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The Global Tax Agreement in the face of the concerns of developing countries

What are the weeknesses of the OECD initiative?

The OECD has been examining tax issues related to the digitalisation of the economy since the launching of the initial Base Erosion and Profit Shifting (BEPS) project in 2013. In 2019, the OECD launched the BEPS 2.0 project, which includes Pillar 1 on new tax and profit allocation rules and Pillar 2 on global minimum tax rules. Currently, 141 jurisdictions are participating in the BEPS 2.0 project under the Inclusive Framework.[1]

Indeed, in October 2021, a final political agreement was reached on the key parameters of the two pillars and an implementation plan.

"Pillar 1" aims at better taking into account the interests of destination countries of the various goods and services of digital companies and the profits generated by these sales. In fact, the idea is to suggest a profit allocation formula that takes into account not only the country where the company has its headquarters, but also the consumer states, to allocate to the latter a fraction of the profits made in their territory by companies that are not established there.[2]

This new tax rule only applies to companies with an average global turnover of more than €20 billion and a profit margin before tax of at least 10%. In other words, if a company earns 20 billion euros in revenue and 3 billion euros in profits, the first 2 billion euros (10 percent of revenue) are excluded from the rule. Of the remaining €1 billion in profits, €250 million (25 percent of the residual) is subject to tax in end-market jurisdictions (using a pre-agreed global reallocation formula). It is planned to reduce this turnover threshold under pillar 1 to €10 billion after seven years if implementation goes well. The first pillar includes a special purpose rule that requires a multinational enterprise to generate at least €1 million in revenue in order for a market jurisdiction to benefit from a reallocation of residual profits (i.e. to have a taxing right)[3].

It is also important to note that these rules may have other implications for the profits that will be generated under this pillar that are uncertain and conditioned. Indeed, the global tax agreement obliges source countries to waive their tax rights and waive taxation of digital services, which implies a loss of tax sovereignty for an uncertain income.

[1] OECD releases public consultation document on Regulated Financial Services Exclusion under Amount A for Pillar One, EY, 16 mai 2022. https://taxnews.ey.com/news/2022-0777-oecd-releases-public-consultation-document-on-regulated-financial-services-exclusion-under-amount-a-for-pillar-one

[2] Martin Collet, « Taxation of the digital Economy : global challenge, local responses?», RED 2021/1 (N° 2)

[3] Ting, Antony, iTax - Apple's International Tax Structure and the Double Non-Taxation Issue (March 19, 2014). British Tax Review 2014 No.1, Available at SSRN: https://ssrn.com/abstract=2411297

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In his article entitled "Global Tax Agreement – Tunisian Perspectives", Chafik Ben Rouine indicates that the concept of source country became more difficult to define when economic activity became digitalized and the concept of destination country (where sales take place) appeared in order to remedy it. Besides, many countries have implemented tax exemptions and incentives to attract MNEs to their country through 10-year corporate tax exemptions, VAT exemptions or other high-cost exemptions, especially for developing countries.[4]

While the political commitment shown by the G7 (consisting of Canada, France, Germany, Italy, Japan, the United Kingdom and the United States) to major international tax reforms and facilitated by the OECD is commendable, Mustapha Ndajiwo and Learnmore Nyamudzanga[5] show that critics have raised concerns about the influence of developed countries in setting international tax standards. The multinationals that have benefited from the existing rules are mostly headquartered in developed countries. A key question would be whether developing countries, although included, could actually influence the framework to make it in favor of Africa.

The refusal of Kenya and Nigeria to sign the declaration of the Inclusive Framework could be interpreted as a sign of the extent to which the continent is far from finding a lasting solution to the challenges of taxing companies that derive huge tax-free revenues from its jurisdiction by maintaining no physical presence there.

The key concern is that although the G7 countries make up only 10% of the world's population, their proposal will influence more than 200 tax jurisdictions. According to estimates by the Tax Justice Network Africa, the G7 will receive 60 per cent of the additional revenue from Pillar 2, leaving only 40 per cent to the world's remaining population (90 per cent). [6]

These concerns also stem from the fact that Pillar Two imposes a fairly low minimum tax rate.

The African Tax Administration Forum (ATAF) estimates that the nominal corporate tax rate in Africa is between 25% and 35%[7]. Although the rate of 15% is low and should be higher, the concentration of criticism on this point has put the essential in the background. Indeed, "it is important to highlight how this rate will be applied in order to measure its effects. This rate will apply for each MNE individually and the rate of 15% is an effective rate and not a nominal one. The difference is significant, especially for developing countries. Whether through generous tax incentives and exemptions from governments, or tax optimization or even the use of

[4] Chafik Ben Rouinen « Accord fiscal mondial – Perspectives de Tunisie», Fondation Rosa Luxemburg - Afrique Du Nord, 2022. Disponible via le lien suivant : https://rosaluxna.org/fr/publications/accord-fiscal-mondial-perspectives-de-tunisie/#:~:text=Le%201er%20Juillet%202021%2C%20130,l'impl%C3%A9menter%20au%20niveau%20national.

[5] Mustapha Ndajiwo and Learnmore Nyamudzanga, "Que signifie la proposition du G7 sur la taxation de l'économie numérique pour les pays africains ?" Africa's Digital Agenda, 3 septembre 2021, https://afripoli.org/what-does-the-g7-proposal-on-taxation-of-the-digitalised-economy-mean-for-african-countries

[6] Mustapha Ndajiwo and Learnmore Nyamudzanga, "Que signifie la proposition du G7 sur la taxation de l'économie numérique pour les pays africains ?" Africa's Digital Agenda, 3 septembre 2021, https://afripoli.org/what-does-the-g7-proposal-on-taxation-of-the-digitalised-economy-mean-for-african-countries

[7] https://www.ataftax.org/a-new-era-of-international-taxation-rules-what-does-this-mean-for-africa

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transfer prices by MNEs, the effective rate actually paid is very often well below the nominal rate announced in the law. For instance, researchers Ndajiwo and Nyamudzanga showed that although the nominal tax rate was 30% in Nigeria, the effective rate was rather 6% below the 15% rate in the overall agreement.[8] ”[9]

Mustapha Ndajiwo and Learnmore Nyamudzanga also show in a Policy Brief published on September 3, 2021 entitled “What does the G7 proposal on taxation of the digital economy mean for African countries?”, that among the 26 African members of the Inclusive Framework, Nigeria, South Africa, Côte d'Ivoire and Senegal are part of the Steering Group. In addition, some countries have also joined pressure groups such as the G24, which was created in 1971 by a group of developing countries, and which represents the interests of developing countries in economic matters and now consists of 28 member countries plus China (as a “special guest”). Six of the G-24 countries are also members of the G20: Argentina, Brazil, China, India, Mexico and South Africa. In addition to the G20, 12 other G-24 members are also members of the Inclusive Framework (Colombia, Côte d'Ivoire, Egypt, Gabon, Haiti, Kenya, Morocco, Nigeria, Pakistan, Peru, Sri Lanka and Trinidad and Tobago).[10]

In previous comments, the G-24 had called for a share of more than 30 per cent of profits to be reallocated to destination countries and for greater room for reallocation. The Inclusive Framework Agreement concluded in July did not adopt the scope change proposed by the G24

and established a potential range to be attributed to market jurisdictions of 20% to 30% of residual profits (i.e. profits above 10% of revenues).[11]

In the light of all these data, it might be useful to review the alternative solutions proposed by international organizations such as the United Nations Tax Committee and the Independent Commission for the Reform of International Corporate Taxation (ICRICT). It should also be noted that the Expert Group of the Financial Accountability, Transparency and Integrity FACTI, among others, and other civil society actors have advocated for the establishment of a global tax body under the auspices of the UN with the aim of increasing legitimacy, fairness and inclusiveness in the development of global tax reforms.

If the idea of a new entity opens the discussion on the conditions of its creation and its functioning, the voices agree in any case on the need to open negotiations on a global tax convention under the auspices of the United Nations. This alternative negotiating framework to that of the OECD could offer more transparency, inclusiveness and fairness in global tax governance. Finally, this framework would also allow us to

[8] https://afripoli.org/what-does-the-g7-proposal-on-taxation-of-the-digitalised-economy-mean-for-african-countries

[9] Chafik Ben Rouinen « Accord fiscal mondial – Perspectives de Tunisie», Fondation Rosa Luxemburg - Afrique Du Nord, 2022. Disponible via le lien suivant : https://rosaluxna.org/fr/publications/accord-fiscal-mondial-perspectives-de-tunisie/#:~:text=Le%201er%20Juillet%202021%2C%20

[10] https://www.g24.org/wp-content/uploads/2021/10/G-24-warns-that-global-tax-deal-will-fail-without-better-terms-for-developing-countries-%E2%80%93-MNE-Tax.pdf

[11] https://www.g24.org/wp-content/uploads/2021/10/G-24-warns-that-global-tax-deal-will-fail-without-better-terms-for-developing-countries-%E2%80%93-MNE-

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think about these reforms from the perspective of their contribution to the realization of human rights, an approach and a demand promoted by certain civil society organizations that were recently supported by the United Nations Independent Expert on foreign debt and human rights, Attiya Waris. [12]

[12] Mustapha Ndajiwo and Learnmore Nyamudzanga, "Que signifie la proposition du G7 sur la taxation de l'économie numérique pour les pays africains ?" Africa's Digital Agenda, 3 septembre 2021, https://afripoli.org/what-does-the-g7-proposal-on-taxation-of-the-digitalised-economy-mean-for-african-countries

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