Mains Practice Question

Q. What do you understand by the term Global Minimum Tax? How does it affect India's economy? Discuss. (150 words)

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- Approach
- Start your answer by briefly explaining about Global Minimum Tax.
- Discuss its implication on Indian Economy.
- Conclude accordingly.

Introduction

- A Global Minimum Tax (GMT) applies a standard minimum tax rate to a defined corporate income base worldwide.
- The OECD developed a proposal featuring a corporate minimum tax of 15% on foreign profits of large multinationals, which would give countries new annual tax revenues of USD 150 billion.
- The framework of GMT aims to discourage nations from tax competition through lower tax rates that result in corporate profit shifting and tax base erosion.

Body

- To address this issue and gain global compliance, an OECD/G20 inclusive framework has been introduced. In June 2021, G7 countries signed a deal agreeing to the framework. On 1st July 2021, around 130 countries including India agreed on the broad deal. The tax framework has the following two pillars:
    - **Pillar one:** The 'largest and most profitable' MNCs need to pay taxes. At least 20% of the profit of the companies above the profit margin of 10% would be reallocated and taxed in the countries where they operate.
    - **Pillar two:** Global minimum corporate tax rate is set at 15% in order to avoid any undercutting.
    - The companies that will be taxed must have annual revenue of at least **Euro 10 billion** and a 10% pre-tax profit margin.
- **Need for Global Minimum Tax:**
    - **Low Tax Jurisdictions:** MNCs follow the system of locating the headquarters wherever the tax is the lowest so that the company ends up paying the tax at a much lower rate. Therefore, the smaller countries such as Ireland (where tax is low) were at advantage, but the bigger countries lost out on tax revenues.
        - G7 countries have announced a minimum 15% tax rate on all MNCs irrespective of whichever place they are so that the advantage of country shifting does not remain.
        - There GMT must be fixed to avoid countries undercutting each other.
    - **To Bring Uniformity:** GMT will end a decades-long race to the bottom in which countries have competed to attract corporate giants with ultra-low tax rates and exemptions. And it will bring uniformity in corporate taxation worldwide.
    - **Multilayering by MNCs for Profits:** Digital giants such as Apple, Alphabet and Facebook, as well as many other major corporations typically rely on complex webs of subsidiaries to hoover profits out of major markets into low-tax countries such as Ireland or Caribbean

nations such as the British Virgin Islands or the Bahamas, or to central American nations such as Panama.
        - India loses **USD 10.32 billion** annually to global tax abuse, equivalent to the annual salary of **4.23 million nurses** and 44.7% of the health expenditure. According to a study, debt shifting, registering intangible assets (copyright and trademarks), and strategic transfer pricing are some ways in which MNCs practice tax evasion in the country they operate and shift it to tax havens.
- **Impact on Indian Economy:**
    - **Bringing Equality:** In the Indian context, the GMT will bring equality to those people maybe operating in India but not located in India and therefore not paying any taxes.
    - **Attract Investments:** India is likely to benefit from the global minimum 15% corporate tax rate pact as the effective domestic tax rate (other than in Special Economic Zones) is above the threshold.
        - In all probability the concessional Indian tax regime would still work, and India would continue to attract investments.
    - **India at Advantage:** Due to India's tax rates too, it will be in an advantageous position because Indian tax rates have come at a position where India can afford to give concessions to big companies and yet not fall down at the international tax rates.
    - **Challenge:** Although the 15% GMT will not affect the current investments in India, setting up more SEZs or giving incentives to companies to invest in India will be a challenge.

Conclusion

This initiative of the G7 countries is a welcome move to address the different challenges that many countries are facing. Putting in place a global corporate tax at the minimum slab fixed by the G7 will majorly impact the developing economies.