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What Exactly Did the Inclusive Framework Agree to Last October?

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Recent developments suggest that the member countries of the OECD-led Inclusive Framework on BEPS may not share the same understanding of what was supposedly agreed to in October 2021. Jeff VanderWolk of Squire Patton Boggs discusses the current causes of uncertainty.

The New Zealand Inland Revenue issued a consultation document earlier this month on the possible implementation in New Zealand of the GloBE rules—i.e., the main component of Pillar Two, the global minimum tax regime. The second paragraph of the document undoubtedly raised a few eyebrows around the world:

“In October 2021, the 2 Pillar solution [to reform the international income tax framework in response to the challenges posed by the increasing globalisation and digitalisation of the economy] was endorsed by over 130 countries in the OECD-sponsored Inclusive Framework, including New Zealand (this endorsement is referred to as the October Statement). This endorsement did not bind any country to adopt either Pillar. The Government has not decided whether to adopt either Pillar One or Pillar Two and has not ruled out adopting a digital services tax.”

This flies in the face of the many public statements by senior officials that the October agreement would ensure that unilateral measures such as digital services taxes could no longer be used by any country that agreed to the deal.

In contrast to New Zealand’s view, a policy paper on Pillars One and Two issued in April 2022 by the government of Jersey says that Pillar One is a “minimum standard” that all signatories of the October statement are obliged to implement, if possible. The Jersey document notes that “GloBE by contrast is not a minimum standard, but a ‘common approach.’ It is therefore not mandatory for Jersey to implement it.”

Jersey's view is based on the implication that Pillar One must be mandatory because Pillar Two is expressly said to be non-mandatory in the October statement. Reinforcing Jersey's view is the following statement in the Inclusive Framework's Report on the Pillar One Blueprint (October 2020): "It is expected that any consensus-based agreement under Pillar One must include a commitment by members of the Inclusive Framework to implement this agreement and at the same time to remove relevant unilateral actions."

In the wake of the statement last October, the G20 leaders considered the two-pillar solution during their meeting in Rome on October 30-31, 2021. Their declaration at the end of the meeting blessed the Inclusive Framework's "historic achievement" and included the following statement:

"The final political agreement as set out in the Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy and in the Detailed Implementation Plan, released by the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS) on 8 October, is a historic achievement through which we will establish a more stable and fairer international tax system. We call on the OECD/G20 Inclusive Framework on BEPS to swiftly develop the model rules and multilateral instruments as agreed in the Detailed Implementation Plan, with a view to ensure that the new rules will come into effect at global level in 2023."

As for the October statement and Detailed Implementation Plan referred to by the G20 leaders, there is no explicit mention of the mandatory nature of Pillar One. But as noted above, the explicit statement that Pillar Two implementation is not mandatory implies that Pillar One is different in that regard. The plan refers to being "committed to the Statement" in the following passage regarding Pillar One implementation: "The Inclusive Framework has mandated the Task Force on the Digital Economy (TFDE) to define and clarify the features of Amount A (e.g., elimination of double taxation, Marketing and Distribution Profits Safe Harbour) and develop the Multilateral Convention and negotiate its content, so that all jurisdictions that have committed to the Statement will be able to participate."

In addition, the Detailed Implementation Plan says at the outset that Inclusive Framework members "are fully committed to use all efforts within the context of their legislative process" to implement the agreement on the two-pillar solution.

Where does this leave us? New Zealand's assertion that it can choose not to implement Pillar One and to enact a digital services tax doesn't appear to have a basis in the text of the relevant documents. It does indicate, however, that countries take national sovereignty in tax policy for granted, regardless of whether they have joined other countries in signing a high-level statement of agreement to implement certain tax proposals in common.

For taxpayers, this means that the implementation of the new rules under either of the pillars is likely to be inconsistent, as each country will do what it thinks is best for itself.

Meanwhile, the implementation of Pillar Two remains uncertain. The EU finance ministers have already failed twice to approve the draft EU directive on the implementation of the GloBE rules in the laws of the member states. Poland insists that the global agreement embodied in the October statement included a commitment to concurrent implementation of Pillars One and Two, and therefore the Pillar Two rules should not be adopted on a standalone basis. When the finance ministers meet again toward the end of this month, the rest of the world will be watching.

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