting (BEPS) programme**, the proposal for GMT is another positive step towards global taxation reforms.

This aims to stop giant companies from shifting their profits to low-tax havens via what are basically shell companies. Another rationale that runs behind this proposal is the rise of money laundering and terror financing.

However, there are many issues associated with GMT, especially pertaining to the developing world. These issues must be resolved before coming to the final agreement.

Understanding Tax Haven

- **Definition:** A tax haven is generally an offshore country that offers foreign individuals and businesses little or no tax liability in a politically and economically static environment.
- **Characteristics:** Characteristics of tax haven countries generally include no or low-income taxes, minimal reporting of information, lack of transparency obligations, lack of local presence requirements, and marketing of tax haven vehicles.

- **Modus Operandi:** Generally, tax havens do not require residency or business presence for individuals and businesses to benefit from their tax policies.
    - Individuals and corporations can potentially benefit from low or no taxes charged on income in foreign countries where loopholes, credits, or other special tax considerations may be allowed in accordance with the law.
    - An IMF research paper estimated that $12 trillion of global corporate investment was "just phantom investment" to avoid tax.
- **Popular Tax Havens:** A list of some of the most popular tax haven countries includes Andorra, the Bahamas, Bermuda, the British Virgin Islands, the Cayman Islands, the Channel Islands, the Cook Islands, Hong Kong, Mauritius, Lichtenstein, Monaco, Panama, British Virgin Islands, and the Cayman Islands.
- **Intranational Tax Havens**: In some cases, intranational locations may also be identified as tax havens if they have special tax laws.
- **Regulatory Oversight:** Worldwide, there are some programs in place to increase the enforcement of offshore investment reporting. The Automatic Exchange of Financial Information is one example, overseen by OECD.
    - To maximize tax receipts, many foreign governments maintain relatively constant pressure on tax havens to release information regarding offshore investment accounts.
    - However, because of the monetary burdens, regulatory oversight may not always be a top national priority.

How Will GMT Work?

- **Taxing Ultimate Parent Entities:** It gives the jurisdictions of the ultimate parent entities — of firms with revenue above 750 million euros — the first right to tax the differential between the actual and the effective tax rate.
- **Mirror Rule:** A mirror rule that gives source countries such as India the right to withhold a higher rate on cross-border payments to low-tax jurisdictions is subject to certain thresholds and more so would require bilateral treaty renegotiations unlike the rules applicable to residence countries.

Associated Issues With GMT

- **Race To Bottom:** The minimum tax will essentially imply that even tax incentives that exist in treaty rates or local tax systems may no longer be available.
    - This remains a problem for developing and underdeveloped countries, where tax incentives work in attracting investment.
    - Even for a country like India, the recent push to bring foreign investors through the international financial services centre is an incentive.

- **Exclusivist in Nature:** The proposal of GMT is exclusivist in nature, as the rules for the world were being decided by select developed countries.
    - Further, there concerns of loss of sovereignty to tax remain for developing countries.
- **Counteractive Effect:** If all nations do not agree to the global minimum tax proposal, it may spark a new sort of competition — corporations will search for countries without the minimum tax rule as their residence.
    - This inturn will result in creation of new tax havens.
- **Dualistic Nature of Developed Countries:** Britain has long connived in creating tax havens in British territories like Bermuda, British Virgin Islands, Cayman Islands, and the Channel Islands.
    - Further, some countries, including India, have already started taxing digital MNCs on the basis of their revenue. It was the US administration that threatened India and other such countries with retaliation.
- **Impeding Development in Developing Countries:** A 15% minimum corporate tax will hit not just tax havens but countries, including India, that offer tax breaks for specific purposes — export industries, investment in backward areas or Special Economic Zones, green investments, R&D, accelerated depreciation, and affecting other legitimate incentives.

Conclusion

The simplest, most honest solution is to decree an Alternative Minimum Tax of 15% regardless of tax breaks. Any country wishing to attain political or social goals through special incentives will have to do so through budgetary grants, not tax concessions.

Drishti Mains Question

The proposal for Global Minimum Tax is a positive step towards global taxation reforms. However, there are many issues associated with it, especially pertaining to the developing world. Discuss.