TAX CHALLENGES ARISING FROM THE DIGITALISATION OF THE ECONOMY

ECONOMIC IMPACT ASSESSMENT

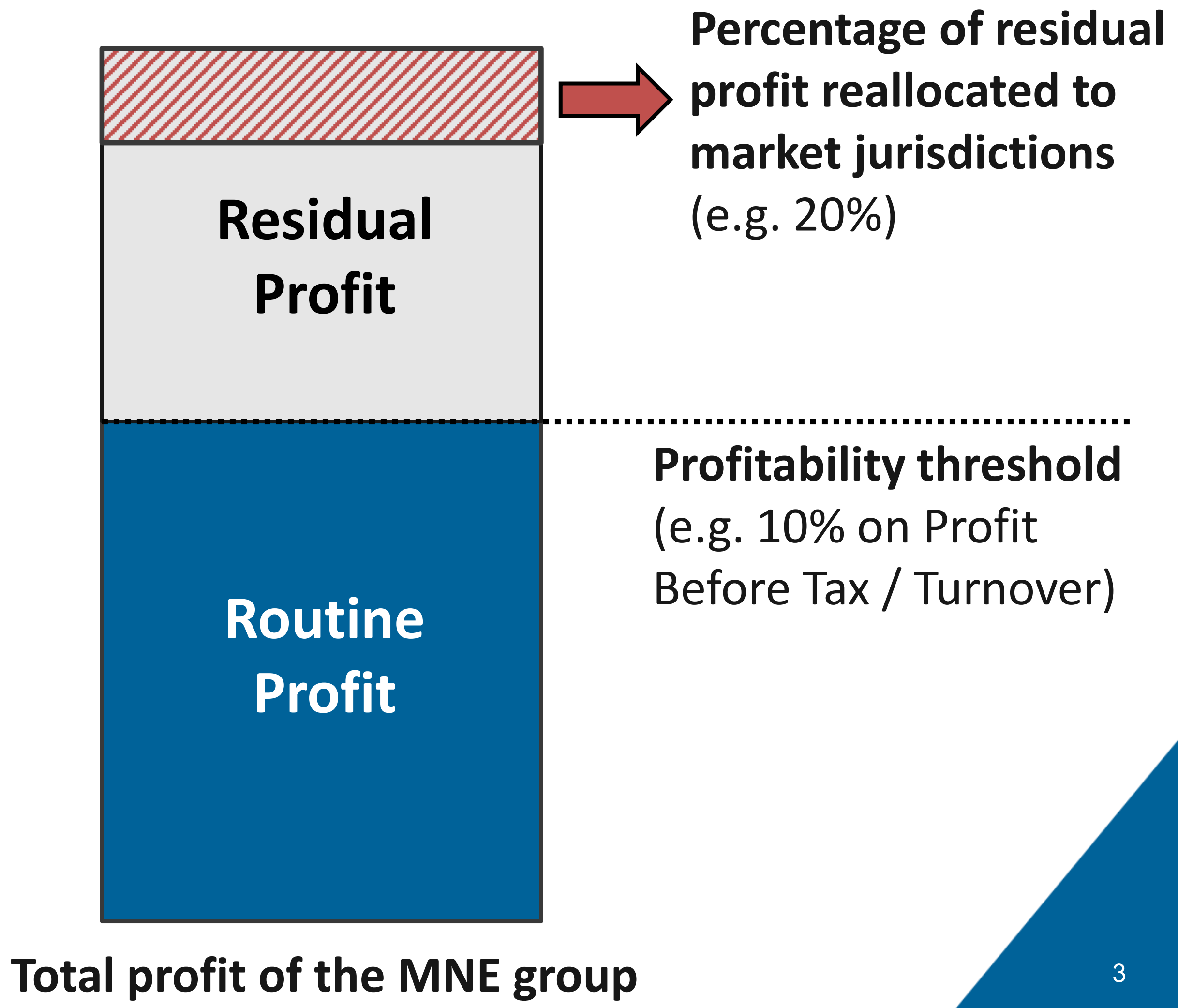
OECD
BETTER POLICIES FOR BETTER LIVES

Economic Impact Assessment: Approach and caveats

- **'Ex ante' assessment based on illustrative assumptions** on the design and parameters of the reform and potential reactions by MNEs and governments
  - **Combines firm-level and more aggregate data in a consistent framework** (including newly available CbCR data)
  - **The underlying data have limitations** and pre-date the 2017 US tax reform and the COVID-19 crisis.
- **Presents global results and results for jurisdiction groups.** No jurisdiction-specific data or results are included

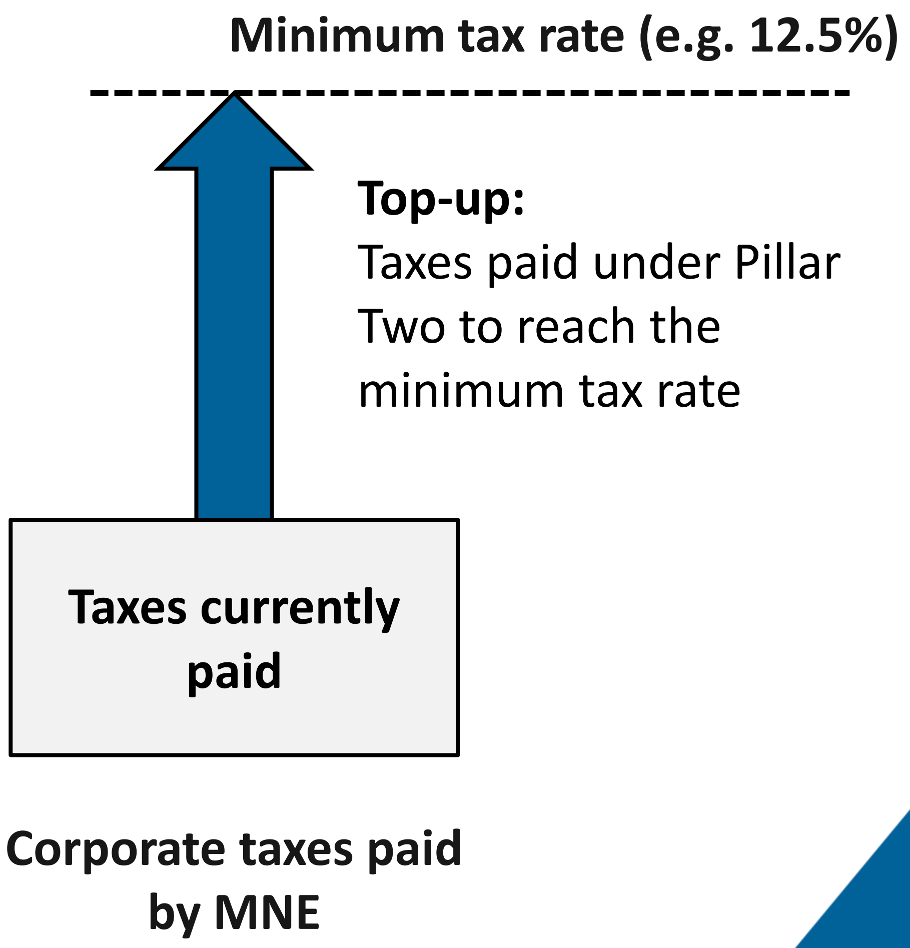
Pillar One would reallocate a percentage of residual profit to market jurisdictions

- **Amount A would involve significant changes** to current tax rules (e.g. going beyond physical presence)
- **Amount A could lead to a substantial reallocation of taxing rights** across jurisdictions (e.g. taxing rights on about USD 100 bn of profit could be reallocated)
- **Only Amount A was modelled**. The effect of Amount B and the Tax certainty component of Pillar One is expected to be small at the global level, but it could be significant in some jurisdictions



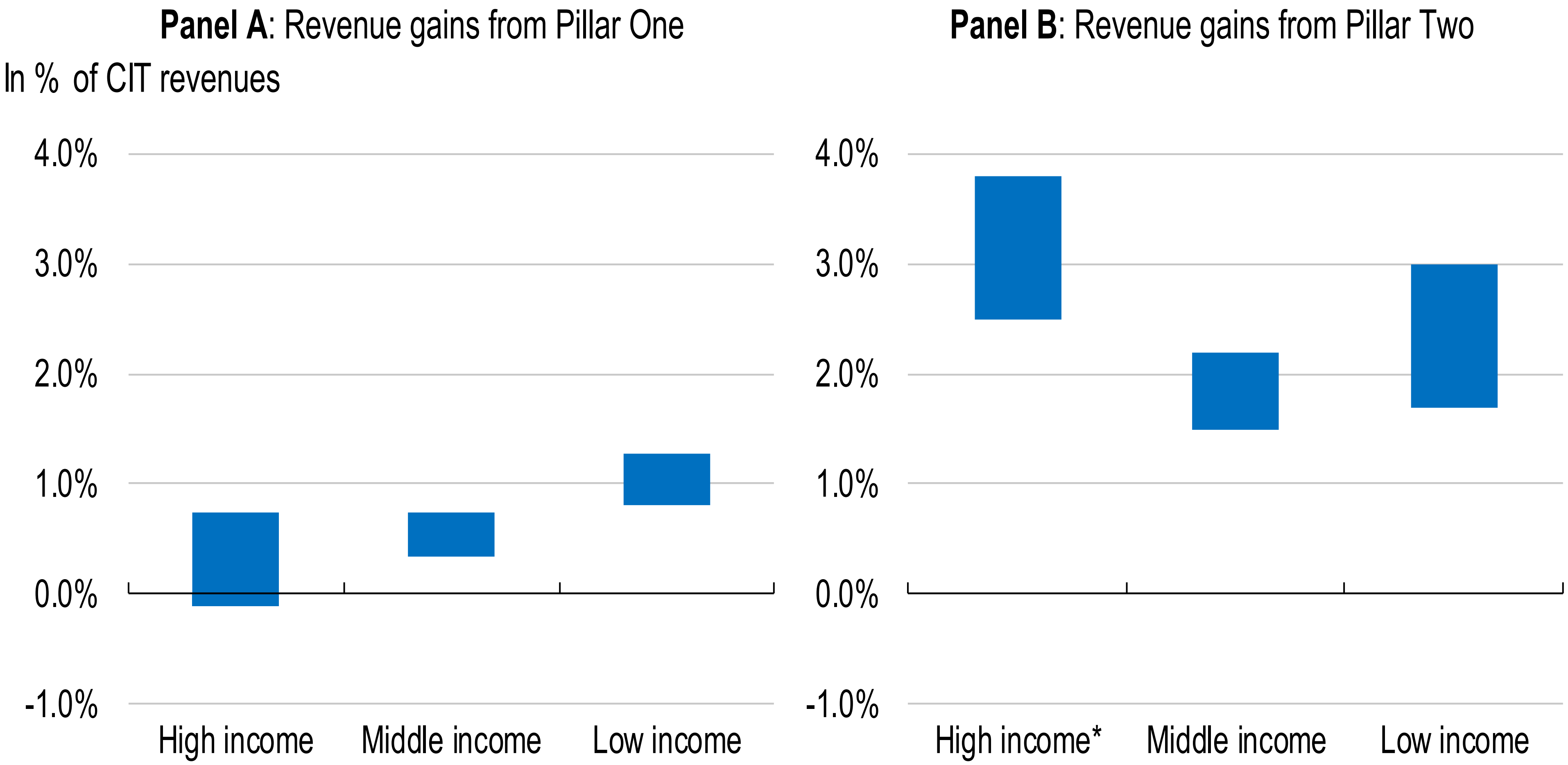
Pillar Two comprises a number of interlocking rules that would operate as a minimum tax rate

- **Pillar Two would give countries the right to 'tax back' profit** that is currently taxed below the minimum rate
- **It would essentially operate as a 'top-up' tax,** up to the minimum rate
- **The impact assessment assumes that it applies jurisdiction-by-jurisdiction** (i.e. jurisdictional blending)
- **It could involve a substance-based 'carve-out'** (i.e. subtract from profit a fixed percentage of payroll and depreciation expenses)
- **The US GILTI regime is assumed to coexist** with Pillar Two



Estimated tax revenue effects of the proposals

By jurisdiction groups



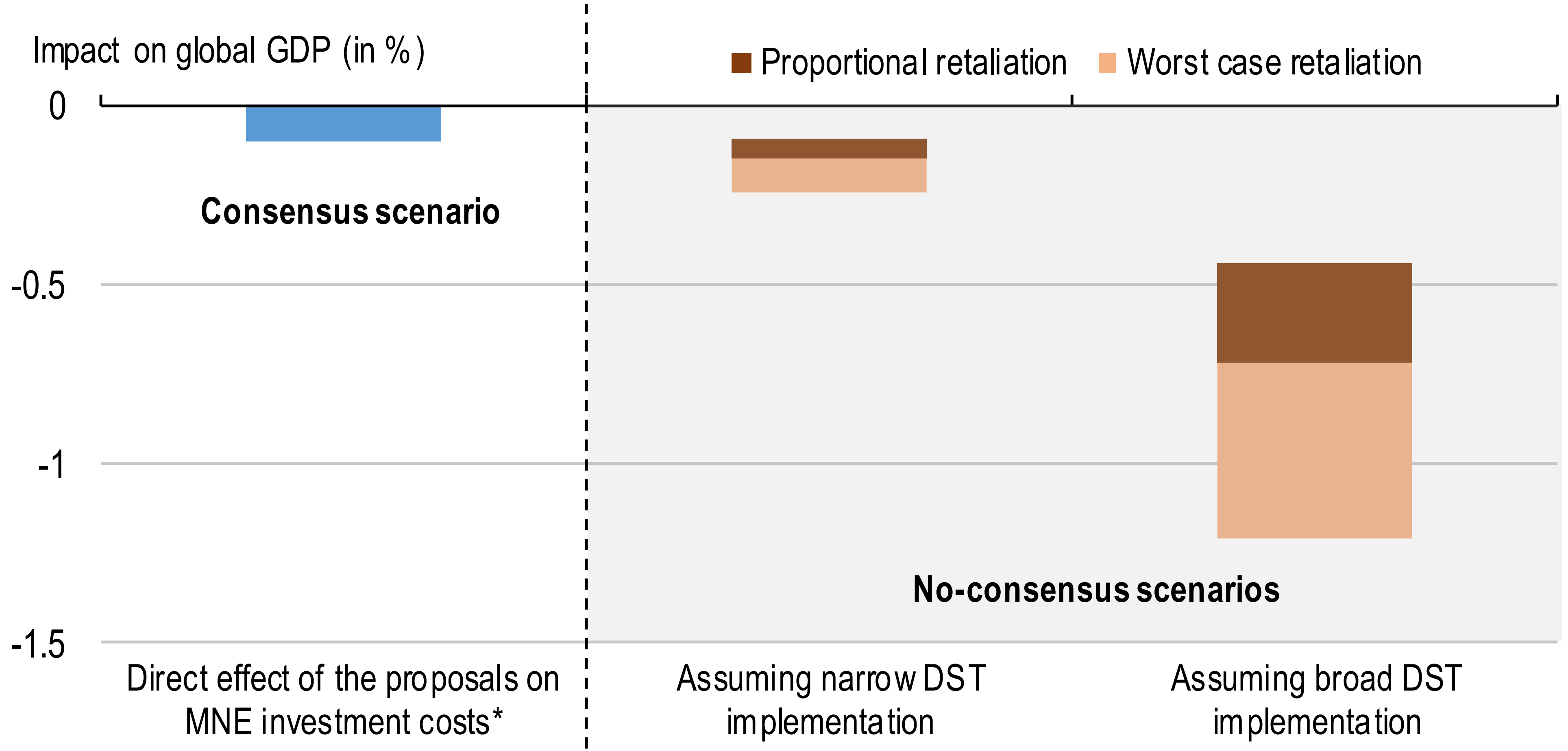
Note: These estimates are based on illustrative assumptions on the design and parameters of Pillar One and Pillar Two. The United States is excluded from the group of high income jurisdictions in the Pillar Two panel, reflecting the illustrative assumption that the US GILTI would co-exist with Pillar Two. Estimates for "investment hubs" are not included in these figures as they involve more uncertainty due notably to heterogeneity among investment hubs.

Main findings on investment effects

- **Both pillars would lead to a relatively small increase in the investment costs of MNEs**
  - The negative effect on global investment would be small, as the proposals would mostly affect highly profitable MNEs whose investment is less sensitive to taxes
- **Pillar One & Pillar Two could support global investment and growth through indirect channels that are significant, although less quantifiable by:**
  - Enhancing the efficiency of global capital allocation
  - Increasing tax certainty
  - Reducing the need to raise revenues through other (potentially more distortive) tax measures
- **In the absence of consensus, there would likely be a proliferation of uncoordinated and unilateral tax measures (e.g. digital service taxes) and an increase in damaging tax and trade disputes**

The consensus & no-consensus scenarios

Stylised scenarios: estimated effect on global GDP



* The proposals would also have positive impacts on GDP through indirect channels (e.g. increased tax certainty, reduced need to increase other distortive taxes) which are not quantified in this figure.

Summary of main findings

- **Pillar One and Pillar Two could increase global corporate income tax (CIT) revenues by about USD 50-80 billion per year**. The combined effect of the reforms and the US GILTI could represent USD 60-100 billion per year (i.e. up to around 4% of global CIT revenues).

- **The reforms would lead to a more favourable environment for investment and growth** than would likely be the case in the absence of a consensus-based solution.

- **In the absence of consensus, there would likely be a proliferation of unilateral tax measures (e.g. digital service taxes) and an increase in tax and trade disputes,** which could reduce global GDP by up to 1% in the worst case scenario.

- **The COVID-19 crisis is likely to accelerate the trend towards the digitalisation of the economy and exacerbate the tax challenges arising from digitalisation** in the absence of an agreement by the Inclusive Framework.

References

- **Economic Impact Assessment report**: https://www.oecd.org/tax/beps/tax-challenges-arising-from-digitalisation-economic-impact-assessment-0e3cc2d4-en.htm
- **Working paper on ETR analysis** (Hanappi and González Cabral, 2020): https://www.oecd-ilibrary.org/taxation/the-impact-of-the-pillar-one-and-pillar-two-proposals-on-mne-s-investment-costs_b0876dcf-en
- **Working paper on taxation and MNE investment** (Millot et al., 2020): https://www.oecd-ilibrary.org/taxation/corporate-taxation-and-investment-of-multinational-firms_9c6f9f2e-en
- **Highlights brochure**, with an overview of the Pillar One and Pillar Two Blueprint reports and of the impact assessment: https://www.oecd.org/tax/beps/brochure-addressing-the-tax-challenges-arising-from-the-digitalisation-of-the-economy-october-2020.pdf
- **Additional background**, including Pillar One and Pillar Two Blueprint reports: https://www.oecd.org/tax/beps/beps-actions/action1/