Tax Policy Alert

Global Minimum Tax and International Investment Treaties: Risks & Opportunities

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In brief

What happened?

The Global Minimum Tax (GMT) rules forming part of Pillar Two consist of a set of rules politically agreed by the OECD Inclusive Framework ("IF") in 2021/2022 by more than 140 countries. The rules aim to solve remaining BEPS issues and to set the floor for tax competition at a country-specific minimum Effective Tax Rate (ETR) of 15%. As of mid-2025, 55 jurisdictions have implemented the GMT wholly or partly (see here). The GMT rules in those jurisdictions alone bring into scope most of the global entities of large multinational groups, thereby representing critical mass for the rules to take effect.

In many instances, the GMT might impact a business's return on investment (ROI) in a way that poses the risk of infringement of obligations of jurisdictions under international investment agreements (IIAs) ratified by a majority of states globally (see here). Notably, the GMT may be at odds with investment protection standards, which could prompt multinational groups to initiate arbitration under IIAs against states, or, at least, to negotiate with states to find alternative solutions.

This topic is currently very important, not least because of the US-G7 agreement to pursue a "side-by-side" approach between the GMT and the US tax rules, and the Belgian Constitutional Court decision of 17 July 2025 which refers the Undertaxed Profits Rule (UTPR) to the Court of Justice of the European Union. Both of these developments may have an impact on the extent to which the GMT influences (particularly US) multinationals ROI, and therefore the taxpayer's legitimate expectations under the relevant IIA.

Why is it relevant?

The interplay between the GMT and IIAs is of significant relevance for multinational groups and states for (i) legal (certainty and protection) and (ii) monetary reasons:

(i) IIAs (international law) override the GMT (domestic law) in most jurisdictions. Even if constitutional law allows for treaty override, customary international law (CIL) generally provides that the domestic laws should respect these international obligations. Any conflict between the GMT and IIAs is open to cross border litigation or arbitration;

(ii) Tensions between the GMT and IIAs may affect the investment climate of states, discourage investors and increase the price of contemplated projects. The most vulnerable are low-income developing countries insofar as the GMT directly affects the rationale of special economic zones (most often found in these countries) that provide tax holidays (0% of effective tax rate) for foreign investors.

Strategically managing these interactions can optimize investment outcome, investment attractiveness, risk profile, reputational exposure and compliance.

Actions to consider

Multinational groups and states may consider taking the following precautions:

1. *Risk identification and evaluation* — recognizing that there are IIA protection standards that might be invoked under specific circumstances against taxation under the GMT and modeling the potential financial impacts of GMT on existing investments, highlighting areas of potential risk.

2. *Reassessment of tax incentives* — evaluating tax incentives to understand whether they are still effective or not. If they are not, businesses should alert states so that they might amend them to ensure their continued effectiveness; or consider repealing them from the domestic tax system in accordance with IIAs, i.e. without violation of any investment treaty protection standard.

3. *Risk mitigation* — deciding whether there is a justification for states for (i) transforming income-based tax incentives into Qualified Refundable Tax Credits (QRTC), noting what constitutes a QRTC may change; (ii) a general replacement of tax incentives with non-tax incentives such as "reduced customs duties, sales or excise taxes, or renegotiated royalty agreements in case of natural resource projects"; (iii) entering into a dialogue with specific investors negatively affected by the GMT to provide them with non-tax incentives.

4. *Policy alignment and strategic planning* — align policy frameworks with investment strategies and evaluate IIA frameworks with GMT requirements.

In detail

What is the issue between the GMT and IIAs?

The GMT approach to taxation impacts the future of FDI attraction through tax incentives that lead to an effective tax rate below 15%. It may trigger conflicts with provisions in state's IIAs primarily by: (i) violating investors' legitimate expectations not to revoke prematurely tax incentives reducing their tax burden to an effective tax rate below 15%; (ii) indirectly expropriating low-taxed constituent entities; and (iii) treating foreign investors worse than domestic ones.

Four key investment treaty protection standards

The four standards of investment treaty protection which are most likely to cause tensions with the GMT are: (i) fair and equitable treatment (FET); (ii) the umbrella clause; (iii) non-discrimination; and (iv) and non-expropriation. In the majority of IIAs, tax carve outs will be of no or little relevance to eliminate investment protection under IIAs in respect of the GMT rules.

FET

A breach of FET is the most frequently invoked claim in investor-state dispute settlement (ISDS) cases overall, including tax related cases. It is also recognized as the most relevant investment protection standard under IIAs against the GMT. Among core elements of FET recognised by the investment treaty jurisprudence of vital importance to the GMT are: (1) the requirement of stability, predictability and consistency of the legal framework and (2) the protection of investor confidence or legitimate expectations. Arguably the most important among such investments are those in the energy sector, which are at the same time of strategic importance for states around the world.

Umbrella clause

Irrespective of alleged violations of any other investment protection standard, the state's promises may be brought under the protective scope of IIAs via so-called umbrella clauses. Such clauses oblige the host states to comply with obligations the state has entered into with respect to investments protected by the treaty in which the umbrella clause is found. Umbrella clauses extend to all obligations arising under any investment contract between the host state and an investor (parties of the IIA with an umbrella clause). In the absence of an umbrella clause, a violation of contractual obligations by the host state would not be covered by the IIA, unless that violation was so severe that it violated any of the IIA's standards of investment protection. Investors often look for a state's promises to include specific provisions such as tax stability provisions, set-off clauses, adjustment clauses, advance tax rulings, or other agreements relating to the tax treatment of investment in order to be better protected against unforeseen tax measures. As a result, application of the GMT may be in conflict with IIAs when such application leads to taxation contrary to the relevant agreement between a state hosting investment and an investor.

Non-expropriation

The prohibition of indirect expropriation is the second most frequently invoked standard of investment treaty protection in tax-related cases. It is *indirect* expropriation because it is done via tax measures. It is generally illegal under investment treaties for a host state to deprive an investor of its investment without prompt, adequate and effective compensation. In principle, IIAs do not preclude states from expropriating investments if the action is for a public purpose, is done in a non-discriminatory manner under due process of law and involves the payment of compensation.

This standard of investment treaty protection is relevant for investors whenever a tax assessment exceeds the capacity of the local investment entity to pay tax, thereby threatening the entity's solvency, leading to the permanent loss of ownership or control over that investment by a foreign investor. In such instances, taxation renders the investment worthless and thus subject to application of the expropriation clause under a relevant IIA.

The threshold of indirect expropriation in investment treaty tax-related cases is very high. It may be crossed by one of the GMT rules – the UTPR – in at least two scenarios: (1) imposition of the UTPR on loss making constituent entities (CEs) or (2) imposition of the UTPR on other CEs in situations in which the amount of top-up-tax equals or exceeds their income and assets.

Non-discrimination

National treatment (NT) precludes *de jure* and *de facto* discriminatory treatment of foreign investments in comparison to domestic ones in like circumstances. According to investment treaty case law, a taxation measure violates NT even if discrimination was not the legislative intent behind the measure if the result of its application leads to a less favourable treatment of the foreign investor in comparison to the domestic one. Thus, whenever the GMT rules lead to such taxation, investors can invoke NT to arbitrate against a host state levying it.

The special case of the UTPR

Focusing on the UTPR when considering strategic litigation and arbitration is of special importance for multinational groups because this GMT rule is a highly contentious rule under international law. The QDMTT-UTPR and the IIR-UTPR interactions explicitly encourage states to engage in non-customary extraterritorial taxation. If there is any residual amount of top-up tax that remains unallocated after the QDMTTs or IIRs apply, the UTPR allocation mechanism applies in the states that introduced the UTPR. This threatens existing tax policy in many states insofar as the UTPR forces tax collection in respect of states that have deliberately chosen not to adopt a QDMTT or IIR. Taxation under the UTPR is also potentially in conflict with bilateral tax treaties, in particular article 7(1) of the OECD/UN Model Tax Convention, as well as their non-discrimination provisions (Kuźniacki & Vergouwen (2025)).

The fixed income allocation formula under the UTPR, based on the share of total employees and tangible assets, permits for taxation of profits of a foreign entity without any significant link of that entity with an economic activity in the state imposing the tax. The profits subject to tax under the UTPR are neither directly nor indirectly owned by the resident taxpayer (i.e., local constituent entity). Many tax experts consider such taxation as extraterritorial, asserting bad faith and negligence in designing the UTPR because its extraterritoriality "departs from one of the fundamental elements of tax jurisdiction — the nexus requirement — in an unprecedented way.

The UTPR's characteristics may make it vulnerable to challenge as a potential violation of the major investment treaty protection standards of relevance to the GMT. It also means that a neutralization of the UTPR's effect by means of a reconciliation between states and investors (e.g. providing non-GMT related benefits) would considerably reduce conflicts between the GMT and IIAs.

Approaches championed by international organizations

The OECD

In 2022, the OECD recognized a potential conflict between the GMT and IIAs (OECD 2022, paras 21-22). In 2023, the OECD recommended that countries add a rule to their domestic legislation implementing the GMT, according to which any legal challenge of a multinational group against the QDMTT on the basis of law superior to the GMT rules, e.g. IIAs, will permit another jurisdiction to collect additional tax under the IIR or the UTPR in order to prevent the taxpayer from achieving any tax savings by applying the IIA (OECD 2023, paras 73-81). This approach aims to discourage multinational groups from legally challenging the QDMTT via IIAs by apparently making such challenges economically unviable, i.e., the challenge in the QDMTT state will lead to inevitable taxation under the IIR and the UTPR in other states.

***Observation**: It is questionable whether the OECD's recommendation will persuade multinational groups not to arbitrate against states imposing the GMT on their profits. A payment of compensation in line with the arbitral award by the host state does not necessarily trigger additional tax elsewhere through the IIR or the UTPR. This all depends on very specific rules around the computation of covered*

and adjusted covered taxes, allocation of taxes among countries, and the applicable accounting rules. In addition, the amount of top-up tax paid in the host country under its QDMTT and compensated as a result of the arbitral award may be different from the top-up tax to be paid in the home country via IIR or the third country via UTPR. The final financial result will be driven by different factors such as the level of flexibility around financial accounting standards afforded by different countries. Further, even if payments of compensation may raise difficulties in operation of IIAs and determination of final benefit for investors, such difficulties may have little bearing on the motivation of some investors to pursue arbitration challenges.

***Observation**: Given the G7's statement on side-by-side co-existence of Pillar Two Rules and the U.S. minimum tax rules, as well as the G7 commitment to pursue further simplification of the Pillar Two Rules and to re-examine the treatment of incentives, the OECD may consider to undertake a more conciliatory approach towards the application of the global minimum taxation rules. Notably, the IF members (147 states and jurisdictions) may voice a need for more concessions that benefit their economic interests and allow them to comply with obligations under IIAs. For example, a distinction between refundable and non-refundable tax credits could be abandoned together with the concept of collateral benefits either in general or, at least, in respect of multinational groups protected by IIAs.*

The UN

The UN recommends states to undertake "a coordinated action with respect to tax and investment policymaking on the international plane" in order to enact "a multilateral instrument that clarifies the relationship between the GMT and IIAs to create legal certainty and ensure that the latter does not impede the implementation of the former" (UNCTAD 2023, pp. 15-16). The UN also suggests that states organize "inter-ministerial task forces that allow different government stakeholders to exchange experiences and work in an integrated manner [that] can help to ensure a consistent approach to tax-based incentives for investment", i.e. "[m]ost tax administrations could develop technical expertise with respect to IIA disciplines through closer interaction with government departments in charge of the negotiation of IIAs and the defence of ISDS cases and vice versa." Finally, the UN highlights that investors can rely on IIAs to convince countries to grant them incentives that provide economically comparable benefits to corporate tax incentives, for example, reduced customs duties or renegotiated production sharing agreements (UNCTAD 2023, p. 1).

***Observation**: The UN aims to induce states and multinational groups to avoid arbitration under IIAs through a conciliatory process, which focuses on replacing tax incentives with non-tax incentives or providing QRTCs. Such an approach, if broadly adopted, could result in increased legal certainty in tax and investment domains.*

Let's talk

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