G7 Finance Ministers commit to Pillars One & Two, including global minimum tax rate of 'at least' 15%

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In brief

The G7 Finance Ministers announced an agreement on June 5, in which the participating countries committed to new taxing rights that allow countries to reallocate some portion of profits of large multinational companies to markets (i.e., where sales arise—'Pillar One'), as well as enact a global minimum tax rate of at least 15% ('Pillar Two'). The meeting marked an early test of whether the US position on the OECD Inclusive Framework's 'Taxation of the Digitalising Economy' project would provide momentum to finding a common base for agreement.

In detail

In the communiqué, the G7 Finance Ministers noted a commitment to "reaching an equitable solution on the allocation of taxing rights, with market countries awarded taxing rights on at least 20% of profit exceeding a 10% margin for the largest and most profitable multinational enterprises. We will provide for appropriate coordination between the application of the new international tax rules and the removal of all Digital Services Taxes, and other relevant similar measures, on all companies. We also commit to a global minimum tax of at least 15% on a country by country basis."

Observation: The agreement would involve a careful mix of political trade offs as it would result in both winners and losers for different countries on separate issues. At least in theory, large developed countries may benefit in the sense that the largest markets would attract most of the new income reallocated under Pillar One. Under Pillar Two, many of them already have higher tax rates and often represent the headquarters jurisdiction that should receive a large part of the top-up relating to low-tax jurisdictions (if any). By contrast, smaller jurisdictions such as Ireland, Singapore and Switzerland may stand to lose some tax revenues under Pillar One and would face stiffer competition for inward investment as a result of Pillar Two. There is also a question as to whether this agreement would benefit developing countries.

The G7 members (Canada, France, Germany, Italy, Japan, United Kingdom, and United States) have no formal power to fashion an agreement that is binding on other countries—the G20 is the mandated group -- although as the largest world economies, any actions taken often have significant effects on global issues.

The next important tests for the agreement are the OECD Inclusive Framework meetings at the end of June, and the next G20 Finance Ministers meeting on July 9-10 in Venice. Any decision taken then by the G20 is more likely to have an impact on the forward movement of the OECD project. The G20 includes countries like Brazil, China, India and Russia, which to date have been more hesitant on some of the elements discussed in the OECD's Pillars One and Two. The G20 countries account for a major share of global economic investment, production, and corporate tax base, so any agreement in July would go a long way in creating a consensus of how mostly developed economies intend to resolve frustrations voiced around the current international tax rules. However, given some outstanding differences still to be resolved, including the thorny issue of repeal of various G20 members' Digital Services Taxes (DSTs), it is not clear how much detail the Finance Ministers may agree. Some tough -- and important -- decisions are likely to be deferred until October.

So, although public officials and media outlets have termed the agreement as 'historic' and conveyed the sense that global adoption is inevitable, while there is clearly momentum, there nevertheless remain numerous political and technical elements of disagreement among countries that will have to be bridged for real consensus to emerge. There is also an implementation challenge as the European Union – which forms an important bloc of economic power – must unanimously agree to certain legal changes for tax issues in their Directives. To date, several EU members have expressed strong opposition to any global minimum tax that impinges on their sovereignty to establish corporate tax rates, especially if the agreed rate is set at a level such as 15% or above.

The takeaway

While much attention in the coming days will be focused on the statements from the G7 meeting, a more important indicator of whether major corporate tax changes are coming will be those determinations made by the Inclusive Framework at the end of June and the G20 Finance Ministers next month. Even with an agreement in July, further important design elements will still need to be decided. Also, we expect that the coordination between the application of any new rules and repealing DSTs may have its own dynamics. Implementation of any new rules is likely to take several years and is likely to create additional complexities for globally-engaged taxpayers, as countries are very unlikely to implement any agreed rules in exactly the same way and with the same effective dates.

Let's talk

For a deeper discussion of how the G7 Finance Ministers' agreement might affect your business, please contact:

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