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WEBINAR

GLOBAL CORPORATE TAX REFORM:
WHY IT'S IMPORTANT AND WHAT IT WILL DO (AND NOT DO)

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Introduction:

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Moderator:

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Discussants:

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P R O C E E D I N G S

MR. WESSEL: Good morning. I'm David Wessel, Director of the Hutchins Center on Fiscal and Monetary Policy at the Brookings Institution. With so much going on in the world, the Russian invasion of Ukraine, the persistence of the pandemic, the burst of inflation, there are major economic policy issues that aren't getting the attention that they deserve, and one of them is the subject of our conversation today. The effort by 136 or so countries to change the way they tax multinational corporations, both to discourage a race to the bottom among companies to set low corporate taxes, and to make it harder for firms to park their profits in low tax countries.

Now, I found that much of what is written and said about this is aimed at people who are already well-versed in the details of corporations. People who speak in acronyms like BEPS, which stands for the Base Erosion and Profit Shifting Initiative of the OECD, the Organization for Economic Cooperation and Development. Our goal today is a little different. We want to explain to people who know these issues are important but haven't studied up on them. And we're going to try and keep the undefined acronyms to a minimum.

We're going to try and do a lot in 90 minutes, but if you have questions, please share them on Twitter at #globaltax, by email events@brookings.edu, and on a website called Slido, S-L-I-D-O, where you can use the #global tax. We're going to start and end our morning with Lilys, different Lilys. We're going to open with a presentation in a moment by Lilian Faulhaber, who is a professor of law and associate dean for research and academic programs at Georgetown. And we've asked her to give a primer on what this is all about. Then my colleague from the Brookings Urban-Tax Policy Center, Thornton Matheson, is going to moderate a panel of three people who are well-versed in these issues. Dhammika Dharmapala, from the University of Chicago Law School, Alex Klemm, from the

International Monetary Fund, and Pam Olson, of PricewaterhouseCoopers, and a former Assistant Secretary for Tax Policy of the Treasury. And then, finally, we're lucky to be joined by Lily Batchelder, who is the current Assistant Secretary for Tax Policy on leave from the NYU Law School. So, with that, I'd like to turn the virtual podium over to Lily Faulhaber.

MS. FAULHABER: Great, thank you so much. I'm thrilled to be here and I'm excited to be opening this discussion. So, let me share my screen quickly. Great. Can everyone see that? That's great, excellent.

Okay. So, I have been given about 15 minutes to just give an overview of what is this agreement? What's going on? Where are we? In order to sort of open the floor for the panelists to discuss the import of this the likelihood of significant changes.

So, let me start off with just the big picture of where are we? So, right now, we have 137 countries that have agreed to what's called a two-pillar corporate tax reform. So, the two pillars are made up of Pillar One and Pillar Two. Pillar One, as a very general matter, is made up of new additions to allocation and nexus rules. So, what does that mean? The question is what countries get to tax income and what is that allocation of income based on, right? How do countries divide a company's income when companies are doing business in several countries.

Pillar One sets out new rules on top of the existing rules about how to allocate income, to whom, and based on what. Pillar Two is a minimum tax that applies to the foreign subsidiaries of multinational corporations. So, that's essentially addressing what happens when multinationals are shifting their income into low tax jurisdictions. Is there a way for the parent jurisdictions of those multinationals to discourage other jurisdictions from having low tax rates. And so, this is a minimum tax that tries to address this. So, I'll go into more specifics in a few minutes. But that's just the big picture for understanding sort of where we are.

So, now, the next question is how did we get here? Well, so, how did we get here? We've had years of concerns since the early 2000s about the international tax system just not keeping up with the current economic climate. There have been concerns about the so-called digital economy. Sometimes Europeans have referred to this as concerns about the GAFAs, Google, Apple, Facebook, and Amazon. There have been concerns about tax competition, which is normally meant to mean a country is imposing low tax rates to compete against countries with higher tax rates.

There have been concerns about mobility of income and the reliance on intangibles. The idea that income can just be booked in different countries and that the fact that so much value comes from intangibles, means that those intangibles themselves can be placed in different countries on paper and that income can be allocated to different countries. And on top of this, there's just been an increasing need for revenue.

So, some of these concerns have been packaged as concerns about a level playing field or companies paying their fair share. And these are basically all the same concerns. They're concerns that multinationals are able to avoid corporate income tax in multiple jurisdictions because they're able to shift their intangible assets and, therefore, their income to lower tax jurisdictions. This has come up particularly in the context of these so-called digital companies because they're, in particular, able to earn significant revenue but not pay taxes in the countries where customers or users are located. So, this has been just a constant discussion over the last few decades.

So, these have been all these concerns, and for years, countries and international organizations have been trying to address these concerns. So, the first approach to this was the OECD's BEPS Project. So, this was from 2013 to 2015. It was the Base Erosion and Profit Shifting Project and it involved 44 countries. It focused on 15 different so-called action items. And what they were meant to do was to address income

shifting across jurisdictions.

Now, one of these action items was Action One. Action One was titled, Addressing the Tax Challenges Arising from the Digitalization of the Economy. And Action One created the Task Force on the Digital Economy, the TFDE. I know that we are not supposed to use acronyms, but I'm just going to come back to the TFDE in a few minutes. And so, Action One created this task force, but at the end of 2015, when the BEPS Project issued its final reports, the final report from Action One essentially said this task force couldn't reach any conclusions on the digital economy. It couldn't define the digital economy. It couldn't define solutions to the digital economy. What it could agree was that the digital economy could not be separated from the rest of the economy.

So, the BEPS Project did lots of great things. I'm biased because I worked on it. But the digital economy work was -- essentially produced something where there wasn't really any recommendation or best practices. In response to this, lots of countries ended up imposing unilateral measures.

So, here's another selection of acronyms. So, there were many, many digital services taxes. Many of you probably heard of the French digital service tax. That got a lot of attention. The U.S. trade representative imposed but didn't actually force the sanctions on France in response to it. The U.K., and some other countries, imposed things called diverted profits taxes, or DPTs. Australia and other countries ended up imposing things called multinational anti-avoidance laws. There were substantial economic presence rules. There were new withholding taxes. There were a whole variety of unilateral measures.

And the general idea of all of these unilateral measures is that these were new types of taxes that were designed to capture revenue from large multinationals that did not have a physical presence in the jurisdiction. Because one of the fundamental parts of

our international tax system is that when profits from a corporation are being allocated between countries, they're being allocated based on physical presence. And so, what these unilateral measures were doing is they were essentially saying the current rules won't allocate income to our jurisdiction. And so, we're going to come up with a different solution to allocate income to this jurisdiction.

Another response to the concerns about digital taxation, an outdated international tax system, all of these concerns I listed in the previous slide, another response to this was the 2017 tax reform in the United States. And one of the main ways that the U.S. was responding to concerns about tax competition was to itself engage in some tax competition to lower its tax rate. But there were also some brand-new provisions that were put into this 2017 tax reform that are going to become important in the next few minutes.

And two of those primary ones were GILTI, the global intangible low-taxed income provision, and BEAT, the base erosion and anti-avoidance tax. And the GILTI was the first example of a minimum tax that applied to foreign subsidiaries of U.S. multinationals. It essentially says, if you are a foreign subsidiary of a U.S. multinational, and you pay less than a certain percentage in taxes in that foreign country, you're going to have to make up the different in the United States. You're going to essentially pay a top-up tax to the United States. So, if you pay less than 10.5 percent in taxes, you're going to pay the difference between 10.5 percent and the amount that you paid to the United States.

What's the theory behind this? The theory behind it is that there's money on the table, right? The theory behind it is that up until now a country with a 5 percent tax rate could attract multinationals, the subsidiaries of U.S. multinationals, because they would owe 5 percent. But now, if they pay 5 percent, they're still going to have to pay a total of 10.5 percent, but the U.S. is getting the 5.5 percent difference. And so, the U.S. is essentially creating an incentive both for the country that has a 5 percent rate to increase their rate, and

for the subsidiaries that are moving to that low tax jurisdiction to stay in the U.S. because they're going to have to pay some amount anyway.

So, those are sort of the background to the work that led to this global tax agreement. So, after all of these unilateral developments, after the BEPS Project, after the 2017 tax reform, then the G20 and the OECD started to expand the countries that were involved in the global tax work. So, during the BEPS Project, 44 countries, all of the members of the OECD, plus any G20 countries that were not members of the OECD ended up working on all of the tax reform -- all of the tax reform proposals under the BEPS project.

Now, we have 141 countries that are sitting at the table in these meetings about tax reform. And how did that happen? Well, the G20 and OECD created what they call the inclusive framework. And more and more countries started to join. There were certain requirements to join, but the idea of signing on to these requirements was that you got a voice in the global tax reform debates. And as the inclusive framework grew, there was also growing consensus over the past several years over the idea of having two pillars.

And these two pillars are the ones I mentioned at the start. And in October of 2021, 136 countries agreed to these two pillars. So, we went from 2015, where the task force on the digital economy essentially issued a publication saying we can't agree on how to solve the digital economy. We can't even agree on what the digital economy is. To 2021, when the task force on the digital economy had almost 100 more countries and 136 of those countries agreed to these two pillars.

So, what are these two pillars? Well, so, Pillar One is this new nexus rule based on sales instead of physical presence. So, remember that in the earlier discussions, I've mentioned that physical presence is what's required in our tax system for income to be allocated to a country. But now we have a new connection based on sales that allows a marketing jurisdiction to get a portion of a company's income allocated to it. Now, this

doesn't completely change our existing profit allocation rules. We still have normal transfer pricing rules. This has not changed our transfer pricing system. Routine profits are allocated according to existing transfer pricing rules.

But Amount A is this -- a new amount that's created by Pillar One. And it's a percentage of what is a deemed residual profit, okay? So, there's a clear percentage that is calculated, that is allocated to market jurisdictions using a new nexus rule and a formula. And Pillar One only applies right now to multinationals with global turnover above €20 billion and profitability above 10 percent. So, the amount that's -- so, this is a very small number of companies who are going to subject to this. But they're the most profitable companies with the most revenue, right? They're the highest revenue companies and they're the most profitable.

Along with this -- I'm not going to talk much about this, but others can talk about it -- along with this there's also Amount B. So, Amount B focuses on baseline marketing and distribution functions. The idea is that there are two types of jurisdictions that are being excluded from our current system that focuses on physical presence. And those are marketing jurisdictions, but they're also distributional jurisdictions. The jurisdictions that are involved in distributing. And so, Amount B would focus on more on that.

So, the other important thing to note about Pillar One is that in the Pillar One agreement, there's an agreement that countries that have digital services taxes and similar measures will eliminate them. So, one of the big critiques over the last few years has been that countries have been implementing these unprecedented digital services taxes that are subjecting tech companies, primarily U.S. tech companies, but tech companies to taxation in an unprecedented way. And the countries are agreeing that they will eliminate their digital services taxes in exchange for Pillar One.

Pillar Two is very different from Pillar One. Pillar Two is a global minimum

tax of 15 percent. And this applies to multinationals with consolidated revenue of greater than or equal to €750 million. I will point out, countries can choose to apply it to others, right? But this is, the sort of idea of this, is that this is the scope of it.

Let me just pause for a second on what it means to have a global minimum tax of 15 percent. A lot of news articles have written that 136 countries agreed to change their corporate income tax rate to 15 percent. That's not what this is, right? This is not a tax rate. This is not a 15 percent tax rate. This is, instead, a top-up tax very similar to what I described when I talked about GILTI. This says a country that imposes a Pillar Two minimum tax will require the subsidiaries of its parented multinational, so the multinationals parented in that country, will be required to have their subsidiaries pay a top-up tax for the difference between the amount they pay to a foreign jurisdiction and 15 percent, right? That's not everyone changing their tax rate to 15 percent. That's, instead, a top-up tax that applies to subsidiaries that are working in low-tax jurisdictions.

This Pillar Two is broken into a few parts. I'm going to focus mainly on what's called the IIR, which is the income inclusion rule. That's what I've been talking about as a top-up tax. The UTPR is another portion, which essentially says if there's a payment made from one jurisdiction to a jurisdiction with a rate below 15 percent, there's going to be treatment in the payment jurisdiction that's going to disallow beneficial treatment like deductions if there's not a 15 percent rate on the other side. So, it's a way of -- it's a secondary rule that's a way of encouraging other jurisdictions to keep their rates at 15 percent, even if they're not the jurisdictions where there's the subsidiary being paid.

There's also discussion of a subject to tax rule that would be put into model trees, which has a different rate but which has a similar concept. There are also various carve-outs here. So, there's a de minimis carve-out and there's a substance-based carve-out, which is based on payroll and investment in a foreign country.

So, one thing I didn't mention about the U.S. tax reform is that our GILTI currently has its own carve-out for 10 percent of your investment in a foreign country. This is similar in concept in that you don't pay the minimum tax if you have sufficient investment in the foreign country. But it's not just sufficient investment in tangible assets. It's sufficient investment in payroll and in tangible assets. So, the more employees you pay in that foreign jurisdiction where your subsidiary is, the more investment that you do in that foreign jurisdiction, the less of the minimum tax that you will end up paying.

So, where are we? The use of Pillar One and Pillar Two, as I said, there's agreement, right? So, on July 1, 2021, 130 of the then 139 countries of the inclusive framework agreed to this in concept. Then 136 countries ended up agreeing in October. In November, one more country joined. Mauritania joined. So, Mauritania brought us up to 137 agreeing countries and 141. You'll note there's a different between 137 and 141.

So, who are the holdouts? Well, interestingly, they're not the same holdouts that you had in July. So, in July, the holdouts included Estonia, Hungary, and Ireland. They ended up agreeing for reasons that we can talk about in the Q&A. But they ended up changing their role, which is important to the European Union because the European Union needed the member states of the European Union to agree to this together in order for it to be possible for there to be a directive.

But the remaining holdouts that we have right now are Kenya, Nigeria, Pakistan, and Sri Lanka. And there have been some statements from some of these countries about some of their reasons for being holdouts. And one of their reasons is that Pillar One has two exclusions. Pillar One, you'll remember, reallocates income to countries that previously might not have been able to have access to that income. And Pillar One has an exclusion for regulated financial services. But it also has an exclusion for extracted industries. And so, some of these countries have come out and said that those exclusions

mean that they wouldn't get the benefit of Pillar One that they were hoping to get from signing on to that.

So, agreement, this is a huge step, right? In terms of how important this is, if you had asked anybody in 2015 if we would have 137 countries agreeing to the concept of a minimum tax, agreeing to a multilateral convention that was going to reallocate certain income to market jurisdictions, that would have seemed completely impossible. So, the fact that we're having this discussion is a huge step.

I am, however, going to raise some questions, which is why I have this next slide, which is agreement with a question mark. So, let's just talk about what it means to agree. So, 137 countries have agreed to an agreement about Pillar One and Pillar Two. What exactly have they agreed to? So, most of these dates that I put here come from the OECD's own publications. And some people will criticize whether or not these dates will actually happen. This is what the OECD is predicting.

So, what has been agreed to? What's the OECD stated? Well, first, Pillar One is going to be implemented in a multilateral convention. This multilateral convention is going to be developed and opened for signature in 2022. And Amount A is going to come into effect in 2023. That still raises a lot of questions. It raises questions about the specific details that will be in the multilateral convention. And it raises questions about who will sign on to the convention. And even if countries sign on, who will ratify the convention, right? So, that's why I have this question mark about agreement.

Pillar Two is actually, I would argue, even more interesting because Pillar Two is not actually required for any countries. Pillar Two is what's referred to as a common approach. And so, the OECD very explicitly says no country needs to have a minimum tax. But if a country has a minimum tax, it must be consistent with Pillar Two. Who has a minimum tax? The United States has a minimum tax, right? Other countries don't have a

minimum tax yet.

So, the big question is who's actually going to adopt a minimum tax? Now, it seems as if the European Union member states are on track to implement minimum taxes because they're in the process of discussing a directive. There's a little bit of back and forth about that that's going on right now. But this is a big open question. Pillar Two is not required. Again, despite all of the newspaper articles about a 15 percent rate, right? Countries have agreed to the concept of a minimum tax and they've agreed to the constraints of Pillar Two if they do adopt a minimum tax.

What the OECD has said is that this will be brought into law in 2022. It will be effective in 2023. And the UTPR -- remember that's the under-tax payment rule -- will come into effect in 2024.

So, let me just end by talking about some outstanding issues and then I look forward to discussing this more. So, the OECD has been producing consultation documents and model rules at an extremely impressive pace. And so, the OECD has been asking for questions about who -- let me actually skip the Pillar One for a second -- about who is actually -- how these rules will actually work and sort of who thinks that these should be designed differently.

So, some of the consultation documents that have come out recently have been about draft model rules for nexus and revenue sourcing. So, how do you even define Amount A, right? Or draft model rules for tax-based determination? Draft model rules for the scope? And there's been a consultation document about the extractives exclusion, or there's been a request for comment on that. And then for Pillar Two, the OECD has issued an implementation framework of the global minimum tax. So, the OECD is very aware that there's still a lot of work to be done and they're getting a lot of public consultation about that.

Where do I think that there are a lot of questions? Well, Pillar One -- I've

already raised this -- which countries will refuse to sign on to the MLC? Will it be only the four holdouts? Will it not be the four holdouts? Will it be other countries? Will it depend on what happens in these model rules that the OECD is consulting on? What if countries sign on and don't ratify it? Is there a country that we can imagine that might have problems ratifying treaties right now? Will countries be allowed to keep withholding taxes and other rules that are not DSTs?

So, this I actually think is an important question. When Pillar One refers to DSTs and similar rules, there's a question about how broadly it's defining it, right? I define similar rules very broadly. I include things like diverted profits test on taxes. I include things like multinational anti-avoidance rules. I include things like withholding taxes. Will all of those be eliminated or only some of them?

For Pillar Two, since this isn't required, who will implement this? Will GILTI be found consistent? This is a big U.S. question. And how will the EU's Pillar Two directive affect implementation?

So, again, I think this is a huge step. It's an incredibly exciting place to be to have all these countries who have worked on this and to have these two different types of rules that sort of hadn't existed a few years ago. And I look forward to hearing discussions and questions about all of these and where we're going with this. So, thank you all again for including me.

MR. WESSEL: Thank you very much, Lily. That was very complete. Let me ask you one question if you can answer it briefly, and then we'll move to Thornton's panel. What does Congress have to do here and do you think they'll do it?

MS. FAULHABER: So, this is a big question, right? So, one question -- and I'm not a tax treaty person and I know that there are experts, that there are people who are watching us who are tax treaty people, or I'm not a sort of constitutional treaty person. So,

the one big question is does this have to be ratified as a treaty, right? Is there a way that Pillar One at the multilateral convention can be treated as an executive order of some sort or can it escape the need for ratification? If it can escape the need for ratification, that's a huge problem, right? The idea that we need to have the super majority of Congress necessary for ratifying treaties.

Whenever I speak before international audiences about taxation, I have people in the audience who highlight the tax treaties that haven't been ratified for a long time, right? So, that's the first, you know, that's the big issue for Pillar One. Sort of built into that question is, are there things in the Pillar One rules that could make Congress more or less likely to sign on to a Pillar One multilateral convention either as an executive order of some sort or fully ratifying it, right? So, what is Congress demanding? Currently, Congress seems to be sort of writing angry letters about the fact that this -- that, you know, the executive branch negotiated this. But that's what they did for the BEPS Project too. And then, honestly, they ended up implementing most of the BEPS Project in domestic law. So, Congress can surprise you by being willing to accept things that they previously said were unacceptable multilateral or international agreements.

On the Pillar Two question, I think this really depends on how willing the OECD is to accept GILTI as it is and as being consistent with Pillar Two, right? So, the OECD is very aware of this. GILTI and its interaction with Pillar Two have been included in documents from the OECD for years now. They know that they have to work with the U.S. to figure out how to make it so that the U.S. can change GILTI in a way that Congress will be willing to change it. I mean, the Biden administration has proposed changes to GILTI that haven't come into effect because Congress hasn't passed the laws.

But, you know, Congress has to be willing to make some changes. Currently, our tax rate for GILTI is 10.5 percent, with a plan to go up to just over 13 percent.

That's not 15 percent, right? What Ireland got in order to stop being a holdout was that GILTI is exactly 15 percent. It's not higher, but it's also not lower.

MR. WESSEL: Thanks. Okay.

MS. FAULHABER: Thank you.

MR. WESSEL: Let me turn the virtual podium -- that was really clear, Lily, and I really appreciate that.

MS. FAULHABER: Thanks.

MR. WESSEL: There were a lot of acronyms, but you did do a good job of defining them. So, thanks for that.

MS. FAULHABER: I mean, you hadn't warned me that I couldn't use acronyms. I would have changed it. Thank you.

MR. WESSEL: Let me turn this over to Thornton Matheson, my colleague from the Urban-Brookings Tax Policy Center.

MS. MATHESON: Thank you, David. And thank you, Lily, for that great and very thorough wrap up. So, welcome to the panel discussion section of today's event. I'm Thornton Matheson, Senior Fellow at the Urban-Brookings Tax Policy Center, and I'll be serving as the moderator.

I am honored to introduce today's expert panel to discuss how BEPS Pillars One and Two could affect different groups of countries and also multinational corporations. So, let me briefly introduce our panel members. Dhammika Dharmapala is the Paul H. and Theo Leffmann Professor at the University of Chicago Law School. Dhammika will be looking at the effect of BEPS 2.0, which is another way of saying Pillars One and Two, on developed countries, including tax havens. And Alex Klemm is the Division Chief at the IMF Fiscal Affairs Department Tax Policy Division. Alex will be considering the effect of BEPS 2.0 on developing countries. And last but not least, Pamela Olson is Senior Policy Advisor

at PricewaterhouseCoopers and as David remarked, a former Assistant Secretary at the U.S. Treasury. And Pam will be discussing how BEPS 2.0 will affect multinational corporations.

So, to begin with, each of our panelists has prepared some brief opening remarks on their assigned topics. And after that, we'll open it up to Q&A with audience input. So, Pam, please, we'd like to start with you.

MS. OLSON: Good morning. Thank you. It's great to be with all of you. You know, so, first, I'll note that companies certainly respond to incentives. And so, to the extent that BEPS 2.0 alters economic incentives or disincentives then, you know, we can certainly expect companies to respond. And we can see a lot of evidence about how companies respond from how companies responded to BEPS 1.0, which was just described by Lily, as well as TCJA. Sorry for all the acronyms. But you just heard Lily define them all.

So, companies did, indeed, respond to BEPS 1.0 and I think they're still responding. And there have been a lot of studies about the impact of BEPS 1.0, as well as the impact of the TCJA. But most of those studies rely on data that's not particularly relevant to how companies responded to both of those items because they're too -- the data is too old, too much predates. In some cases, the data goes back to 2016 or 2017, and that was after BEPS 1.0 had been agreed to, but before countries had really started implementing the changes to it.

Just, you know, as a note, some of the BEPS 1.0, the most substantive changes, countries had a five-year period to implement the changes. And so, we really need to look at data from say 2020 or, you know, going forward, 2021, to really understand how BEPS 1.0 and TCJA affected companies' behavior. But we can certainly see that there have been a lot of changes in countries to their laws. There have been changes in company structure. There's been a lot of IP that has been brought to the United States as a result of

the changes.

And, you know, the BEPS 1.0 changes were a lot of substantive changes. TCJA was as well. Lily described the rate reduction as the U.S.'s competition. I would say it was more the U.S. bringing its tax rate into line with the rest of the world. And because it had been such an outlier, it was a distorter of investment decisions, particularly when you take into account the worldwide system with the, you know, sometimes called lockout effect. The fact that companies didn't pay tax on those foreign earnings until they reinvested them in the U.S. And so, that had the effect of making companies decide to leave the earnings offshore or reinvest them outside of the U.S. because they didn't have to pay the much higher U.S. rate.

Another thing I want to put on the table that I think has to be taken into account as we consider what the impact of BEPS 2.0 might be on companies, is that there have been societal changes that I think have affected, you know, how companies conduct themselves. Some of that's, you know, captured in the corporate social responsibility or sometimes called stakeholder capitalism kinds of things that have affected a company's decision making.

A second thing is just there's a lot more transparency. And that transparency goes to corporate social responsibility, but it also goes to tax. And companies have been doing a lot to think about their tax footprint, their global tax footprint, if you will, and to share more information about what they're doing on the tax side with respect to transparency.

And then, finally, we've got a lot of unanswered questions out there on BEPS 2.0. As Lily said, we have agreement, but, you know, agreement explanation point, agreement question mark. A really good way to put it. So, you know, questions, will governments actually implement? How will they implement? How will they administer it?

This is an extraordinarily complex idea and when you get into the details of it, it's even more complex than what, you know, Lily laid out. Just, you know, like -- and there are surprises that keep coming up. And Lily talked about the under-tax payment rule. If it were an under-tax payment rule, it would probably work something like the U.S.'s BEAT does. It's not. It's become the under-tax profits rule and is explicitly labeled that now by some countries that are looking at implementation.

We also have questions about whether governments will cooperate, whether they'll coordinate. And I would say on that that the initial signs are, you know, iffy. They've cooperated and coordinated to get to this agreement, but there's a lot of very important details that have to be worked out as we look at how governments coordinate tax systems. And those issues are, to my mind, they don't bode well. One of the big ones is, you know, what do we do with dispute resolution? This is going to put every country's fingers, potentially, in other countries' tax bases. There's got to be some coordination and cooperation. But we're having a hard time getting there.

And then the last unanswered question, I think is a really important one, is, you know, will companies actually change the incentives? Or will they simply move them around? So, does this end tax competition? Or does it just shift tax competition out of tax and into other things? And if you think about some of the things that are explicitly permitted under the agreement, you know, if your tax credits are refundable, that's okay. If you can do things through grants, et cetera. So, does it actually, you know, end the competition or does it merely shift it?

MS. MATHESON: Thank you so much. Now, we'll move on to Dhammika.

MR. DHARMAPALA: Thank you very much, Thornton. So, my remarks will focus mostly on Pillar Two. And I'll try to address very briefly these two distinct issues of profit shifting and tax competition for real economic activity.

First, there's general agreement, I believe, that if Pillar Two is implemented, there will be a reduction in profit shifting to haven jurisdictions. There is some disagreement as to the magnitude of the change. And that is because there is disagreement among empirical scholars about how much profit shifting there is under the current system. But nonetheless, the direction of change under Pillar Two is very clear. Essentially, a zero-tax jurisdiction. Whereas today, a zero-tax jurisdiction would be transformed through the implementation of Pillar Two into, effectively, a 15 percent jurisdiction for in scope multinationals. Those multinationals that satisfy these criteria that Lily described.

However, it is less clear what will happen to tax competition for real economic activity among large high-income, non-haven economies. Bear in mind that the phenomenon of tax competition is quite distinct from profit shifting. And, indeed, in most circumstances, it might be expected to be inversely related to the extent of profit shifting. So, to just clarify this point, imagine a world with three countries. United States with a 21 percent tax rate, another large economy that we'll call Ruritania, and something that is not the 142nd member of the inclusive framework. It's a fictitious country, but suppose it has a 25 percent tax rate. And there's also a zero-tax jurisdiction.

Under the current dispensation, the difference between the tax rates of the United States and Ruritania is not that important from the perspective of a firm that's choosing where to locate its real activity. Some of the income generated in the U.S. and some of the income generated in Ruritania can be shifted to the haven attenuating the tax rate difference, the impact of tax rate differences among these large non-haven economies.

Suppose now that Pillar Two is implemented and that it eliminates profit shifting to the haven, then the difference in tax rates between the United States and Ruritania now becomes rather more consequential. And this implies either greater distortion to the location of real economic activity, or greater incentives for tax competition between the

United States and Ruritania to attract real investment, or some combination of the two.

I would also note that Pillar Two substance-based income exclusion or a substance-based carve-out that was mentioned by Lily, plays a significant role in preserving incentives for tax competition for countries with rates below 15 percent. There's also the issue of alternative forms of competition through subsidies that Pam mentioned. Ultimately, the effect on tax competition among higher tax rate countries, countries with rates above 15 percent, is ultimately ambiguous. But whether or not the new regime intensifies tax competition for real activity or not, it is possible that tax competition may become more harmful in terms of economic efficiency because it may potentially distort the location of real economic activity to a greater extent than would occur when profit shifting is possible.

And there's a little bit of irony, I think, here because as Lily mentioned, one of the motivations for the BEPS Project was this concern about tax competition. Ultimately, while Pillar Two will -- can reasonably be expected to reduce or eliminate profit shifting to havens, it is, however, much less clear what will happen to tax competition for real economic activity among high income, non-haven countries. So, let me stop there.

MS. MATHESON: Thank you very much. And finally, Alex.

MR. KLEMM: Thank you very much, Thornton. So, I will turn to developing countries and how BEPS 2.0 affects them. So, first, I'll give you the correct answer, which is it all depends, and each country is different. And, of course, that's the completely correct answer but it's not very interesting. So, now I will generalize a little bit to get to some more insights.

First, I'd like to remind everybody what the situation is in developing countries regarding corporate income tax rates. So, many of these countries, if we are not talking low tax jurisdictions, but about normal developing countries, they actually tend to have relatively high corporate income tax rates and corporate income tax revenues are also

quite important for their revenues.

But what has happened over the decades is that they have developed a parallel tax system where they use tax incentives or special economic zones and the like to bring tax rates down. So, they have two systems. One with high rates and one with rates close to zero. Some of them have attempted to coordinate. But it's really hard to agree on that because every time a couple of countries coordinate, the incentives for the other are to not participate in that because then they become even more attractive as a place to locate profits and capital.

And the other thing that has been a problem for some of these countries is that the global tax system is hugely complicated. We have extremely complex transfer pricing rules that are difficult to enforce in the most advanced countries as well. But for developing countries, it's a major difficulty. And then there are complicated treaties, which can sometimes be abused. So, that's the starting position.

And now, Pillar Two comes. How does it change it? And I think the fundamental thing that changes is that the income inclusion rule, which is kind of the output minimum tax it acts like an enforcement mechanism. Suddenly, you don't need, among developing countries, everybody to agree to cooperate and decide on having some minimum tax rate because now they know that as long as all the major capital exporters apply this income inclusion rule, multinationals within their borders will have to pay a minimum tax of 15 percent, so, now they can costlessly reap the revenue themselves because it will not add to the cost to pay for multinational companies.

And one really important aspect of the Pillar Two, I think, is something that came in quite surprisingly to some of us around December in the model rules, which is -- and, sorry, that's another acronym, the QDMT, the qualified domestic minimum top-up tax, which basically, allows each source country, including each developing country, to

implement a minimum tax domestically using exactly the same criteria as used under the income inclusion rule that Lilian described earlier. So, they can, in a way, make sure that they reap the revenues from this and it will not be paid at home where headquarters of multinationals are located.

And then because of a twist of how this is calculated, actually, this is the safest route for developing counties to implement this minimum tax. It is safer for them than doing it by increasing their standard tax rate. Now, explaining exactly why this quirk happens would take too much time here. It's something about the order with which you calculate the effective tax rate and then the top-up rate. But it's safe to remember that this will ensure that the revenues are collected at source. So, this is really a game changer. It might reduce the incentive to reform tax systems, but still countries will get a revenue gain. I still would hope that countries use the lower overall tax competition pressure to look at some of the features of their tax system, which might not be particularly effective, especially some of the incentives.

One difficulty some countries might encounter is stabilization agreements, which they have signed with many multinationals. So, that might prevent them from imposing such a qualified domestic minimum top-up tax. It's an interesting question whether they can then renegotiate those on the grounds that companies will have to pay this anyway. They have to pay it at home under the income inclusion rule. And the country of residence of the multinational, they will not be bound by any locally signed stabilization agreement. So, they should not really care about paying this tax. But legally, they are not obliged to. So, this could lead to an interesting question.

One thing, though, to address. I mentioned before the complexity that creates problems for developing countries. That is one aspect that is not improving. So, the world is becoming more complex. Understanding this should have been clear from the

presentation in the beginning, it's hugely complicated even at the abstract level. And once you go down to the laws, it becomes hugely complicated.

I think I've run out of time. So, I will skip over the effect of Pillar One, which is fine because I think it will have much fewer effects. Just to end with the idea that we should not expect miracles. Developing countries have major revenue needs, even if this reform turns out to be a fantastic one that raises more revenues, it will not be enough for them. And they will have to keep doing domestic revenue mobilization efforts to be able to address all of their needs. Thank you.

MS. MATHESON: Thank you so much for all of your opening remarks. The question I get most often, including from today's audience, with regard to both Pillar One and Pillar Two, is is this going to happen? And if so, when? And I invariably punt and say, well, I'm an economist, not a political pundit, so, what else do you want to know?

And, fortunately, we have Lily Batchelder at the end to talk more about the political prospects of Pillars One and Two. But I would like to ask sort of a related question, which is about incentives. And we'll start with Pillar One. As you can tell from the panelists' opening remarks, there is, you know, kind of a preoccupation with Pillar Two. But I want to make sure we look at both.

So, starting with Pillar One, and we'll start with Dhammika, what are the most important incentives for high income countries to ratify Pillar One? And what are their major concerns about doing so?

MR. DHARMAPALA: So, one point I should make at the outset, is, you know, echoes something Alex said just a little bit ago, which is that Pillar One's impacts are likely to be considerably small. The IMF has produced a fiscal -- it's recent fiscal monitor estimating the revenue effects of Pillar One and Pillar Two, among other things. And its actual impact is likely -- the impact of Pillar Two is much more substantial, but the impact of

Pillar One is quite small.

And one can think of Pillar One as a kind of exchange of existing DST and related provisions for Pillar One, right? And therefore, from the point of view of a high-income country that has enacted a DST, or a digital services tax, its incentive to sign on to Pillar One is essentially I would see as being fairly modest but not negligible. It essentially it exchanges the revenues that it would have got from the DST for revenues from Pillar One. But in both instances, right, both DSTs and Pillar One, the revenue at stake is very modest.

And in addition, I suppose an incentive is that one gets to be part of this multilateral -- one gets to be part of this multilateral system initiative and you can stop getting criticized for imposing DSTs by various people in the tax world. But in terms of revenue and efficiency affects, I think the costs and benefits are fairly small. So, I would imagine that a big motivation is just being part of the wider multilateral process.

MS. MATHESON: Okay, great.

MR. KLEMM: Can I add something to that?

MS. MATHESON: Alex, well, actually, go ahead and jump in, Alex.

MR. KLEMM: Okay.

MS. MATHESON: Because I was going to ask you the exact same question for developing countries, what are their incentives regarding around Pillar One?

MR. KLEMM: Okay. So, because my answer is the same thing that I wanted to actually say in reaction to Dhammika. First of all, I agree with everything that Dhammika said. But there's one more aspect that is really important about this is that Pillar One is, of course, mostly a redistribution of revenue, rather than a new effort of raising revenues. And from looking at what has been published so far, we have some idea of where Pillar One will be allocated because we have some idea of what the allocation formula will be like and what it will be based on.

But because it's not a replacement of the tax system, it's an addition to the tax system, somebody has to give a credit for the tax paid in other countries. And that is the part that has not been clear. I think at the beginning most people thought, oh, it's going to be the country where the headquarters is, which will give up most of their revenues. Then it was really easy where the developing countries mostly gain and the countries with the headquarters are mostly lose. But actually, it's not true and if we now look at it, we don't really know who will give the credit and how. So, we also don't really know who will be in revenue terms, gainers or losers. But I take Dhammika's point that there are issues beyond revenue that are really important in order to be there. Thanks.

MS. MATHESON: So, I'm glad you brought that up because I had a separate question about that. It seems pretty clear that Pillar One, we know how the revenue would be allocated. It would be allocated on the basis of sales, but where does it come from? And that seems more debatable. Certainly, not all of the largest multinationals are reporting 100 percent of their income in their home countries. So, I'm glad you raised that issue.

So, Pam, I'm going to ask you a slightly different question. If Pillar One is enacted, it would be the first instance of a destination or a sales-based formulary apportionment at the international level. We have some of this already at subnational levels in the U.S. and Canada where there's some kind of formulary apportionment of revenue among jurisdictions, often heavily sales based.

And as Lily Faulhaber pointed out, Pillar One would apply only to the world's largest corporations. So, what are those corporations' main concerns about Pillar One? And how could they potentially react if it's enacted?

MS. OLSON: Well, that's a really good question and I think the answer is completely unknown because we still are missing so many details. You know, to the extent

that it replaces the DSTs, it does in fact, get rid of the unilateral measures, you know, that's good news for a fair number of companies. And, you know, I think it's important to look at the fact that the revenue cutoff of €20 billion is the starting point. And the expectation is that at some point down the road if this is successfully implemented, then it's expanded so that the revenue threshold drops and more companies become subject to it.

But until we know things like the surrender jurisdiction as it's called, the question that Alex was just referring to, it's difficult to say what the impact is going to be. You know, I think that there were a fair number of industries that would have been happy to have had a -- I'm sorry, there's a phone going off in the background here. A fair number of companies that would have been happy to have had the DBCFT, the destination based cashflow tax that was considered leading up to the 2017 Tax Cuts and Jobs Act. They would have found that kind of a division of profits preferable while others would have been adamantly opposed to it.

So, you know, the surprising thing about Pillar One as it's come out in the last year is the fact that it applies much more broadly, not just to the high-tech companies, but that it picks up high profit -- large high profit companies from around the globe. And I think it's really to be seen how the rules come out before we know how it's going to affect how and where it changes how companies operate.

MS. MATHESON: Okay, great. Well, we may come back to Pillar One at the end. But since our time is limited, I wanted to make sure that we cover both pillars. So, I want to move on to Pillar Two. And ask similar types of questions. So, again, we'll start with Dhammika. And if you could talk about what are the economic incentives for developed countries, most of which have significant outbound investment to adopt Pillar Two? And how much do those incentives depend upon what other countries do? So, especially, you know, other developed countries adopting Pillar Two themselves.

MR. DHARMAPALA: So, one way to think about this is many of the high-income developed countries that have substantial outbound investment already have CFC rules. I'm sorry, that's an acronym. It's controlled foreign corporation rules. And what those do is to impose a kind of top-up tax on passive income earned in low tax jurisdictions, meaning, you know, income from holding financial assets rather than from real business activity.

And so, this concept isn't entirely foreign. So, Pillar Two extends it to active business income and makes and kind of extends it in various directions, but countries already have these controlled foreign corporation rules. And one can view them though as having -- one view would be that they're trapped in a kind of prisoner's dilemma situation where if all countries adopt something like Pillar Two, they would all be better off. But no one has an incentive to do it unilaterally. Although as it happens, the U.S. did something not very different, you know, unilaterally through the GILTI system.

So, I do think that -- so the revenue with this new QDMTT, the qualified domestic minimum top-up tax that Alex mentioned earlier, the revenue incentives to adopt Pillar Two are really not as powerful as they might otherwise be. It's not that if you're Ruritania and you're taxing Ruritanian resident multinationals on their income in a low tax foreign jurisdiction, the low tax foreign jurisdiction is certainly going to increase its tax rate for in scope multinationals. So, that revenue incentive is not very powerful. And that's another factor that must be considered, you know, when thinking about this.

But countries have other reasons for doing this. There is this sort of general public sentiment that multinationals pay too little tax. And rightly or wrongly that sentiment exists and political leaders will respond to it. So, I think, you know, the fact that so many countries have already agreed to this is revealing, I think, of the wider forces at play. But I think it's not going to primarily about revenue for the reasons I described.

MS. MATHESON: Okay. Thank you. So, Alex, similar question for developing countries where the major obvious difference is most of them are predominantly capital importers. So, their host countries are receiving investment from more developed countries. What are their major incentives or disincentives to join Pillar Two? And if Pillar Two adoption among advanced countries is patchy, how does that affect those incentives?

MR. KLEMM: Thank you, Thornton. I think that last part of the question really is the key. If we get full -- or not full, but really widespread adoption of Pillar Two rules along advanced countries or among capital exporters, then it is so easy to see what happens in developing countries. They have a very strong incentive to adopt at least a qualified domestic minimum tax so that they reap any revenue gain.

But if it's patchy, we are really in a different world because depending on where the investment comes from that takes place in their territories, it may still be really hit by a domestic minimum tax. So, such countries where the investment does not come predominantly from the U.S. whereas we have discussed there is already something similar in place, but maybe from other jurisdictions, they would have incentive to be really cautious about adopting a minimum tax or about any other tax increase. So, I think their main incentive is to wait and see and to adopt Pillar Two rules only once they are certain that maybe not all, but a large group of advanced economies have legislated their implementation.

And just another very minor additional thought, I think the key really is the qualified domestic minimum tax for developing countries. For them to adopt the whole rest of rules, it might be good, but it's not going to be such a major thing. And it's also not something we should worry about because if there is a large enough group that has this income inclusion rule and call it under tax profit rule, we should be certain that the incentives globally are well aligned so that most countries would implement that minimum taxation.

MS. MATHESON: Thank you. So, and then finally, Pam, we've seen that corporations have been highly adept at arbitraging the prevailing source-based or territorial global tax system, meaning that, you know, under the -- with the exception of the U.S. GILTI regime, currently companies are basically taxed in the jurisdiction where they are operating. They're subject to domestic tax regimes throughout the world and they're not subject to a worldwide tax in their country of residence on their foreign income. But that would change under Pillar Two, which would move to a residence-based or a worldwide system that would greatly reduce, potentially, international tax rate differentials that that arbitrage has been based on. So, if Pillar Two were widely adopted, how would you expect multinational corporations to respond?

MS. OLSON: Well, it'll certainly require them to reconsider all of the operational structures that they have in place now and the planning that they've done in the past to minimize taxes. And one of the concerns that I have about Pillar Two is that I don't think that there's been sufficient detail to the likelihood of double taxation from a number of these provisions. So, you know, BEPS 1.0 was said to be about eliminating double non-taxation. In the past, you know, the goal has always been to make sure that there wasn't double taxation because the double taxation resulted in an impediment to investment and trade, which, you know, betters lives of both ends of the trade and investment side of things.

But so, the companies will certainly have to reconsider. There's just an unbelievable amount of complexity in these rules. You know, when you think about things like the global -- our system, GILTI, we base that on tax rules. The income inclusion rule is going to be based on financial statements. And so, just that difference alone means that companies have to evaluate on the basis of two different sets of books.

And when you look at how those rules interact right now, you know, one of the things that a lot of companies and tax advisors looking at this have seen is that you can't

look at it and say, well, all of my income is subject to tax at, you know, 21 percent, to pick the U.S. rate. I'm paying at least that rate around the globe and, therefore, I don't need to worry about this. When you factor in the financial statement treatment and then the restrictions on use of the tax that has been paid or that is expected to be paid, you can end up with a rate much higher, notwithstanding that. So, you know, those are all things that companies will be taking into account and trying their best to structure their affairs so that they end up with reasonable tax results.

MS. MATHESON: Great. Dhammika, I wanted to make sure that we talked a little bit about tax havens. That is, you know, countries with very low or zero effective rates on corporate tax. If Pillar Two were widely adopted, what would be the impact on tax havens? And how would you expect them to adapt both in terms of their -- certainly in terms of their tax policies, but possibly, also in terms of their sort of overall business plan?

MR. DHARMAPALA: Right. So, I think first we need to distinguish between two different kinds of jurisdictions that people refer to as havens. One, extremely small jurisdictions with zero tax rates where there is little real activity and where there's little possibility of real activity given the small size of the geographical size of the jurisdiction. And then there are larger countries that have low tax rates that -- but also have some significant economic activity.

So, for the first type of country, the point is not to attract, you know, to attract tax base to generate tax revenue. That's not the point at all. The point is usually to generate fees from incorporations, and activity by in some cases, by accounting and law firms. So, that will obviously be -- that model will obviously be adversely affected. It remains to be seen whether profit shifting to those zero tax jurisdictions will be eliminated or simply reduced. If the latter, then there will be some continuing activity there. But as you say, you know, those types of havens are potentially adversely affected.

The other type of haven has a low but generally not zero tax rate and has significant real activity. And I think they are perhaps less affected because of the substance-based carve-out, which allows countries with say, you know, 10 percent tax rates to remain viable locations for significant activity. And, indeed, in a sense preserves their incentives to keep their tax rates where they are or even to lower them.

So, I would bifurcate the answer into those two different categories. And there is, obviously, a real question as to how widely Pillar Two will be implemented, of course. So, and that will matter as well.

MS. MATHESON: Great, thank you. Alex, you brought up the issue of developing countries tax incentives. And developing countries have used, you know, under the current system, where there's regular tax competition, developing countries have used a variety of devices such as accelerated appreciation, investment tax credits, reduced tax rates, or even complete tax holidays to try to lure investment capital from developed countries. And, of course, all of these devices lower your effective tax rate. So, they could trigger, you know, an income inclusion rule in the home country.

So, my question is, you know, if Pillar Two were widely adopted, how could -- could developing countries continue to use tax policy to attract investment? And if so, you know, what would be the most effective devices?

MR. KLEMM: Yes, thanks. So, the short answer is, yes, for various reasons. The one reason is that under the income inclusion rule, not every tax incentive is treated the same. So, where, for example, a zero rate or reduced tax rate, would be ignored. So, in the effective tax rate calculation, therefore, it would trigger an additional payment under the income inclusion rule.

There are other things that are accepted and certain refundable tax credits for R&D, and things like that, they are perfectly acceptable under the income inclusion rule.

And having them will not trigger an additional charge, even if they reduce your tax. So, countries could move into those that are more accepted under the income inclusion rule. That's one thing.

The other thing is that we have to remember this is all about corporate income tax. But countries have been using other things, even on the tax side, to attract companies. So, we have heard of countries not charging personal income tax on managers working for companies. There could be games being played with the VAT, although in case of exports, it doesn't matter. So, there might still be tax measures countries use and just like now, not all of these measures will be good. So, some of them actually will be just throwing away money for little return.

Yeah, and then, I mean, my hope would be that countries would also just move away from them and use non-tax measures to just make their countries more attractive as places for a location. But there is no guarantee that this is what will happen.

MS. MATHESON: Great, thank you. Pam, we have a question from David Wessel, who is asking about the impact of BEPS, both pillars, or either pillar, about a compliance cost for MNEs.

MS. OLSON: Well, they're going to go up considerably, I think. You know, again, you go back to, again, the factoring in of the different tax bases. You know, just if we look at the legislation that's currently pending in the U.S. Congress that's been passed by the House and we're waiting to see whether or not the Senate will take it up, but, you know, that has among other things, a new book minimum tax. And so, that brings in one level of complexity.

Then we move into what's going on globally and the changes to GILTI that are proposed as part of that legislation would move us from a global calculation to a country-by-country calculation. And moving to a country-by-country calculation, is very complicated.

You also have to factor in limits on foreign tax credits that are a part of our law. And so, you know, you end up with many more calculations that have to be done for a current year and then have to be carried forward.

And then if we factor in the adoption of some of these measures by other countries, and particularly if they're doing it on the same basis as Pillar Two proposes using financial statements rather than tax base, then companies will be using the tax bases in those countries to calculate their regular income tax but then also, recalculating all of this with respect to what they're going to owe for the income inclusion rule.

And then we layer on top of that the under-tax profit rule, which, you know, as Lily described it, it was about payments between jurisdictions, but you don't actually have to have a payment going between a jurisdiction in order to trigger the under-tax profits rule.

And so, that's another layer. And if there isn't agreement that GILTI either in its current form or as amended, constitutes a good income inclusion rule, then we're also going to have to add onto that that multinationals are going to have to look at the under-tax profits rule and how the under-tax profits rule applies to them. So, it's going to be an enormous increase in compliance.

MS. MATHESON: Thank you very much. Well, I could keep peppering you with questions all day long, but we are out of time. And need to move on to Lily Batchelder, who's going to tell us about those political prospects. So, thank you all very much.

MR. WESSEL: Thank you, Thornton, and thank you to the panelists. I'm very pleased that Lily Batchelder has been able to find some time to be with us today. She has a hectic job these days as you can see, a great office. Lily spent some time on the Hill working for the Senate Finance Committee. She spent some time in the Obama White House. And then she was at NYU Law School when the Treasury drafted her for the job of Assistant Secretary for Tax Policy, the one that Pam Olson once had. So, Lily has some

remarks and then we'll have time for a few questions afterwards. So, Lily, all yours.

MS. BATCHELDER: Thank you, David. Thanks for the kind introduction and for inviting me today. Brookings and the Tax Policy Center are such incredible resources for the tax policy community and I really admire both institutions ever since I started out in tax, which is now many years ago. So, it's really an honor to be here today. And I've also really enjoyed just a fascinating panel and introductory remarks and I'm also pleased to part of an event with another Lily. I want to thank you for the opportunity to explain why we at Treasury and, indeed, the entire administration are so committed to this project and what lies ahead.

So, the Global Tax Agreement is one of the biggest accomplishments of this administration to date. It would stabilize the international tax system and make it fairer to the benefit of U.S. workers and businesses. And really a remarkable testimony to multilateralism, 137 jurisdictions as has been discussed, have joined this agreement. A result which really wouldn't have been possible without the strong leadership of the U.S. and really, as was alluded to, would have been unimaginable just even five years ago.

These agreeing jurisdictions include all G20 and EU countries and represent nearly 95 percent of the world's GDP. Of course, more work does need to be done to implement the global deal. But before I get into that, which I'm sure will be of interest, I want to first highlight why this deal has been such a top priority of the administration.

So, let me start with the global minimum tax called Pillar Two as we've been discussing. Currently, the U.S. is the only country with a formal minimum tax on foreign earnings. The global minimum tax rate is zero. To be sure, some countries have anti-abuse regimes that limit profit shifting at the margins. But many of these regimes have been and are leaky and poorly coordinated.

So, what the global agreement does is set a floor so that multinational

corporations, whether they're headquartered in the U.S. or abroad, will pay taxes on their earnings in each jurisdiction in which they operate at at least 15 percent. That means that all 137 countries that are part of the agreement, have agreed to impose this country-by-country minimum tax on the foreign earnings of all multinationals that are resident in their country.

But that's not all. In a new step for international tax law, the agreement includes a strong enforcement mechanism, which has been discussed. And this ensures that countries honor this commitment while creating very strong incentives for non-signatory countries to join the conferencing framework.

Specifically, the enforcement rules allow agreeing countries to impose top-up taxes called UTPRs on companies operating in their jurisdiction if the corporate group's effective tax rate falls below the 15 percent minimum in any jurisdiction. So, essentially, if a country does not enact the country-by-country minimum tax on its resident multinationals, other countries will apply that minimum tax to those multinationals via their subsidiaries and soak up all the revenue that the non-implementing country could have collected.

These enforcement rules make the regime robust by creating strong incentives for adoption. No longer is it going to pay off to root earnings through daisy chain subsidiaries in search of the lowest tax rates. Instead, most countries will have a minimum tax and countries that do not, will be heavily incentivized to adopt one because of this enforcement rule I just mentioned, which would tax their multinationals' low tax profits anyways.

So, turning to the rationale, the fundamental reason why we see this global agreement as so critical is because it's essential to saving the corporate income tax. Over the past 40 years, nations have engaged in tax competition generating a race to the bottom in corporate tax rates. In particular, the OECD average corporate tax rate has declined from

40 percent 40 years ago to just 23 percent today. The global agreement would end this race to the bottom by largely eliminating the benefits from engaging in it.

And what's more, saving the corporate income tax is in turn, key to making sure that we can tax capital income. If we can't, we'd have to solely rely on taxes on workers and labor income. And at home, we've been seeing labor bear an increasing share of the tax burden in recent decades. We desperately need to reverse this trend. And that's why the President is focused so heavily on taxing wealth like work.

To be sure, there are a lot of different ways to accomplish this goal and Treasury and the administration have put forth multiple proposals for performing the taxation of capital. But shoring up the corporate income tax is a key component of that effort. It's a straightforward way to rebalance the tax system to more effectively tax capital and it's also one of the most progressive components of the federal tax system.

A further benefit of the agreement is that it would enable our government and others to raise more revenue and reduce taxes on workers and small businesses. The race to the bottom corporate tax rates has reduced government resources, which could be used to build infrastructure, to educate our citizens, to support R&D, or combat climate change. And unless we stop it, this general shortfall in corporate tax revenues is ultimately going to have to be picked up by someone, most likely workers and small businesses. That's why this deal is part of what it means to have a foreign policy for the middle class. It's ensuring that capital incorporations pay their fair share.

I think it's also important to note that the deal illustrates the benefits of reviving international economic multilateralism. By putting a floor on tax competition by large multinationals once and for all, it will help ensure we all have the resources we need to make investments that expand opportunities. It will enhance economic growth by creating a less distorted international tax system. And it's the kind of thing we can only do together and not

alone, which is why a multilateral solution is so essential.

I do also want to emphasize though that this is not a zero-sum game. Workers are going to benefit significantly because the deal will ensure that the owners of capital share fairly in the burden of financing government investments. But it will also bring significant benefits to U.S. businesses. As I mentioned, small businesses will benefit because they'll no longer face a competitive disadvantage relative to large multinationals that can shift profits on paper to low tax jurisdictions, while small businesses pay full U.S. rates.

But our large corporations will benefit too. They'll no longer be based in the only country that formally requires them to pay a minimum tax on their foreign earnings. And that level of playing field has been the single most frequent international tax policy request that the multinational community and the U.S. has made. The deal will enhance their competitiveness relative to foreign corporations along with all the other extraordinary benefits that U.S. residence, of course, offers. And it will help stop the offshoring of jobs and corporate inversions.

So, before I move on to Pillar One, I want to spend a moment on our domestic legislative agenda as it relates to Pillar Two. And in particular, I want to underscore the benefits of strengthening our current minimum tax system, called GILTI, even apart from the global deal.

Our current GILTI rules are poorly designed to combat profit shifting. They apply globally, not on a country-by-country basis. And that means that countries can blend income from high tax countries with income from low tax countries. What this effectively means is that the U.S. is often a last place, ironically, where a U.S. multinational would want to earn income because it's the only place where income does not offset high taxed or low taxed GILTI income earned elsewhere and because multinationals get a 50 percent rate cut

on foreign income.

The House-passed international reforms last fall would strengthen and reform GILTI and BEAT. Actually, I'm not sure we've discussed the BEAT acronym, but maybe I will delay that. And this includes applying GILTI on a per country basis. These reforms would align our law with the global deal and would fulfill our commitments under it. But just as importantly, they would dramatically reduce profit shifting incentives for both U.S. multinationals and foreign multinationals operating in the U.S. And these profit shifting incentives are really inefficiently inhibiting domestic productivity.

The BEAT reforms in that legislation would also serve as a major incentive for countries to adopt minimum taxes on the foreign earnings of their multinationals. And meanwhile, the revenue raised could be used to finance the transformative investments that I've discussed earlier.

You may have noticed, for those of you who perused our Green Book, that we have proposed a slightly different approach to addressing base erosion and enforcing the global minimum tax, also called a UTPR. The Treasury and administration fully support the BEAT reforms in the House-passed bill. And the UTPR proposal in the Green Book is really an alternative model for accomplishing the same objectives that raises even more revenue. Both the Green Book, UTPR proposal, and the House-based BEAT reforms would create powerful incentives for other countries to join and comply with the new global regime and both would further the goals of it.

So, shifting to Pillar One, it also has substantial benefits for U.S. businesses, including the largest ones, because it would stabilize a system that's frankly been upended. Over the last 15 years, the current system for allocating taxing rights has lost the support of foreign sovereigns. And in particular, it's ignored the realities of doing business in a modern world by demanding physical presence for taxing rights to be

triggered.

This outdated paradigm initially led to longstanding complaints by countries that are primarily market economies rather than headquarter jurisdictions. And then more recently, these objections were joined by complaints from high income countries, especially in Europe, that were frustrated by the ability of the so-called digital giants to escape taxes in their jurisdictions.

At the same time, political pressures abroad began creating a chaotic array of digital services taxes and other unilateral measures. And these taxes often discriminated against U.S. businesses. They threatened multiple layers of taxation and escalated trade-related -- tax-related trade tensions.

To make matters more complicated, these measures were also threatening to expand beyond the digital sector, as more sectors are, of course, digitizing and nations inherently get more creative. In response to this increasingly untenable situation, the prior administration acknowledged there was a problem with the current system for allocating international taxing rights. And they strongly and correctly emphasized that it was not limited to digital services. But they proposed a safe harbor approach to Pillar One, which would have essentially made it voluntary and that understandably was a non-starter for the rest of the world. So, when Secretary Yellen dropped that safe harbor demand last February, the negotiations restarted in earnest.

There have, of course, been many challenging issues along the way. The original proposal, which would have limited any reallocation of taxing rights to the digital tech companies was popular abroad, but it was conceptually indefensible, discriminated against U.S. businesses. And wasn't future proofed because the global economy is going to continue to digitize. There were other proposals, for example, to also include consumer facing businesses. But these, instead, introduced definitional problems that potentially

discriminated against U.S. businesses as well.

So, ultimately, we reached a compromise, again, supported by 137 countries that applies Pillar One reallocation to the largest and most profitable companies in almost all sectors. And Pillar One, as it now stands, would restabilize the system in a way that's sustainable and would put an end to unilateral discriminatory measures.

Importantly, Pillar One also protects U.S. interests. As one of the largest market economies in the world, we would benefit from Pillar One's partial reallocation of taxing rights to such jurisdictions. Our companies would also benefit from the increased tax certainty it would create because they no longer would face unilateral tax measures that threaten them with multiple layers of taxation. And no longer would they face the threat of escalating tariff retaliations and trade wars that are bad for U.S. business. Instead, under Pillar One, they'll be able to plan for the future and invest their capital based on economic and non-tax considerations.

So, finally, I want to turn to what's next. And I'd be ignoring the elephant in the room if I didn't acknowledge that there are important steps left for the global deal to become reality. Nations, of course, need to implement these rules.

Europe is strongly moving towards implementation of Pillar Two. Although they did not gain consensus on a draft directive this month, the French presidency is committed to doing so in the coming weeks. And Poland remains really the only outlier here. We're disappointed that they did not join the otherwise unified EU on this important measure that will, when implemented around the world, raise crucial new revenue for 137 participating countries. But we remain optimistic that in the coming weeks, Poland will no longer block unanimity in the EU.

In terms of the U.S., the past board has, of course, had many twists and turns. But we're confident that we will meet our commitment to reform GILTI and BEAT,

which remains a top priority for the administration. There's broad support across the Democratic Caucus for these international proposals, and we're optimistic that we'll meet our commitment to enact Pillar Two in 2022.

I also want to acknowledge that there's been a lot made in recent -- much has been made in recent weeks of the possibility that the agreement could curtail certain domestic tax incentives through UTPRs. Under the Pillar Two model rules and commentary, tax incentives do generally reduce a taxpayer's tax expense and thus their effective rate. And this general rule was necessary, given the goal of Pillar Two is to level the playing field for U.S. businesses and end the race to the bottom for corporate effective tax rates. So, if the deal just disregarded all tax incentives, it would render the minimum tax meaningless because any rate cut can be framed as a tax incentive.

But it's worth emphasizing that the number of U.S. taxpayers even potentially affected by UTPRs is incredibly small. The global agreement provides that the UTPR may only apply to the largest and most profitable multinationals, and only if they pay less than a 15 percent effective rate to each jurisdiction in which they operate. Only a 0.02 percent of U.S. corporations are above those thresholds. As a percentage of U.S. corporate returns, that's two in 10,000. And the share of all U.S. businesses affected is much small. So, this is emphatically not something that small or even reasonably large corporations will be affected by.

Moreover, the effect of UTPRs on tax credits depends on several factors, including who controls the projects that give rise to the credits and whether the credits are refundable. So, some of the credits that are being raised as concerns would almost certainly fall outside of the scope of UTPRs. And for those credits that do not, we're committed to working with Congress to explore other ways to protect U.S. tax incentives that promote U.S. jobs and investment.

After GILTI and BEAT reform, the U.S. will need to turn to the multilateral instrument for Pillar One. Important pieces of which are currently being negotiated and submitted for public consultation as they become ready. Although the business community is understandably reserving judgment until details of Pillar One become clear, we're confident that once the deal is brought to the implementation stage, the benefits to the U.S. fisc in U.S. businesses will be readily apparent.

Pillar One would restabilize the allocation of taxing rights in the international tax system in a way that would be sustainable and would put an end to the chaotic array of unilateral discriminatory measures that were proliferating and can result in multilayers of taxation. These measures currently only threaten certain sectors of the economy, but they're poised to apply more broadly potentially escalating tariff retaliations of trade wars. And certainty is, of course, invaluable to investors and business leaders and Pillar One would deliver on that.

So, to conclude, this is a generational achievement that would benefit not only working class and middle-class Americans, but also citizens around the world. Workers will find themselves in a position where they're no longer bearing a disproportionate share of the tax burden. Individuals and families will benefit from the revenues this deal raises to pay for important social goods like childcare, healthcare, climate protection, and education. And the race to the bottom that's bedeviled the tax system for decades, will be replaced with a different kind of race that asks who has the most productive workers, the strongest infrastructure, who has the most recreative R&D. And that's what I call a race to top. It's one that benefits citizens around the world, rather than depriving them of resources and investments.

And with that, I'd just like to thank you again, David. I know we've actually hit our time but would have otherwise been very happy to answer questions.

MR. WESSEL: Let me ask you to elaborate on one thing, if you would. So, what happens next? You said that you think you can get through Congress legislation this year that changes the provisions of the Tax Cut and Jobs Acts to comply with Pillar Two. Can you do Pillar One with an executive order? Is this a treaty? What's going to happen going forward?

MS. BATCHELDER: So, Pillar One, there are different approaches and it's hard to speak while it is still being negotiated. But the administration has consistently said that a Pillar One multilateral convention must be approved by Congress. So, we look forward to consulting with Congress as to the appropriate process to obtain such approval once it's ready for signature. And in the meantime, we're very actively consulting with Congress on the building blocks of Pillar One. A discussion which is very heavily informing our negotiating position.

MR. WESSEL: I see. And one final question. Pam Olson made a point of pointing out that this is complicated. And I wonder what your response to that is, especially relative to the current complexity of the corporate tax code and the capacity of corporations to make it even more complicated by finding ways to reduce their taxes. Does this make the tax code too complicated? Or is this a response to the behavior of corporations?

MS. BATCHELDER: Yeah, I mean, the important thing to note is the current code is incredibly complicated. And there are very extensive tax planning incentives, which is part of why these reforms are so important. There is this race to the bottom, which then requires very extensive tax planning to take advantage of. And what the deal would do is eliminate the benefits of engaging in profit shifting so that companies can locate their operations in sort of a race to the top that I discussed of looking at where are the most productive workers. And that's a race that we think we can win.

As I also mentioned, this deal is covering a very, very small share of

companies. It's two in 10,000 corporations. So, when you talk about corporations with tax departments that have 700-plus people and are already engaging in a great deal of complexity, I think it's important to note that they are the kind of taxpayers that can manage complexity and we do in the long-term think that this will simplify things, including by providing them with more certainty, which is one of the most difficult things for any taxpayer to deal with.

MR. WESSEL: Great. So, I want to thank both Lilys and Thornton and her panel for a really illuminating discussion in which we packed an incredible amount into 90 minutes. The whole video will be posted on our website so you can watch it over and over again. And I have a feeling we'll be revisiting this question again but thank you very much for listening, and thank you particularly to the Urban-Brookings Tax Policy Center for partnering with the Hutchins Center today for this interesting event.

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I, Carleton J. Anderson, III do hereby certify that the forgoing electronic file when originally transmitted was reduced to text at my direction; that said transcript is a true record of the proceedings therein referenced; that I am neither counsel for, related to, nor employed by any of the parties to the action in which these proceedings were taken; and, furthermore, that I am neither a relative or employee of any attorney or counsel employed by the parties hereto, nor financially or otherwise interested in the outcome of this action.

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