# Fight against Tax Havens and International Tax Law
# —New Taxing Right and a Global Minimum Tax—

OKA Naoki

***Tokyo Foundation for Policy Research, Certified Public Tax Accountant***

## Abstract

Global corporate tax revenue is vanishing due to the shifting of profits to tax havens. Under the current principles of international taxation, taxable income of each member of multinational enterprises (MNEs) is calculated on the assumption that individual companies are engaged in business transactions as a separate company dealing at an arm's length (principle of separate accounting). However, MNEs can easily reduce their group tax burden by booking intangible assets that generate a significant amount of profits (assumed to be excess profits) on the books of group companies in tax haven countries granting low tax rates.

This paper pays attention to the fact that a package of solutions worked out by the international community in January 2020 has boldly adopted the taxation of consolidated group income and a global minimum tax for income taxation of MNEs, and explores the meaning of the package under international taxation law. Will the package be effective in restraining "a race to the bottom" (Tax competition and corporate tax rates reduction)?

Keywords: international taxation, BEPS, tax avoidance, tax haven, multinational enterprise, intangible assets, OECD

JEL Classification: H25, H26, F23

## I. Introduction

While the economic growth in the OECD area has been weak for the last couple of decades, the amount of foreign direct investment (FDI) to countries considered as "tax havens" has been skyrocketing (See Figure 1). Tax haven countries provide "benefits" such as low or no taxation, the confidentiality of the information, and high-quality and accessible legal and financial services to multinational enterprises (MNEs) and high-net-worth individuals, in exchange for large amounts of nominal investments into—or passing through—their jurisdictions. Since 2013, The Organisation for Economic Co-operation and Development (OECD) has been working on the Base Erosion and Profit Shifting (BEPS) Project with the aim to set up an international framework to combat tax avoidance by MNEs through artificial shifting of profits to low-tax jurisdictions (tax havens) which results in tax base erosion in non-tax haven areas. The OECD BEPS project produced a series of final reports in 2015. However, the trends of profit shifting and tax base erosion remained. The amount of profits of MNEs shifted to tax havens in 2015 was estimated to 616.4 billion USD (Table 4). In

2017, the tax haven jurisdictions, whose combined amount of GDP accounts only for 3% of the global GDP, attracted 25% of global foreign direct investment (FDI). Profits are flowing into—and wealth is concentrating in—tax haven countries.

In January 2020, the OECD/G20 Inclusive Framework on BEPS ("IF")[1], in which nearly 140 countries participate, agreed and published a statement (OECD, 2000a) on the two-pillar approach to address the issue arising from the digitalization of the economy and the remaining BEPS issues as a basis for the negotiations of a consensus-based solution to be agreed by the end of 2020.

The IF Statement (OECD, 2020a) consists of Amount A (new taxing right), the Income Inclusion Rule, and the Undertaxed Payment Rule (in this paper collectively referred to as "new measures"). Amount A is for taxation of digital businesses in market jurisdiction (Pillar One), and income inclusion and undertaxed payment rules are for dealing with remaining BEPS issues. Table 1 outlines the key elements of these measures.

This paper discusses the relationship between the core elements of these new measures and international tax law by examining the following:

- First, to form a basis for analyzing the effectiveness and practicality of the new measures, this paper overview data concerning the concentration of wealth in tax haven countries.
- Second, this paper discusses the reported tax avoidance schemes of MNEs using tax havens and high-value intellectual properties (IPs), casting light on the digitalization of the economy.
- Then, this paper discusses that the new measures are a package for taxing excess profits of MNEs. Amount A will drastically replace the century-old separate accounting system with a unitary taxation system (i.e., corporate taxation based on consolidated profits of MNEs). GloBe measures (i.e., global minimum tax) will introduce taxation of a member of MNEs by referring to its foreign affiliates' tax situation and ensure that they bear a minimum level of corporation tax agreed internationally.
- Finally, this paper discusses the relationship between the above-mentioned characteristics of new measures and the international taxation principles.

Appendix 2 at the end of this paper discusses items for consideration and recommendations for designing rules for applying the new measures.

[1] The Inclusive Framework on BEPS, in which nearly 140 countries participate, allows interested countries and jurisdictions to work with OECD and G20 members on developing standards on BEPS related issues and review and monitor the implementation of the BEPS Package. More information is avairable at: https://www.oecd.org/tax/beps/beps-about.htm/. See Appendix 3 for the timeline of developments thus far.

Table 1. Outline of the three new measures discussed in this paper

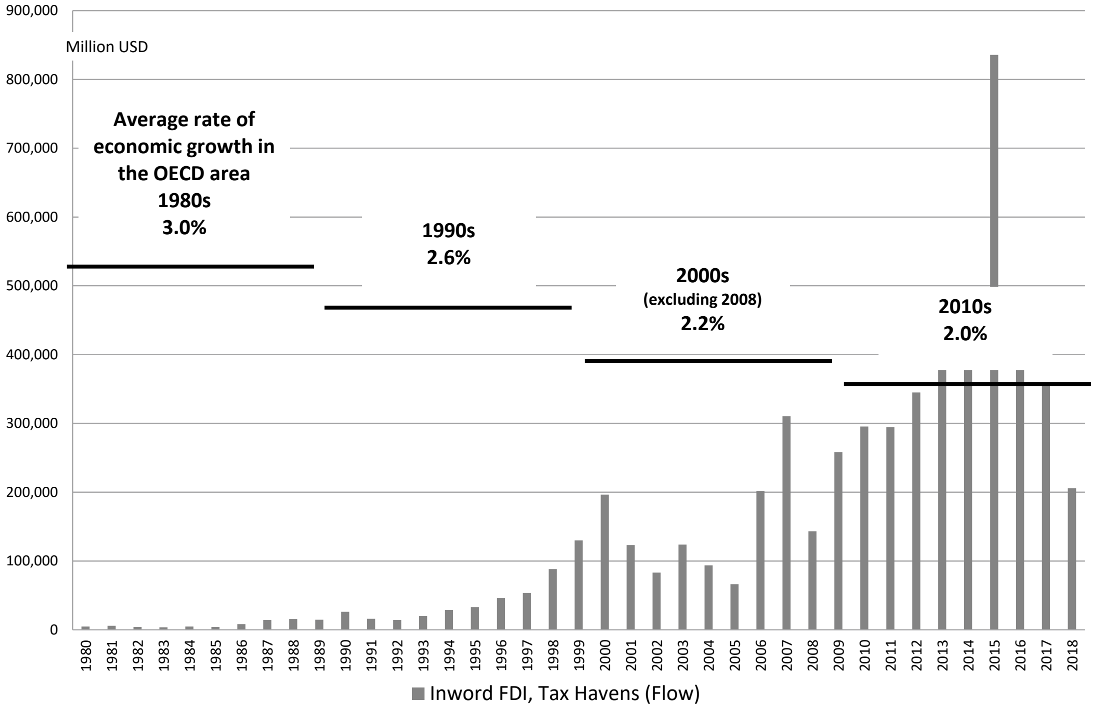
| | Measures | Taxpayer/Taxing jurisdiction | Purpose | Issues to be dealt with |
|---|---|---|---|---|
| Pillar One (unified approach) | New taxing right (Amount A) | Foreign corporation of a MNEs/ Source country | Reallocation of taxing right from remote locations (tax havens) to market jurisdictions | Under the digitalization of the economy, businesses are able to provide digital services remotely (often from tax havens) to customers in markets using little or no local (physical) infrastructure. Under the existing international tax rules, which have been applied for over 100 years, a (physical) infrastructure is required as a prerequisite for taxation. Thus, market jurisdictions may not be able to tax profits arising from digital businesses carried out in their jurisdictions. |
| Pillar Two Global-minimum tax ("GloBE" proposal) | Income inclusion rule (e.g., US GILTI) | Domestic corporation of MNEs/ Resident country | Provide jurisdictions with a right to "tax back" where (i) other jurisdictions have not exercised their primary taxing rights, or (ii) the payment is otherwise subject to low levels of effective taxation. | Focuses on remaining BEPS issues. Tax avoidance schemes of MNEs through the use of intangible property (IPs) and tax haven affiliates. |
| | Undertaxed payments rule (e.g., US BEAT) | Domestic corporation of MNEs/ Resident country | | |

(Source) OECD (2019) on Global Anti-Base Erosion Proposal ("GloBE"), and OECD (2020b) and OECD (2020c) reports on Pillar One and Pillar Two blueprints.

## II. Situation of tax havens today from the viewpoint of international taxation

This section introduces the data concerning the increase in foreign direct investment in tax havens, and the empirical study on the profit shifting behavior of MNEs and the flow of investment passing through tax havens (as investment hubs).

Figure 1. Increase of FDI flows into tax havens and the economic growth rate in the OECD area (1980-2018)




(Source) Author, based on data from UNCTAD database

### II-1 Geographical definition of "Tax havens"

(1) A report of the OECD project on "harmful tax competition" identified factors of tax haven (OECD, 1998) p. 23. Box 1

(a) No or only nominal taxes: whether a jurisdiction imposes no or only nominal taxes

(b) Lack of effective exchange of information: laws or administrative practices which prevent the effective exchange of relevant information with other governments on taxpayers benefiting from the low or no tax jurisdiction

(c) Lack of transparency: a lack of transparency in the operation of the legislative, legal, or administrative provisions in another factor in identifying tax havens

(d) No substantial activities: the absence of a requirement that the activity be substantial (it would suggest that a jurisdiction may be attempting to attract investment or transactions that purely tax-driven)

(2) OECD BEPS Final Report (2015) discusses six indicators of BEPS (Table 2).

Table 2. Indicators of BEPS

| Category | Six Indicators of BEPS |
|---|---|
| A. Disconnect between financial and real economic activities | 1. Concentration of high levels of foreign direct investment (FDI) relative to GDP |
| B. Profit rate differentials within top (e.g., top 250) global MNEs | 2. Differential profit rates compared to effective tax rates<br>3. Differential profit rates between low-tax locations and worldwide MNEs operations |
| C. MNE vs. "comparable" non-MNE effective tax rate differentials | 4. Effective tax rates of large MNE affiliates relative to non-MNE entities with similar characteristics |
| D. Profit shifting through intangibles | 5. Concentration of high levels of royalty receipts relative to research and development (R&D) spending |
| E. Profit shifting through interest | 6. Interest expense to income ratios of MNE affiliates in high-tax locations |

(Source) OECD (2015), para 79.

(3) Geographical definition of tax haven in this paper

In this paper, the term “tax havens” means a shortcut for jurisdictions listed in column A of Table 3

Table 3. Various tax haven lists

| A: Tax haven list in this paper | B: Reference | | | | |
|---|---|---|---|---|---|
| | OECD (2020)[2] "investment hubs" | IMF (2019)[3] | Tørsløv et al. (2020)[4] | Hines, J et al. (1994)[5] | US John Dow Summons[6 7] |
| Ireland | ○* | ○* | ○ | ○ | |
| Luxembourg | ○* | ○* | ○ | ○ | ○ |
| Netherlands | ○* | ○* | ○ | | |
| Switzerland | Not applicable | ○* | ○ | ○ | ○ |
| Bermuda | Not applicable[15] | ○* | ○ | ○ | ○ |
| Hong Kong SAR | ○* | ○* | ○ | ○ | ○ |
| Singapore | ○* | ○* | ○ | ○ | ○ |
| British Virgin Islands | ○* | ○ | ○ | ○ | ○ |
| Cayman Islands | ○* | ○ | ○ | ○ | ○ |
| Barbados | Not applicable | ○ | ○ | ○ | |
| | Investment hubs are jurisdictions with inward FDI above 150% of GDP | Other Caribbean countries | Other Caribbean countries, including Belgium, Malta, Puerto Rico, etc. | Other countries, including Panama, Channel Islands, etc. | Other countries, including Aruba, Malta, Lebanon, Cook Islands, etc |

(Source) Author, based on various information

[2] OECD Webcast 13 February 2020 presentation p. 12 https://www.oecd.org/tax/beps/presentation-economic-analysis-impact-assessment-webcast-february-2020.pdf

[3] IMF (2019) Figure 7, p. 34

[4] Tørsløv et al. (2020) Table 2

[5] Hines, J & Rice, E. (1994) Appendix 2 Tax haven Countries

[6] GAO (2008) Table 1. U.S. District Court order granting leave for IRS to serve a “John Doe” summons.

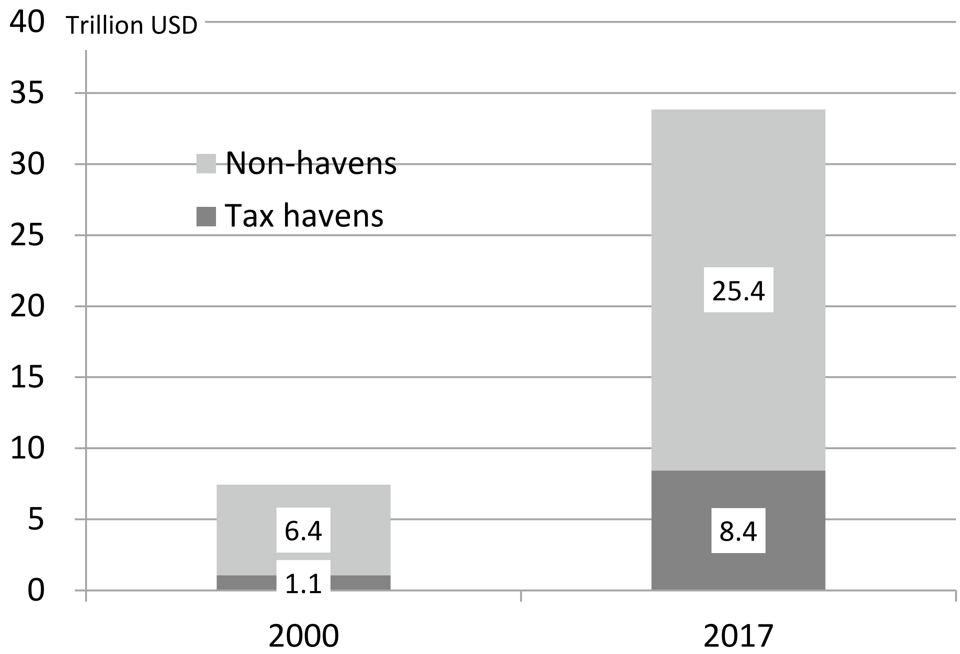
[7] GAO (2008). “a U.S. District Court order granting leave for the Internal Revenue Service (IRS) to serve a “John Doe” summons that included a list of offshore tax haven or financial privacy jurisdictions.”(p. 3). “The court did not address whether these jurisdictions were in fact tax havens in its ruling.” (Footnote 11).

## *II-2 Investment in tax havens*

(1) Foreign direct investment into tax havens is growing

The amount and ratio of investment in tax havens in global FDI is increasing. In terms of inward foreign direct investment balance in tax havens, it was 8.4 trillion USD in 2017, which was 25% of the global direct investment balance of 33.8 trillion USD (See Figure 2). In contrast, the aggregate amount of GDP of tax haven jurisdictions accounts only for 2.6 trillion USD, which is only 3% of the global GDP of 80.5 trillion USD in the same year.

Figure 2. Growing FDI in tax havens (Stock)



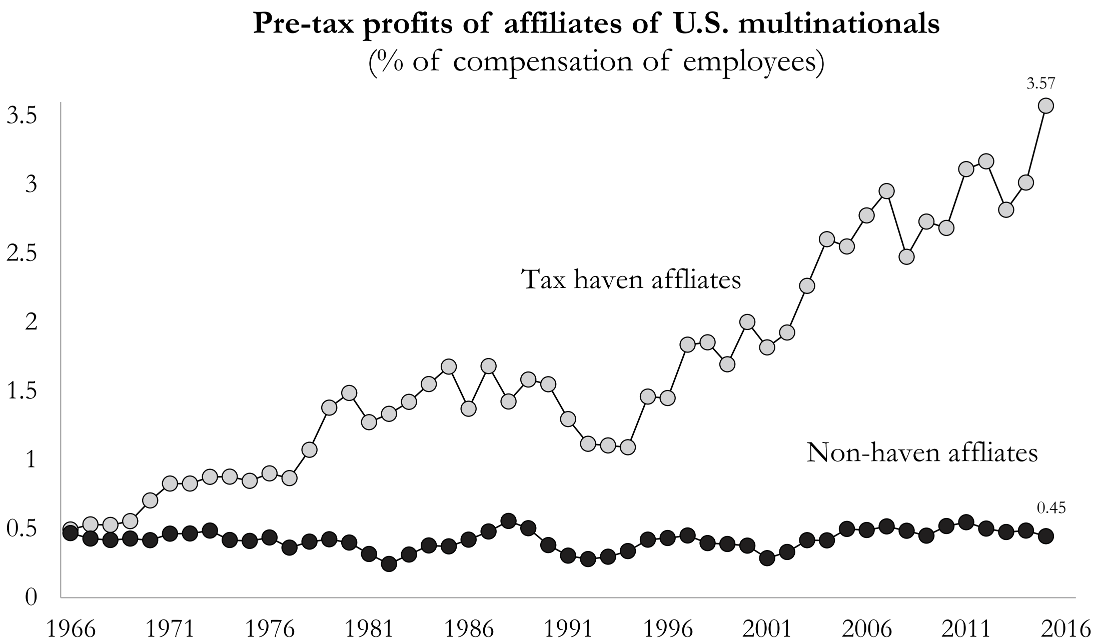

(Source) Created from UNCTAD database.

(2) Concentration of wealth in tax haven affiliates

Sullivan (2020a) estimates that the US MNEs booked at least 230 billion USD of profits at their affiliates in tax haven jurisdictions (Singapore, Ireland, Switzerland, Netherlands, Luxembourg, Cayman Islands, Bermuda).

As shown in Figure 3, the growth of pre-tax profits of US MNEs of their tax haven affiliates is unusually high compared to the non-tax haven affiliates.

Figure 3. Increasing pre-tax profits of tax haven affiliates of US MNEs (ratio to wages)




(Source) Tørsløv, Wier, and Zucman (2020) Figure 5

## *II-3 The amount of profit shifted to tax havens (estimate)*

Torslov, Wier, And Zucman (2020) estimates that the amount of profits of MNEs artificially shifted to tax havens was 616 billion USD in 2015. This is 5% of the global profits of MNEs (Table 4).

Table 4. Global Output, Corporate Output, and Corporate Taxes Paid (2015)

| Billion USD | Global | | Japan | | United States | |
|---|---|---|---|---|---|---|
| Net corporate profits | 11,515 | 100% | 634 | 100% | 1,889 | 100% |
| –Net profits of foreign controlled corporations | 1,703 | 15% | 32 | 5.0% | 153 | 8.1% |
| –of which: shifted to tax havens | 616 | 5% | 28 | 4.4% | 142 | 7.5% |
| –Net profits of local corporations | 9,812 | 85% | 602 | 95.0% | 1,737 | 91.9% |
| Corporate income tax (Effective corporate tax rate) | 2,154 | 19% | 196 | 26% | 397 | 21% |

(Source) Auther, based on Tørsløv, T; Wier, L; and Zucman, G. (2020) Table 1, Table 2 and online Appendix Table A7 and C4.

(Note) Tørsløvm,W.et al (2020) explained that they used the same methodology used by the OECD is estimating the amount of tax base erosion in is BEPS final reports in 2015 (p. 8). In estimating the amount of artificially shifted profits, they focused on the fact that the profitability of tax haven affiliates of MNEs (as shown in figure 3) is much greater than that for non-haven affiliates (the level of profitability is measured by comparison to wage level). (p. 22). Then, they assumed that the difference was created by artificial profit shifting. (p. 27). The following illustrates the difference

| | Profitability of foreign affiliates | Profitability of domestic corporations |
|---|---|---|
| Ireland | 800%* | 68% |
| Singapore | 218% | 48% |
| Japan | 24% | 44% |
| United States | 28% | 32% |

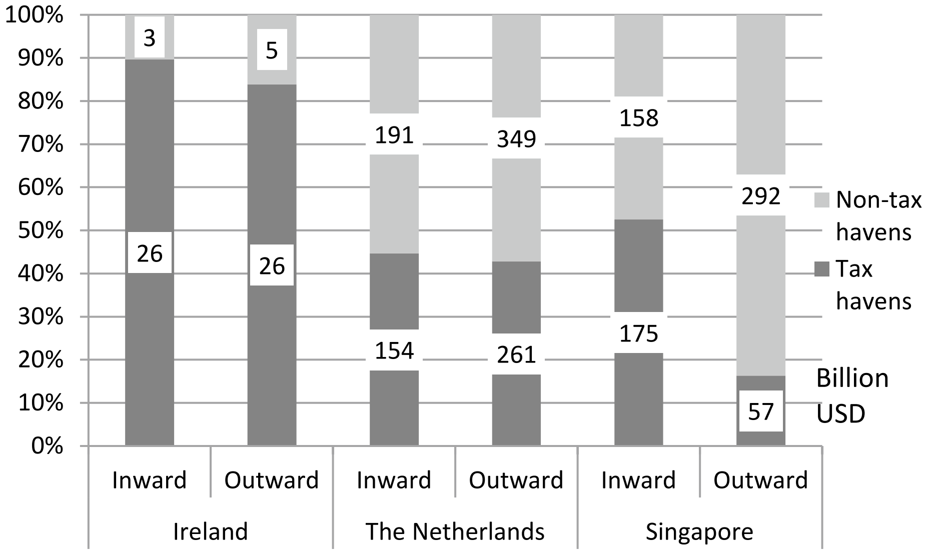
* Percentages are based on the wage level

### *II-4 Tax havens as "conduit"*

Kaneko (2019) p. 618 stated, "In tax havens, it is generally very easy to establish a legal entity, and such entity does not have their own offices or staff. It just acts as a "conduit" between the parent company and its business partners. Tax havens are often used as a conduit."

Figure 4 shows the balance of inward and outward foreign direct investment in Ireland, the Netherlands, and Singapore, and their top 10 partners from tax haven and non-tax haven countries

Figure 4. Inward-outward foreign direct investment (balance) of selected countries Top 10 Investment Partners: Tax Havens and Non-Tax Havens (2016)




## III. Tax issues arising from the use of tax havens and intangibles

This section describes tax challenges arising from the use of tax havens and intangibles by MNEs under the digitalization of the economy.

### *III-1 Issues discussed in the 1990s*

The OECD Report on harmful tax competition project published in 1998 points out six items as challenges caused by tax havens (Table 5).

Table 5. Problems caused by tax havens

| |
|---|
| 30. Tax havens or harmful preferential tax regimes that drive the effective tax rate levied on income from the mobile activities significantly below rates in other countries have the potential to cause harm by: |
| (1) distorting financial and, indirectly, real investment flows; |
| (2) undermining the integrity and fairness of tax structures; |
| (3) discouraging compliance by all taxpayers; |
| (4) re-shaping the desired level and mix of taxes and public spending; |
| (5) causing undesired shifts of part of the tax burden to less mobile tax bases, such as labor, property, and consumption; and |
| (6) increasing the administrative costs and compliance burdens on tax |

(Source) OECD (1998) para 30.

### *III-2 The estimated size of base erosion*

As a mode of tax avoidance using tax havens, it is said that for individuals, tax evasion is often performed by using the confidentiality of the information, and for MNEs, tax avoidance is often performed by profit shifting[8].

According to the report published by the US Congressional Research Service, Gravelle (2015, p. 1), the United States loses as much as 40-70 billion USD due to the tax evasion of individuals and 10-90 billion USD due to the profit-shifting of MNEs.

The OECD estimates that as much as 100 to 200 billion USD of corporation tax revenue (or 500-1,200 billion USD if the corporation tax rate is 20%) is lost annually due to tax avoidance and artificial shifting of profits[9]. This is 4-10% of the global corporation tax revenue. As was discussed earlier, the estimated amount of profits of MNEs artificially shifted to tax havens is was 616.4 billion USD in 2015.

### *III-3 "Race to the bottom"—Tax competition and corporate tax rates reduction*

The average corporate tax rate for each OECD country was 32.2% in 2000, but it became 23.7% in 2018, a decrease of 8.5 points in 20 years. As Keen (2019) noted, if the OECD's estimation of the amount of profit shifting and the corporation tax loss is accurate, this means the reduction of the corporation tax rate by 2.5% worldwide (p. 22). This is much

---

8 Guttentag & Avi-Yonah (2005).

9 https://www.oecd.org/tax/beps/about/.

smaller compared to the decrease in corporation tax rates in the recent past. Keen argues that if governments want to secure their tax revenue, they should pay more attention to tax competition (corporate tax rate cuts), rather than counteracting tax avoidance.

### *III-4 Tax avoidance schemes using tax havens and intangible properties*

In the business models of the digital economy, intangible property (intellectual property, IP, e.g., trademark, know-how, algorisms) plays an important role. MNEs can book intangible property at their affiliates (often “post box companies” or “shell companies” that do not possess infrastructure nor ability to carry out substantial activities) in tax haven countries where no or only nominal tax is applied. Then, MNEs can then attribute income from sales in overseas markets to such tax haven affiliates, or pay the license fee for the use of intangible property to such tax haven affiliates from affiliates in high-tax countries. As a result, MNEs can achieve tax avoidance by reducing the overall tax burden.

A tax avoidance scheme called “The double Irish with a Dutch sandwich,” which was used by big US technology companies (i.e., Appl Inc. and Alphabet Inc. (Google)), is structured by using tax havens and high-value intangible properties. The scheme’s thrust is shifting sales license (intangible property) developed in the US necessary for the sale of products in overseas markets to Irish subsidiaries. By doing this, the US MNEs can attribute sales in overseas markets (high-tax countries) to their subsidiaries in Ireland (tax haven).

In the Ichijo-Koumuten (constructer) tax case (Nagoya District Court, Judgement, September 29, 2005), a scheme with a similar structure was used. The taxpayer transferred intangible property to a Singapore affiliate for attributing royalties from business partners in Japan to it. (Appendix 1-1)

The tax reduction effects of such schemes that utilize high-value intangible property and tax havens are powerful. Apple Inc. admitted at the US Senate hearing that the Irish subsidiary’s effective tax rate was less than 2% for decades[10].

### *III-5 Refinement of Arm’s length principle regarding intangible properties and the obscuring of application of the principle (the “black-boxfication” of transfer pricing rule).*

In recent years, the OECD has devoted a great deal of time and energy to the application of transfer pricing taxation rules on intangible assets. For example, BEPS final reports 8-10 (2015)[11] and, the revised OECD Transfer Pricing Guidelines (2017) introduced the concept of “DEMPE” for evaluating the compensation of members of MNEs owning and using intangible property. The revised OECD Transfer Pricing Guidelines (2017) discusses the issue in ownership of intangibles and transactions involving the Development, Enhancement,

[10] S. Hrg. 113-90 OFFSHORE PROFIT SHIFTING AND THE U.S TAX CODE--PART 2 (APPLE INC.) MAY 21, 2013. https://www.govinfo.gov/content/pkg/CHRG-113shrg81657/pdf/CHRG-113shrg81657.pdf

[11] OECD “Aligning Transfer Pricing Outcomes with Value Creation: ACTIONS 8-10: 2015 Final Reports”

Maintenance, Protection and Exploitation (DEMPE) of intangibles as follows:

Para 6.32 (Excerpts) "…Although the legal owner of an intangible may receive the proceeds from exploitation of the intangible, other members of the legal owner's MNE group may have performed functions, used assets, or assumed risks that are expected to contribute to the value of the intangible. Members of the MNE group performing such functions, using such assets, and assuming such risks must be compensated for their contributions under the arm's length principle. This Section B confirms that the ultimate allocation of the returns derived by the MNE group from the exploitation of intangibles, and the ultimate allocation of costs and other burdens related to intangibles among members of the MNE group, is accomplished by compensating members of the MNE group for functions performed, assets used, and risks assumed in the development, enhancement, maintenance, protection and exploitation of intangibles according to the principles described in Chapters I–III."

These enormous amounts of efforts for Refinement of transfer pricing (or international taxation rules) rules have been made in order to "Aligning Transfer Pricing Outcomes with Value Creation" as stated in the OECD BEPS final report (2015). In other words, these efforts have been made in order to bring back for tax purposes the profits of MNEs attributed to intangible properties "booked" at tax haven affiliates to other members of the MNEs. Efforts were made to attribute profits to members of the MNEs involved in "actual activities" concerning the development of the intangible property, production of goods and services using such intangible property, or sales of goods and services using such intangible property.

Such an aim might have been achieved to some extent and hoped to deliver certain effects in combating tax avoidance of MNEs using intangible property and tax haven. However, the use of arm's length principle has become much complicated. In practice, in applying each element of DEMPE, issues of evaluation and estimation remain significant.

Ito (2015, Chapter 5) has noted that one of the main reasons why the MNEs are thriving is because it is hard to evaluate intangible property fairly between third parties through markets.

According to Shiga (2011, p. 267), the theoretical flaws of transfer pricing taxation is that, although the essence of transfer pricing taxation is the issue of distribution of taxation rights between nations, it is trying to present the system as based on the arm's length principle, i.e., comparison of prices between related parties and independent parties through markets. Application of arm's length principle inevitably became fictitious where comparable transactions cannot be found in markets. There is room for the taxation agency's arbitrariness. Where intangible properties are involved, the problem became acute.

The application of the arm's length principle for intangible property for which comparable transactions do not exist in market is hard. The application of arm's length principle has become obscure (a kind of "black-box"), arbitrary, and all these allow the artificial transaction/evaluation of intangible properties by MNEs. Neither National Tax Administration (Japan)[12] nor Internal Revenue Service (US)[13] has been successful in transfer pricing enforcement as they often lose important litigations involving intangible property[14].

### III-5-1 Views on the use of market as a benchmark

Originally, the arm's length principle was considered as a natural reaction. By using the market as a benchmark, it was conceived that transparency is retained and arbitrary application of tax rule would be excluded.

Surry (1978, p. 414) stated:

> The use of this arm's length standard is a natural reaction. Tax administrations do not question transactions that are governed by the marketplace. If Company A sells goods to unrelated Company B at certain price or furnishes services at a particular price, the income of both companies is determined by using that price. One company may be large and the other small; one may be a monopoly; one may be financially strong and the other in a weak condition. But these and other factors which may affect the price at which the transaction occurs are not the concern of the tax administrator. His task is not to correct the injustices or unfairnesses of the marketplace nor to turn bad bargains into fair arrangements.

Avi-Yonah (2004) is critical about the application of the arm's length principle without market benchmarks. He commented on the expansion of the US transfer pricing regulation as follows (p. 24)

> (Excerpts) "It even initially called profit split the "basic arm's length return method." But as I have pointed out elsewhere, once you abandon the search for comparables, it is meaningless to call a method "arm's length," because, without comparables, nobody can know what unrelated parties would have done."

### *III-6 Residual profits (excess profits) of MNEs booked in tax haven*

(1) Residual profit means the excess profit due to the contribution of intangible assets

For transfer pricing taxation purposes, income arising from the contribution of intangible property constitutes "residual profits"[15]. The amount of residual profits of MNEs is calculated by subtracting the amount of profits from routine activities (remuneration of routine activities) from the amount of consolidated profits of the MNEs.

Therefore, "routine profits" represent remuneration of routine function for which comparable transactions are likely to found in markets. And "residual profits" represent "profits

---

[12] For example, Judgement of Tokyo District Court (April 11, 2017) held in favor of taxpayer (a subsidiary of US MNEs) over the transfer pricing taxation of goods using Disney character (high-value intangibles) and tax haven affiliate (Bermuda). See World Family Case in Appendix 1-1.

[13] Finley, Ryan "Ninth Circuit Affirms Tax Court in Amazon Transfer Pricing Case" Tax Notes International August 26, 2019.
"The Ninth Circuit affirmed the Tax Court's 2017 decision in favor of Amazon, holding that the transfer pricing regulations' definition of the term "intangible property" excludes goodwill, going concern value, and other residual business assets."

[14] For more information concerning experience of Japan in this area (profit shifting court cases), please see Appendix 1-1

[15] National Tax Administration (Japan) "Commissioner's Directive on the Operation of Transfer Pricing (Administrative Guidelines).

from special contribution intangible properties, etc." for which comparable transactions are not likely to found in markets. Therefore, in essence, for the purpose of taxation (transfer pricing), "residual profits is "excess profits" of MNEs created by intangible properties.

Keen (2019, p. 44) noted, the residual profit method is a hybrid of the arm's length method and formula apportionment method

"Step 1: Allocate routine profit by Arm's Length Price (or mechanically)

Step 2: Allocate residual by Formula Apportionment (or equivalent)"

Arm's length method is based on separate accounting (accounting books of an MNE group are separated between the entities operating in different countries) and using transactions found in markets as a benchmark for allocation of taxable profits.

Formulary apportionment method (unitary taxation) is a method of allocating an MNE group's consolidated profits to a particular tax jurisdiction in which taxable presence is identified. Allocation of the profits is made based on prescribed keys (such as the amount of sales, property and/or employees).

(2) Concentration of residual profits (excess profits) to the top 1% of MNEs

An empirical study conducted by the IMF (2019) based on accounting data from 7,600 MNEs rivaled that residual profits (excess profits) of MNEs concentrated in the top 1% (100) of MNEs. This share of residual profits of such top1% of MNEs is 85% of the total profits and extremely large. It would be reasonable to assume that such a concentration of excess profits is created by the high markup rate of intangible assets and excess profit arising from the "monopoly." These imply that taxation of residual profits (excess profits) is important in designing taxation of MNEs.

(3) Excess profit booked in tax havens

As was discussed thus far, intangible properties, i.e., source of residual profits or excess profits, are booked/owned by tax haven affiliates of MNEs, allowing MNEs to shift profits from high tax countries to tax havens through the payment of royalties by affiliates in high-tax countries (Table 6).

Table 6. Residual profit (excess profit) ratio and concentration in multinational corporate groups

| | Top 100 MNEs with the largest residual profits | MNEs with positive residual profits | All MNEs surveyed (7600 MNEs) |
|---|---|---|---|
| Share of the global total of residual profits | 1/3 | | |
| Percentage of residual profit to all profit | 85 % | 58% | (Minus) 147% |

(Source) IMF (2019) p. 71

## IV. The architecture of the new measures and its evaluation

The taxation of MNEs is currently based on separate accounting (i.e., accounting books of an MNE group are separated between the entities operating in different countries). This section discusses that three “new measures” ( i.e., Amount A for allocating taxable profits of MNEs to market jurisdiction under Pillar One and income inclusion rule and undertaxed payment rule under Pillar Two) are, effectively, for taxation of foreign corporations (corporations normally outside of geographical tax jurisdiction).

This section discusses that the new measures introduce novel ideas into international tax principle—such as taxation based on consolidated income of an MNE, and taxation by effective tax burden of affiliates of an MNE.

### *IV-1 application of new measures*

This sub-section examines the effectiveness of new measures against tax minimizing/avoidance schemes found in reality.

(1) In September 2019, Google agreed to pay over 965 million Euro to French Authorities to settle disputes concerning the tax affairs of two European Subsidiaries.[16] Below is the overview of the case.[17]

- Google is a global group providing digital services that gets the bulk of its revenue from the broadcast of online advertisements. AdWords (Google Ads) is Google’s leading advertising program. It allows advertisers to broadcast targeted advertising related to the searches made by users or content sites consulted.
- Alphabet Inc (“Google US”) , is a US company and the ultimate parent of the Google group.
- Google Ireland Ltd (“Google Ireland”) is an Irish company and a subsidiary of Google US.
- Google France SARL (“Google France”) is a French limited liability company and is a subsidiary of Google US.
- Google Ireland’s main activity is the sale of Google products and services in France (and in other European, Middle East and African countries. (Presumably, Google Ireland owns intangible property for selling Google products and services)
- Google Ireland and Google France concluded a contract (2002). Under the contract, Google France employees will carry out marketing and sales support to teams of Google Ireland.
- The compensation paid by Google Ireland to Google France was determined by cost plus (8%)

[16] Athanasiou, Amanda. “Google to pay France nearly €1 Billion to settle tax dispute” Tax Notes International, September 16, 2019, p. 1179.

[17] This outline was drafted based on information taken from the press release of the financial prosecutor, Paris, September 12, 2019, and Monsenego (2019).

- In 2012, the French tax authority argued that Google Ireland had a permanent establishment in France (in employees of Google France, i.e., an agent PE)

(2) By applying new measures, the following outcome may be envisaged. The new measures seem to be effective in dealing with profits shifting and base erosion schemes using tax haven and intangible property. It would be reasonable to say that the new measures will be successful in taxing excess profits, which, in this case, presumably accumulated in the Irish subsidiary.

1. A part of consolidated profits of Google Ireland (or Google US, i.e., consolidated global profits of Google as MNEs) would be subject to tax in France as a market jurisdiction, regardless existence of dependent PE in France. (Pillar One: Amount A)
2. If the effective tax rate of Google Ireland is below the level of internationally agreed minimum tax (this is likely to be the case), the difference (up to the minimum tax level agreed internationally) may be taxed in the United States (Pillar Two: income inclusion rule)
3. Hypothetically, if Google France paid royalty to Google Ireland, and the payment is not taxed in Ireland, France could apply tax to the minimum level of taxation agreed internationally (Pillar Two: undertaxed payment rule)

## *IV-2 Structure of new measures and their evaluation*

### IV-2-1 New taxing right (Amount A)

### (1) Outline of the measure and its evaluation

| | |
|---|---|
| Architecture of Amount A | ●Consolidated profits of target businesses of MNEs will be calculated<br>●The excess part of the consolidated profits (10%) is considered as “residual profits” (excess profits)<br>●20% of the residual profits will be allocated to different countries by the amount of sale<br>※ See Figure 5 for calculation and allocation of Amount A |
| Country to take action | ●Source country (market jurisdiction) |
| Target tax avoidance scheme or situation | ●Avoid taxable presence (i.e., permanent establishment) in the market jurisdiction<br>●Carry out business in market jurisdiction from a remote location (i.e., tax haven) or through a Limited Risk Distributor |
| The measure is applied only where base erosion exists? | ●Yes: Compulsory application to multinational companies with large sales (750 million euros)<br>(Note) The US proposed in December 2019 to make this as a safe harbor, i.e., optional to taxpayers |
| Purpose of the measure | ●Redistribution of profits of MNEs from tax havens to market jurisdictions<br>●Effective taxation of excess profits (profits from high-value intangible properties) of MNEs |
| Relationship to International Tax Principle/System | ●It could be considered a drastic departure from Separate Accounting. The OECD paper argues that the “new Profit Allocation Rule going beyond the Arm’s Length Principle” (OECD 2019, p.5)<br>●Could be considered as introduction of Destination-based corporation tax<br>●However, this measure is not intended to be applied generally. There are high monetary thresholds, such as the large size of turnover and profitability. It would be more accurate to consider this measure as a specific targeted anti-avoidance measure for base erosion created by artificial profit sifting |
| Experience of countries | ●Common consolidated corporation tax base (CCCTB) proposal in the EU |

Figure 5. Calculation and allocation of Amount A

| STEPS | Explanation | Remarks |
|---|---|---|
| 1. Tax Base: Use consolidated financial accounts to deter tax base erosion (PBT: profits before tax ) | Determine MNE group PBT based on consolidated financial accounts | -Global revenue test (7.5mil Euro?)<br>-Apply de-minimis foreign source in-scope (ADS and CFB) revenue test |
| 2 Apply revenue sourcing rules / apply the monetary thresholds for ADS and CFB | ADS (Digital services) \| CFB Consumer-facing (goods/services) | -Apply revenue sourcing rules to determine market jurisdictions<br>-Apply monetary threshold for ADS and CDB revenues |
| 3 Nexus test to identify eligible market jurisdictions (EMJs) | Monetary threshold only (A, B) \| Monetary threshold + plus factors (D,E) | -For CFB, the sales may not be sufficient to establish nexus |
| 4 Allocate Amount A to EMJs through a formula (3 steps)<br>(1) Profitability threshold 10%? | Residual profits \| 10 %? \| Residual profits \| 10 %? | -A profitability threshold to isolate the residual profit potentially subject to reallocation (profit before tax to revenue ratio) |
| (2) Reallocation percentage 20%?<br><br>(3) Apply allocation key (local in scope revenue) | C B A: 20%?of the residual profits \| C E D: No plus factor 20%? | -A reallocation percentage to identify the applicable share of residual profits<br>-Allocation key to distribute the allocable tax base |

(Source) OECD (2019b)

(2) MNEs and taxation based on consolidated profits

The most significant feature of the new taxing right is the introduction of unitary taxation (fiscal apportionment) for taxing excess profits of the MNEs. This is the desired direction for taxing the income of MNEs.

Economist points out a limitation in transfer pricing taxation (separate accounting) in evaluating "risk." Risk is an important factor in the taxation of transfer pricing. MNEs bear risk as a group, and it is meaningless to consider the risk is borne by a member or members of the multinational group.

Ito (2015, Chapter 5), who has worked for an accounting firm and has ample experience in practice, noted that multinational companies exist because of intangible property. He argued that taxation of MNEs should be by formulary apportionment of consolidated profits. Below is a translation and summary by the author.

The value of intangible assets is hard to evaluate through the market because of the inherent peculiarities (external effects, information asymmetry, uncertainty of effects). Given the cost theory of multinational corporations, which means that multinational corporations will choose inter-group transactions if the cost of transactions within the group is lower than that of transactions with a third party through the market. Therefore cross-border investments are facilitated. Intangible assets on the manufacturing side contribute to the acquisition of excess profits by lowering production costs. Intangible assets on the sales side contribute to the acquisition of excess profits through increased profits. Then, the excess income (at least the part of it) is being derived from the intangible assets. Ito argues that taxation of consolidated profits of multinational companies by the formula allocation method is desirable.

## IV-2-2 GloBE Proposal: Global minimum tax (Pillar Two)

### (1) Outline of the measures and their evaluation

| | Income inclusion rule | Undertaxed payments rule |
|---|---|---|
| Architecture | Current year inclusion of profits of low-taxed subsidiary: The income inclusion rule would operate as a minimum tax by requiring a shareholder in a corporation to bring into account a proportionate share of the income of that corporation if that income was not subject to an effective rate of tax above a minimum rate agreed internationally | The undertaxed payments rule operates by denying a deduction or making an equivalent adjustment for intra-group payments—if the payment is not subject to the minimum level of tax in the hand of payee. This could also be designed as withholding tax at source and denying treaty benefits (taxation of the payee). |
| Country to take action | Home country (country of residence) of MNEs | Country from which profits are shifted (source country) |
| Target tax avoidance scheme or situation | There are three main types of strategies for inter-company transfer of profits within multinational corporations<br>・Transfer pricing<br>・Payment of royalties and/or interest[18] within the group<br>・Transfer of intangible properties to tax haven affiliates, and then attribute income from third party | |
| The measure is applied only where base erosion exists? | No: Measures to seek tax burdens up to internationally agreed levels There are no thresholds for the size of sale or the amount of deductible payments | |
| Purpose of the measure | ・Establishing the minimum level of taxation based on international agreements on corporate profits in order to counter tax avoidance due to profit transfer and curb competition for tax rate reduction<br>・There is no threshold for the size of turnover, etc. | |
| Relationship to International Tax Principle/ System | Specific provisions to counter base erosion caused by profit shifting<br>⇒In order to clarify this, it may be considered to set threshold and limit the application to large corporations/large amounts of payments that can be said to have base erosion of the tax base. | |
| Experience of countries | US GILTI (Global Intangible Low-Taxed Income) | US BEAT (Base Erosion and Anti-abuse Tax)<br>UK Offshore receipts in respect of intangible property |

[18] UNCTAD (2015, p. 190) discussed the root causes of the outsized role of offshore hubs in global investments (in another word, profits shipting) as (i) intangibles-based transfer pricing schemes (i.e., through inter group payment of royalties), and (ii) financing schemes (i.e. through inter group payment of interests).

(2) Country experiences in this area.

A. Experiences of the United States[19]

(a) GILTI: Current Year Inclusion of Global Intangible Low-Taxed Income by US shareholders (introduced by the Tax Cuts and Jobs Act of 2017) Section 951A

A 10.5% minimum tax on undistributed profits of tax haven affiliates bearing tax less than 13.123%)

Under the provision, a US shareholder of any foreign affiliates (CFC) must include in gross income for a taxable year its global intangible low taxed (at least 13.123%) income ("GILTI") in a manner generally similar to inclusions of subpart F income.

GILTI means, with respect to any US shareholder for the shareholder's taxable year, the excess (if any) of the shareholder's net CFC (tested) income over the shareholder's net deemed tangible income return. The shareholder's net deemed tangible income return equals the excess (if any) of 10 percent of the aggregate of its pro-rata share of the qualified business asset investment ("QBAI") of each CFC with respect to which it is a US Income by US Shareholders.

The applicable effective tax rate of GILTI income is 10.5% (due to the 50% deduction).

Estimated budget effect: 112,413 million USD (2018-2027)

(b) BEAT: Base Erosion and Anti-Abuse Tax (10% Minimum Tax introduced by the Tax Cuts and Jobs Act 2017) Sec. 59A

A 10% minimum tax on certain deductible payment to foreign affiliates. Various thresholds apply.

Liability for this additional tax is generally limited to those taxpayers with substantial gross receipts. It is determined, in part, by the extent to which the taxpayer has made deductible payments to foreign related parties ("base erosion tax benefits"). Taxpayers potentially liable for this additional tax have three-year average gross receipts in excess of $500 million and a "base erosion percentage" exceeding a specified threshold (3%, or 2% for financial institutions). The base erosion percentage is generally determined by dividing "base erosion tax benefits" by the amount of deductions allowable to the taxpayer for the taxable year.

The base erosion minimum tax amount equals the excess, if any, of 10 percent of modified taxable income over the amount of regular tax liability.

Estimated budget effect: 149,568 million USD (2018-2027)

B. Experience of the United Kingdom

Offshore receipts in respect of intangible property (Explanation below are excerpts from the UK HMRC website)[20]

A 20% tax on payments concerning UK sales (over £10 million) to offshore tax haven entities which are taxed less than 50% of the UK tax.

---

[19] (Source) Joint Committee on Taxation (2018) "General explanation of Public Law 115-97 prepared by the staff of Joint Committee on Taxation" (p. 368 and p. 403) https://www.jct.gov/publications/2018/jcs-1-18/.

[20] HM Revenue&Customs Policy paper Published 29 October 2018 https://www.gov.uk/government/publications/offshore-receipts-from-intangible-property/income-tax-offshore-receipts-in-respect-of-intangible-property.

Large multinational groups that hold intangible property in low tax jurisdictions, where the income which arises in relation to that intangible property is referable to the sale of goods or services in the UK. The measure will apply regardless of whether there is a UK taxable presence.

The policy targets multinational groups that generate significant income from intangible property through UK sales and have made arrangements such that the income is received in offshore jurisdictions where it is taxed at no or low effective rates.

The measure will generally apply to entities that are located in jurisdictions with whom the UK does not have a full tax treaty (i.e., a tax treaty with a non-discrimination provision).

The Income Tax charge will be on the gross income that is referable to the sale of goods or services in the UK and realized by the non-UK resident entity from the ownership, or rights over, relevant intangible property.

In the event of non-payment by the non-UK resident entity, joint and several provisions will enable collection of the debt from connected parties.

The measure will include a tax exemption which will exclude from charge, income where the tax payable by the foreign entity in relation to income that is referable to the sale of goods or services in the UK is at least 50% of the UK Income Tax charge that would otherwise arise under this measure. There will also be a £10 million de minimis UK sales threshold.

The measure will have effect from April 6 2019.

Estimated budget effect: £1,135 annually

## V. "New measures" and international tax law

The conflict between the economic rationality pursued by taxpayers (in this paper, the focus is on tax avoidance and/or tax minimizing efforts of MNEs using tax haven and intangibles) and the geographical constraints of national sovereignty is one of the issues that has been discussed for a long time.

The tax jurisdiction of a country is limited by reference to its sovereign power under international law (Vann, 1998 p. 17) . Avi-Yonah (2004, p. 2) explained, "The traditional grounds of jurisdiction to prescribe in international law are nationality ("the activities, interest, status or relations of [a state's] nationals outside as well as within its territory") and territoriality ("conduct that, wholly or in substantial part, takes place within [a state's] territory").

For international taxation, nationality jurisdiction is redefined and expanded as "residence jurisdiction,"—which usually implies mere physical presence in the country. Territoriality jurisdiction is refined and expanded as "source jurisdiction,"—which covers "conduct outside a state's territory that has, or intended to have, a "substantial effect" within its territory" (Avi-Yonah, 2004, p. 4). These are two widely accepted bases of jurisdiction to tax, i.e., residence and source.

Therefore, international tax rules have to deal with the taxation of persons from outside a country (as a source jurisdiction) who have activities or income in the country; and taxation of persons (as a resident jurisdiction) who belong to a country who have activities or income abroad (Vann, 1998, p. 3).

Nakazato (2015, p. 26) pointed out that the limitation imposed by the jurisdiction to tax would hinder the realization of the BEPS project. The international legal order, which is based on the coexistence of sovereign states, has a history of more than 300 years, and "jurisdiction to tax is also limited to the territory of national sovereignty. This restriction on tax jurisdiction is particularly strict with respect to execution of tax law." (in Japanese)

There is a conflict between jurisdiction to tax based on residence jurisdiction and source jurisdiction. According to Shiga (2011, p. 8), the three main themes of international tax law are (1) elimination of double taxation, (2) prevention of international tax avoidance and (3) distribution of tax rights between nations. (in Japanese)

As noted in section IV, thrusts of the new measures are (1) taxation of excess profits of an MNE's consolidated income and (2) application of internationally agreed minimum level of tax to the profits (likely to be the excess profits) of MNEs. All of them have never been seen before.

Based on the understanding outlined above, this section will examine the relationship with international taxation law.

## *V-I Substancial elements of the new measures and relevant international tax principles.*

Table 7 summarizes substantial elements in new measures and relevant international tax principles.

Table 7. Summary of new measures and international tax principles

| New measures | Policy objective | Taxation method (M)<br><br>Taxpayer (T) /<br>Taxing jurisdiction (J) | Base erosion | International tax principle |
|---|---|---|---|---|
| New taxing right (Amount A ) | ・Redistribution of profits of MNEs which was shifted to tax haven to market jurisdictions<br>・Taxation of MNEs excess profits in market jurisdictions | (M) Formula apportionment of consolidated profits of MNEs<br>(T) Foreign corporation<br>(J) Resident jurisdiction | Thresholds apply: the size of the business, the level of profitability | Departure from separate accounting.<br>It has thresholds and does not apply generally. Therefore, the measure should be considered as a specific anti-avoidance/base erosion rule |
| Income inclusion rule | ・Ensure MNEs to pay the minimum level of tax | (M) Current year inclusion of profits of tax haven affiliates by shareholders<br>(T) Domestic corporation<br>(J) Resident jurisdiction | The level of taxation of tax haven subsidiaries | Specific rule for anti-base erosion<br>It goes beyond the anti-tax avoidance rules (e.g., CFC rules) |
| Undertaxed payment rule (UTPR) | Ensure MNEs to bear the internationally agreed minimum level of tax. | (M) Substantially taxable on the payer side due to denial of deduction<br>(T) Domestic corporation (a member of MNEs[21])<br>(J) Resident jurisdiction | The level of taxation of income in the hand of the recipient | The existing measures consider the situation of payer for application of anti-avoidance rules.<br>However, undertaxed payment rules consider the situation of the payee for application of the rule. |
| Note: Subject to tax rule | | (M) Withholding tax on payments to foreign member of MNEs which is taxed under the minimum level of tax<br>(T) Foreign corporation[22]<br>(J) Source jurisdiction | | |

[21] The UTPR requires a UTPR taxpayer that is a member of an MNE group to make an adjustment in respect of any top-up tax that is allocated to that taxpayer from a low-tax Constituent Entity of the same group. OECD (2020c) p. 120

[22] "It is a treaty based rule that specifically targets risks to source jurisdictions posed by BEPS structures relating to intragroup payments which take advantage of low nominal rates of taxation in the other contracting jurisdiction (that is, the jurisdiction of the payee)." OECD (2020c) para 566 p. 150.

### *V-2 Assessing the new measures with reference to Avi-Yonah's "International Tax as International Law"*

(1) Principles in international tax law as outlined in Avi-Yonah (2004).

Avi-Yonah argues that a coherent international tax regime (customary international law) exists that is embodied in tax treaties and the domestic laws of most countries based on two principles, i.e., single tax principle and benefits principle.

Avi-Yonah (2016, p. 12-13) further elaborate single tax principle and benefits principle as the core of the international tax regime

A. The benefit principle—under which active income (e.g., business income such as sale of goods and provision of services) should be taxed primarily at source jurisdiction and passive income (e.g., interest, dividend from the investment) should be taxed primarily at residence jurisdiction. Many commentators agree that the benefit principle has been the core of the international tax regime since 1923.

B. The single tax principle—under which all income should be subject tax at the rate derived from the benefit principle (i.e., for active income, it is the consensus corporate rate, and for passive income, it is the residence rate for individuals).

Avi-Yonah acknowledges that the single tax principle is controversial and many commentators deny the validity and coherence of the single tax principle. However, the IMF economist Keen seems in agreement with Avi-Yonah. Keen (2019, p 26) considered that "the only principle in international taxation is profits exceeding the normal profits (excess profits, rent) should be taxed somewhere" (in Japanese).

C. Avi-Yonah also refers to the "first bite at the apple" principle" adopted by the League of Nations in 1923[23]. Under that principle, the source jurisdiction has the primary right to tax income arising within it, and put the obligation to prevent double taxation on residence jurisdiction (Avi-Yonah, 2004, p. 9).

(2) Assessment of new measures and international tax principles

This subsection attempts to assess the new measures against the existing international tax principles outlined by Avi-Yonah (mentioned above).

- <u>The new taxing right (Amount A) expands source jurisdiction to tax on</u> business income of certain business activities that can be carried out in source (market) jurisdiction from remote locations (tax haven). They are not currently taxed in source jurisdiction due to permanent establishment thresholds (i.e., the source jurisdiction may not tax business profits unless the non-resident corporation earning profits has a permanent establishment in the source jurisdiction). The rule can be justifiable under the benefit principle (i.e., business income), the single tax principle (i.e., active income) and the first bite at an apple (i.e., taxation of source country) principle.

[23] The League of Nations adopted in 1934 "the first bite at an apple" principle which give primarily right to tax to the source jurisdiction and oblige resident jurisdiction to prevent double taxation; and the "benefits"' principle, under which active income should be taxed primarily at source, and passive income primarily on a residence basis.

- The undertaxed payment rule is the rule for ensuring taxation of excess profits. Therefore the rule can be justifiable under the single tax principle (i.e., multinationals' excess profits arising from intangible property).

  Imamura (2019, p. 119) pointed out that professor Avi-Yonah pointed out that taxation at source jurisdiction is appropriate for MNEs. Because businesses benefit from activities carried out in source jurisdiction, and it is difficult for source jurisdiction to refrain from collecting tax on profits arising in their jurisdiction.

- Income inclusion rule, expands resident tax jurisdiction of shareholders country of residence to foreign subsidiaries in tax haven jurisdictions.

Since the rule will "fill in" or "tax back" the space where tax havens (low tax jurisdictions) are not exercising their jurisdiction to tax and impose the minimum at the internationally agreed level. Therefore, it will not harm the taxation right given o the source jurisdiction and will not disturb the existing rules for distributing taxation among jurisdictions.

Avi-Yonah (2004, p. 9), remarked about CFC rules which has the similar mechanism to the income inclusion rule, noted as follows:

> "What, then, enables the United States and other countries to expand nationality jurisdiction to subsidiaries in the tax area? The explanation is the "first bite at the apple rule," adopted by the League of Nations in 1923. Under that rule, the source (territorial) jurisdiction has the primary right to tax income arising within it, and the residence (nationality) jurisdiction is obligated to prevent double taxation by granting an exemption or a credit. Thus, permitting the expansion of residence jurisdiction to CFCs does not harm the right of source jurisdictions to tax them first; residence (nationality) jurisdiction only applies as a residual matter when the source jurisdiction abstains from taxing."

### *V-3 The new measures—anti-avoidance provisions or something else?*

(1) Do new measures ignore private law form?

Anti-tax avoidance rules aim to deal with the problem arising from the basic concepts of "form" and "substance." Form (or legal form) refers to the concepts described by terms used in tax statutes, first and foremost terms used to describe the legal conditions of a tax rule. Zimmer (2002, p. 23).

Taxpayers can, by contrived arrangements, avoid the application of tax laws, or obtaining certain tax benefits. Anti-tax avoidance rules would deny, for tax purposes, legal form.

In order for the new measures to be considered as anti-tax avoidance rules, the target, i.e., abuse of private law form needs to be identified. However, as discussed below, what exploitation of the legal form the new measures are ignoring for tax purposes are unclear.

- Amount A (new taxing right)—Whether the conduct of business from a remote location (often tax haven) immidiately constitutes abuse of private law?
- Income inclusion rule—Whether "deemed dividend" concept applicable to this rule?
- Undertaxed payment rule—This rule is applied based on the tax situation of the payee of income (recipients), and not regarding the situation of the payer of the income.

(2) New measures as specific measures for counteracting base erosion

Masui and Miyazaki (2019, p. 186) pointed out that, after the adoption of the territorial system (exemption of dividend received from foreign subsidiaries) in Japan in 2009, the policy explanation for the CFC rule has been changed. The CFC rule was considered an anti-tax avoidance rule to deal with deferral or non-payment of dividends to shareholders. Before the reform, dividends of foreign subsidiaries received by shareholders were taxed. After the adoption of the territorial system, the CFC rule is explained as an anti-tax base erosion rule.

Therefore, the policy of new counteracting measures should be considered as anti-base erosion rules, rather than anti-abuse rules.

### *V-4 New measures and tax treaties*

The legal sources of international tax law are, domestic tax laws (including jurisprudence), tax laws of foreign countries, and tax treaties concluded between countries. In addition, the judgement of the Supreme Court, October 29, 2009, acknowledged that the OECD Commentaries on the Articles of the Model Convention as a "supplementary means of interpretation" referred to in Article 32[24] of the Vienna Convention on the Law of Treaties (1969).

With regard to the relationship between domestic law and tax treaty, the "savings rule" is relevant. According to the rule, notwithstanding the treaty provision, jurisdiction to tax residents are not affected is relevant.

Therefore, if a taxpayer of a new measure is a non-resident of treaty partner country, relevant treaty provision would prevail. If a taxpayer of a new measure is resident, then tax treaty provision is irrelevant.

It is clear that Amount A (Pillar One) is creating a new tax right for source jurisdiction and therefore would require revision of existing tax treaties because it will give new taxing right to tax business income in source countries without having a permanent establishment.

On the other hand, Pillar Two GloBE rules (global-minimum tax measures) are, in effect, applying tax burden on foreign subsidiary or recipients in tax haven (low tax jurisdiction), but in the form, these are taxation on residents. Taxpayers of income inclusion rule

[24] Article 32 Supplementary means of interpretation: Recourse may be had to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, in order to confirm the meaning resulting from the application of Article 31, or to determine the meaning when the interpretation according to Article 31: (a) leaves the meaning ambiguous or obscure; or, (b) leads to a result which is manifestly absurd or unreasonable.

(IIR)[25] and undertaxed payment rule (UTPR)[26] are defined as domestic taxpayers of the country introduced GloBE rules. Therefore, in principle, the application of these rules are not affected by treaty provisions.

With regard to the income inclusion rule (which resembles existing CFC rules) expands residence jurisdiction to subsidiaries in tax haven.

As Avi-Yonah noted (see above), expansion of resident jurisdiction under the income inclusion rule to subsidiaries may be enabled based on the "first bite of an apple" principle. Judgement of the Supreme Court (October 29, 2008) concluded that the application of the CFC rules in domestic law would not be restricted by the provisions of tax treaty (i.e., Articles 7 and 5 of Japan-Singapore tax treaty).

In addition, if Globe rules in domestic law is considered as domestic anti-avoidance rules, they are not affected by the treaty. Paragraph 58 of the Commentary on Article 1 of the OECD Model Convention states as follows (Excerpts and emphasis added):

> 58. (omitted) For these States, the issue then becomes whether the provisions of tax conventions may prevent the application of the anti-abuse provisions of domestic law, which is the question addressed in paragraphs 66 to 80 below. <u>As explained in these paragraphs, as a general rule, there will be no conflict between such rules and the provisions of tax conventions.</u>[27]

**BOX: Two faces?—Income inclusion rule and a subject to tax rule**

Subject to tax rule (STTR) is designed to complement undertaxed payment rule (UTTR). They are both aim to achieve the same goal and deal with cross-border low taxed payments. However, taxpayers and taxing jurisdictions are different. The taxpayer of UTTR is domestic corporation (payer) and collected by filing of corporate tax returns, so it is a taxation of the country of residence. The taxpayer of STTR is the foreign recipient of the law-taxed payment and collected through withholding at source. Therefore, on the one hand, tax treaty provisions are irrelevant for the taxation of UTTR which is the taxation of resident jurisdiction, on the other hand, application of STTR might require a revision of existing treaty because it is a taxation of source jurisdiction.

---

[25] OECD (2020b) para 411 "The IIR operates in a way that is similar to a CFC rule in that it subjects a domestic taxpayer to tax on its share of the foreign income of any controlled subsidiary"

[26] OECD (2020b) p. 120 regarding UTPR (undertaxed payment rule) "Definition of UTPR Taxpayer: A UTPR taxpayer is any Constituent Entity that is located in a jurisdiction that has implemented the UTPR in accordance with the GloBE rules (a UTPR Jurisdiction).

[27] As discussed above (V-3 (1)), the author do not consider new measures as anti-tax avoidance rules in the conventional sense, i.e., provisions to deny effects of civil law form for the purpose of taxation.

## *V-5 Indicators (hallmarks) for tax base erosion and profit shifting (BEPS)*

I have discussed that the policy goal of new measure are primarily counteracting tax base erosion (caused by profit shifting). It is therefore important to define base erosion. Facts and indicators that infer the existence of tax base erosion could include, for example, (i) large amounts (sales and/or deductible amounts), (ii) high-profit margins, and (iii) low effective tax burdens. Based on these indicators, the new measures can be evaluated as follows (Table 8).

Table 8. New measures and hallmarks for tax base erosion and profit shifting

| | The amount is large | High profit margin | Low tax burden rate |
|---|---|---|---|
| New taxing right (Amount A) | Consolidated sales of 750 million euros | 10% or more (pending) | No |
| Income inclusion rule | No<br><br>⇒the size of sales should be above a certain level. | No<br><br>⇒the level of profit margin should be above a certain level.<br><br>e.g., US GILTI is 10% | 12.5% (pending) |
| Undertaxed payments rule | No<br><br>⇒the amount of payment should be above a certain level.<br><br>US BEAT, UK tax have the threshold | No | 12.5 % (pending) |

Given that large multinationals (with sales over 750 million euros) are filing information return concerning their global activities through Country by Country Reports (CbCR), which are shared among tax administrations, limiting the application of rules for large multinationals would be helpful for tax administrations to overcome limitation imposed by enforcement jurisdiction.

From the policy point of view, a certain level of size would be required to call the problem as “tax base erosion.”

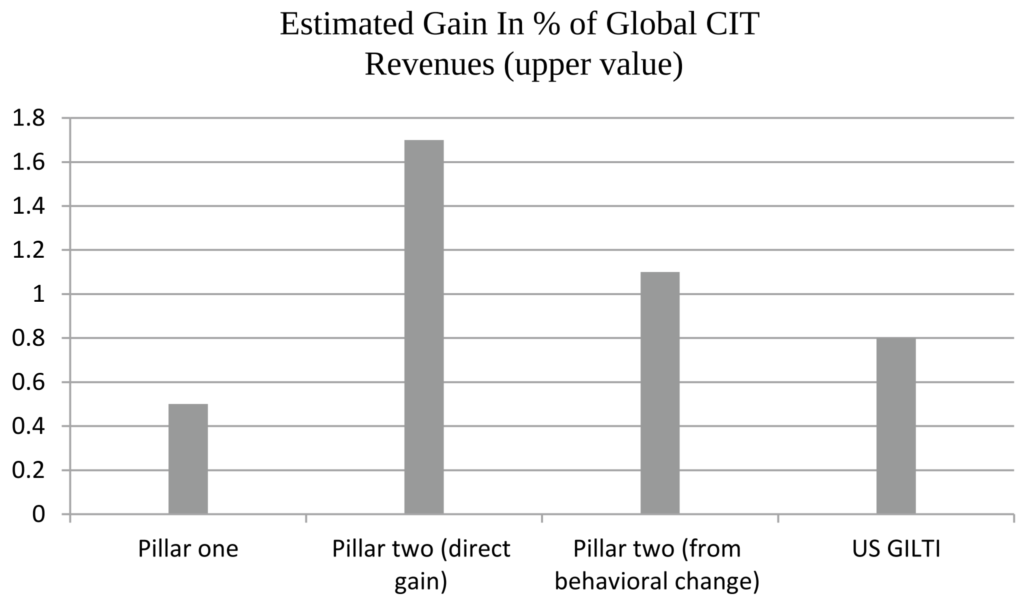
Note: Concerning issues (1) jurisdiction of tax, (2) countermeasures for harmful foreign tax practice, and (3) the relationship with tax treaty, please see Appendix 1-2 "Implications of the Judgement of the Supreme Court, October 29, 2019 - The CFC rule as an expansion of residence jurisdiction and countermeasure for foreign harmful tax measure."

## VI. Points for consideration and recommendations in designing proposed new measures[28]

### *VI-1 Economic impact of new measures (macro estimate by OECD)*

According to the estimation published by the OECD (Figure 6), the new measures would increase corporation tax by 100 billion USD or equivalent to 4% of global corporation tax. It is noteworthy that (i) tax revenue increase created directly by new measures account only about three quarters (or 3% of global corporation tax revenue increase) of the overall anticipated corporate tax increase. (ii) The effects of global minimum tax is larger than that from Amount A. (iii) Behavioral change of MNEs will be important. In addition, the OECD also revealed in its webinar presentation in February 2020 that half of the Amount A revenue increase come from only about 100 MNEs.

Figure 6. Economic impact of proposed measures on global corporate tax revenue (OECD estimate)




[28] See Appendix 2 for the summary of proposals.

| Estimated global tax revenue gains | | In % of global CIT revenues | In USD billion |
|---|---|---|---|
| Pillar One | | 0.2%-0.5% | 5-12 |
| Pillar Two | Direct revenue gains | 0.9%-1.7% | 23-42 |
| | Additional gains from reduced profit shifting | 0.8%-1.1% | 19-28 |
| | Total Pillar Two | 1.7%-2.8% | 42-70 |
| Total Pillar One and Pillar Two | | 1.9%-3.2% | 47-81 |
| US GILTI regime | | 0.4%-0.8% | 9-21 |
| Total, including GILTI | | 2.3%-4.0% | 56-102 |

(Source) OECD “Tax challenges arising from the digitalisation of the economy: Economic impact assessment” webinar presentation material, October 20, 2020[29] (p. 8)

## *VI-2 Implication of empirical study on profit shifting of various countries*

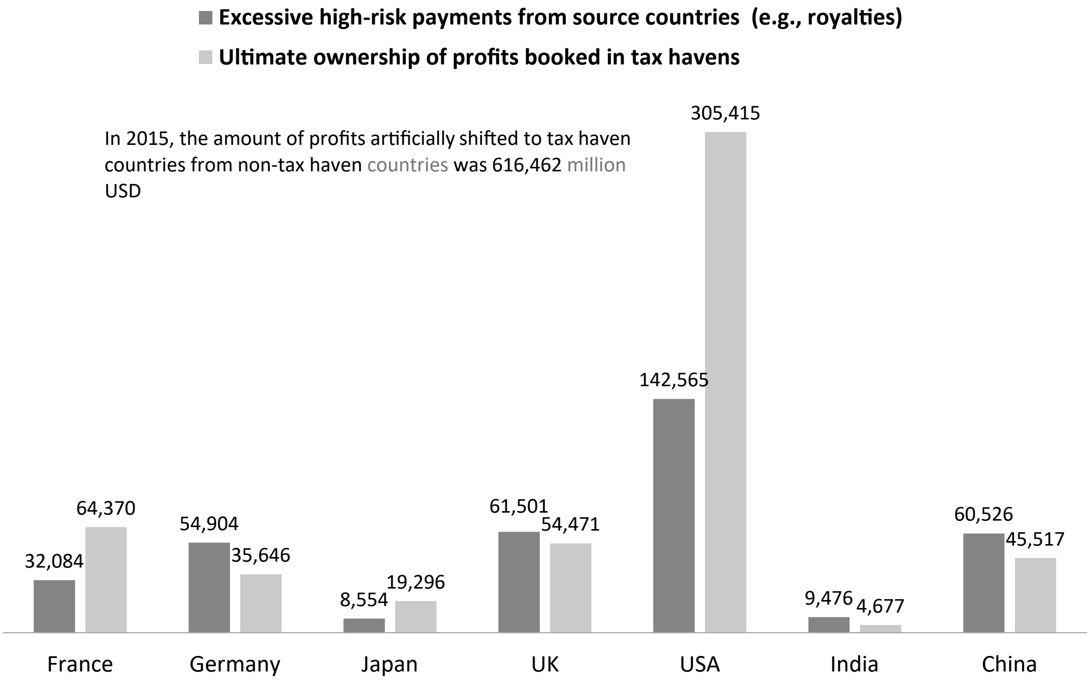
New measures consist of countermeasures from the country of residence and countermeasures from the source country. Which measures are more effective for the maintenance of tax base and competitiveness of each country?

In this regard, the country-specific estimates of the shifting of profits to tax havens in a study conducted by Tørsløv, Wier, and Zucman (2020) provided useful insights. Suppose the amount of profits owned by resident shareholders of Country A is larger than the amount of profits shifted from that Country A, then, for the Country A, it may be more beneficial to adopt countermeasures from the perspective of country of residence.

According to Tørsløv et al. (2020), the total amount of profits that were shifted to the tax haven from non-tax havens was 616.4 billion USD in 2015 (see Figure 7). Half of the global total of shifted profits is owned by the US shareholders, but the profit shifted from the United States to tax havens are one-fourth of the global total. Japan and France also show the same tendency, i.e., the amounts of profits owned by Japanese or French shareholders are greater than the amount of profits shifted from these countries. This might imply that, for Japan, the United States, and France, it might be beneficial to adopt new measures for country of residence (i.e., income inclusion rule) for protecting the tax base and improve compet-

29 https://www.oecd.org/tax/beps/economic-impact-assessment-webinar-presentation-october-2020.pdf

Figure 7. Allocation of the profits shifted to tax havens in 2015 (estimation)




(Source) Tørsløv, Wier, and Zucman Missing (2020) Online Annex Table C4

itiveness.

However, the best answer might not be a dichotomy between resident country measure or source country measure. According to Sullivan (2020, pp. 868-870), in the United States, shifting of profits through payment of royalties within a multinational corporation is enormous. The amount of payments from the US to affiliates in tax haven countries has increased by more than 400% from 2004 to 2014. Affiliates in Ireland (tax haven) receive half of the global receipts. The cost of R&D borne by the Irish affiliates was only 2.8 billion USD, and therefore they receive 12 times more royalties than the amount they spent on R&D. This ratio is only 19% for non-tax haven countries.

## VII. Conclusion: A new corporation tax for the 21st Century

Zucman (2015, Chapter 5) argued that, in essence, the corporation's income taxation is in critical condition because of the manipulation of books by MNEs, and called for the radical departure from separate accounting and the adaption of taxation of MNEs on consolidated profits. This proposal, taxing excess profits of MNEs on consolidated profits, was a quite accurate prediction made four years preceding the publication of new measures in 2019.

"We need a radical reform of corporate taxation. A promising solution consists in starting from the global, consolidated profits of firms, which cannot be manipulated. To attribute profits to the different countries necessitates the use of an apportionment formula, perhaps some combination of sales, capital, and employment.”

The conventional international taxation principle is based on the separate accounting and arm’s length principle. However, multinational corporations are free to decide which companies (likely to be in tax havens) in the group should book intangible assets that generate large profits (excess profits) within the group. Also, assessing the taxable value of intangible assets is difficult. The arm’s length principle has become a kind of “black box, “which allows multinational corporations to manipulate accounting books and avoid taxes. Tax payment costs and execution costs are also increasing.

The three new measures agreed upon by the BEPS inclusive framework in 2020 are for taxing excess profits of MNEs and for ensuring MNEs to pay global minimum tax at an internationally agreed level. Although the final picture cannot be foreseen at this time, it is an event that can be said to be the sprout of corporate tax in the 21st century.

A proposal, made by the US in December 2019, to make the application of Amount A (unitary taxation) optional to taxpayers was received with surprise. In the background, it may be possible that large multinational corporations with political influence, who have been benefited from shifting of profits and minimizing or avoiding taxes, wished to preserve these opportunities for profit shifting through exploitation of the arm’s length principle. It is not surprising that some multinational corporations, other than those in the United States, including Japan, might have groups that (inwardly) agree with these ideas.

Today, with nearly 140 countries, including the tax haven countries, in the international community participate in BEPS Inclusive Framework, a platform that was not available a decade ago. Based on the new framework for multinationalism and administrative cooperation, countries can design and enforce tax systems more freely without being bound by tax sovereignty and administrative jurisdiction limitations. The international community should not waste this opportunity.

In exchange for their tax sovereignty, tax haven countries have been depriving tax base from high-tax countries that need money for the welfare system for their citizens, and forcing non-haven countries to participate in tax competition (a race to cut corporation tax rates). It is time to change and revert such a vicious trend.

The true national interest must be to allow each country to regain true tax sovereignty and determine the tax rate and the size of corporate tax, without being wary of transferring profits to tax havens.

Confidentiality of information is another major feature of tax haven. A number of important progress has been made in the last decade (e.g., FATCA, CRS automatically exchange information, etc.). Next, countries should recover the sovereignty in corporate taxation that has been stolen from them.

## Appendix 1-1 Examples of profit shifting court cases in Japan where tax administration lost

| Judgment | Methods used to avoid tax in Japan | Taxation Agency Claims and Court Judgments | Tax haven countries involved |
|---|---|---|---|
| Japan-Ireland tax treaty case.<br>Tokyo High Court October 29, 2014 | Conduit arrangement<br>Tax treaty<br>Tokumei-Kumiai (TK partnership) | The Cayman corporation's branch in Japan (the proprietor of TK partnership. plaintiff) paid a large amount of profit from the bad debt business in Japan to the Irish corporation (anonymous partner of the TK partnership) as profit distribution of the TK partnership contract. According to the other contract, 99% ofthe distributed profits of the Irish corporation was paid to the Bermuda affiliate.<br>The NTA (National Tax Agency) argued the beneficial owner of the distribution is Bermuda affiliate of the taxpayers group. Thus, ignored the application of Japan-Ireland tax treaty and imposed withholding tax.<br>The court dismissed the NTA's allegation, saying that the application of tax treaties cannot be excluded unless the provisions of the treaty have clear grounds. | Ireland<br>Cayman Islands<br>Bermuda |
| World Family case<br>Tokyo District court<br>April 11, 2017 | High-value intangible (Disney characters)<br>Transfer pricing transactions with tax haven affiliate. | The NTA applied arm's length principle to educational goods for children that use cartoon characters (with adjustments) imported from the MNE group's Bermuda affiliate. A secret-comparable method was used. The court dismissed the NTA's arm's length analysis by saying that there is an "extremely large difference" between the characters used in the comparable transaction the NTA argued and the Disney characters which has uncomparable appeal to customers. | Bermuda |
| Universal Music case<br>Tokyo District Court June 27, 2019 | Debt-push down (by a series of transactions)<br>(Japanese subsidiaries' retained earnings in 2008 was 23.6billion yen. As a result of executing the debt-push down scheme, financial statements for 2009 showed a deficit of 81.8 billion yen. | The NTA argued that (1) such a series of transactions with contrived nature was only possible among a group corporations, and (2) the series of transactions had no substantial economic impact on the controlling relationship or business operations within the group. The NTA made adjustments by invoking Article 132(1), a targeted general anti-avoidance rule (TAAR) for family corporations.<br>The court dismissed the NTA's argument by saying, in order to deny for tax purposes the series of transactions, it has to be proven that there is no economic benefit apart from the reduction of tax burden. | Netherlands,<br>UK,<br>Bermuda |
| Ichijo-constructer case<br>Nagoya District Court<br>September 29, 2005 | Transfer of intangible property (know-how) to Singapore affiliate (HRD)<br>Royalties for the use of the know-how paid by Japanese customers was booked at the Singapore affiliate. | The NTA argued that the transfer of intangible property to a Singapore affiliate (which the NTA considered a shell corporation) was fictitious.<br>The court dismissed the argument of the NTA by saying that : (1)HRD"has the substance of human and physical facilities and invests a large amount of money", etc., (2) In order to decide the owner of the know-how, bearing of the cost and maintenance of researchers necessary for the development of the R&D are important, but business purposes and other factors are also relevant. The court concluded that the contract could not be considered as fictitious. | Singapore |

(Source) Author

## Appendix 1-2 Implications of the Judgement of the Supreme Court, October 29, 2009[30]

The CFC rule as an expansion of residence jurisdiction and countermeasure for foreign harmful tax measure

(Summary of the case)

The NTA has applied the CFA tax system and added the retained earnings of Singapore subsidiary A of Japanese corporation X to X's profits. Taxpayers argued that Singapore Subsidiary A does not have PE in Japan. Under Article 7 Paragraph of Japan-Singapore tax treaty, such taxation on retained earnings of Singapore Subsidiary A is restricted.

(Issue)

Is taxation on retained earnings of a subsidiary (foreign corporation) violated tax treaty even if, in the form, it is taxable on a domestic corporation?

(The CFC rule as an expansion of residence jurisdiction)

| | |
|---|---|
| Aim of the CFC rule (countermeasure) | The CFC rule is established as a countermeasure for tax systems of other countries that may have a detrimental effect on the fairness and neutrality of tax burden in one's own country. (p.3) |
| Taxable profits of the CFC rule | Under the CFA rule, a foreign subsidiary's retained income is regarded as the amount of income of the parent company (resident of Japan) and taxed. (p.4) |
| Jurisdiction of tax | (Country of residence ) The CFC rule is the taxation of residents, and it is a countermeasure for foreign tax systems that have a harmful effect on the tax system in Japan. The establishment of such a rule belongs to the core of national sovereignty. (p.3) |
| | (Country of source) The CFC rule has the substantive curving our and the rules for the avoidance of double taxation, and it is a rational system as a whole. Therefore, it does not hinder the source country's taxation right (p.6-7) |
| Meaning of the substantive carve-out | It will protect the economic exchange between Japan and Singapore.<br>The CFC rule has the risk of unreasonably hindering the overseas expansion of the domestic corporation.<br>The substantive carve-out is for non-application of the CFC-rule where foreign subsidiary has offices, stores, factories, and other fixed facilities and has substance in Singapore. (p.6-7) |
| Relationship with the tax treaty | Domestic countermeasures for resident taxpayers will not be hindered by the provisions of tax treaty unless there is "clear provisions" in tax treaties, etc. (p. 3) |

[30] https://www.courts.go.jp/app/files/hanrei_jp/118/038118_hanrei.pdf (in Japanese).

## Appendix 2 Items for consideration and recommendations for designing rules for applying the new measures (main items)

This Appendix proposes items for consideration and recommendations for designing rules for applying the new measures

1 Starting points

Below are the characteristics, policy goals, and the tax-law structure of the new measures discussed in this paper

(1) Characteristics and policy goals of new measures:

- Aim to deter and counteract tax base erosion (this may include the case where tax base erosion was created by tax avoidance)
- Aim to tax, in substance, profits of foreign member of the MNEs
- Aim to tax excess profits of multinationals
- Aim to reduce pressure on tax competition (reduction of corporate tax rates)

(2) Structure of the measures

| Measures | In substance<br>(what the measure is targeting at) | In form<br>(how tax law will be applied) |
|---|---|---|
| Amount A (new taxing right) (Note 2) | Taxation of the profits of foreign member of the MNEs | Taxation of non-resident member of the MNEs (impose tax) |
| Income inclusion rule (Note 1) | Taxation of the profits booked at the foreign member of the MNEs in tax haven | Taxation of resident member of the MNEs at a minimum level (by current year inclusion of income) |
| Undertaxed payment rule (Note 1) | Taxation of the income of foreign recipient of the MNE in tax haven | Taxation of resident member of the MNEs at a minimum level (by denying deduction) |

(Note 1) The income inclusion rule and undertaxed payment rule are dealing with the remaining BEPS issues, and it is clear that they aim to counteract and deter tax base and erosion.[31]

[31] OECD (2020c, p 5) " Pillar One is focused on nexus and profit allocation whereas Pillar Two is focused on a global minimum tax intended to address remaining BEPS issues."

(Note 2) The Amount A is not designed as a provision to deal with contrived arrangements. However, it is designed to capture the excess profits of the MNEs that, in the digitalization of the economy, can engage with consumers in a market jurisdiction from a remote location.[32] Therefore, it too is a measure to protect the tax base of the market jurisdictions. The UK "Diverted Profits Tax" may be an example of a measure with the policy aim to deal with arrangements that aim to erode the UK tax base.[33]

2 Hallmarks for identifying tax base erosion

The new measures are not for "calculating the correct amount of tax" (i.e., anti-tax avoidance rule) but for counteracting tax base erosion. It is, therefore, necessary to be able to say that "tax base erosion exists." Some of the convincing factors would be the size of the revenue, profits, or payment that affect the tax base. Dealing with de minimis cases would not justify the new measures create administrative difficulties.

(Illustration of hallmarks of tax base erosion)

M: Monetary threshold: consolidated amount of revenue, profits, or deductible payment is large

L: Low tax: the retained earning or deductible payment is subject to no or little tax burden

P: Profitability: high profitability of the MNEs and low effective tax rate.

3 Specific recommendation for each measure

Summary of the recommendations

| | Hallmark for identifying tax base erosion | Comments |
|---|---|---|
| Amount A | M: Monetary threshold is already incorporated (7.5 billion euros?)<br>H: High profitability test (EBIT 10%?) is already incorporated | |
| Income inclusion rule | L: Global blending would be sufficient (Note 2)<br>Curving out for substantive activity would not be needed | Income inclusion rule expand residence tax jurisdiction (Note 3)<br>OECD (2020c) proposes a new type of carve-out, i.e., "formulaic approach" (Note 4) |
| Undertaxed payment rule | M: De minimimis rule should be added (Note 5) | For example, excessive interest payment rule in Japan is applicable has a de minimis rule (20 million yen). |

32 OECD (2020b) para 145.

33 HM Revenue&Customs (2018, overview). "Specifically DPT aims to deter and counteract the diversion of profits from the UK by large groups that either: (i) seek to avoid creating a UK permanent establishment that would bring a foreign company into the charge to UK Corporation Tax, or, (ii) use arrangements or entities which lack economic substance to exploit tax mismatches either through expenditure or the diversion of income within the group.

(Note 1)
M: Monetary threshold test
L: low tax test
H: high profitability test

(Note 2) As discussed above, it is appropriate that the purpose of the system is to counter global tax-based erosion due to the transfer of profits of multinational corporations. Therefore, in order to evaluate the level of tax borne by the MNEs, global blending would make more sense than country or regional blending. This will contribute to the practicality and simplification of the rule.

(Note 3) CFC (controlled foreign corporation) rules expand residence tax jurisdiction to foreign residents.[34] A question might therefore arise that, such expansion of residence tax jurisdiction should accompany certain “carve-out” for excluding entities with, for example, substantial infrastructure and workforce. The income inclusion rule would tax, in effect, profits of foreign affiliates that do not have permanent establishment in the country of residence of the shareholders. Such a carve-out might be considered necessary in order to preserve taxation right of source jurisdiction, avoid breaching tax treaty obligations, avoid discouraging legitimate outbound investment[35]. The recommendation of this paper is such carve-out (may be optional but) is not necessary because income inclusion rule is not for calculating correct amount of tax but for protecting tax-base[36]. Substantive-carve out might accelerate outward investments, undermine a level playing field, and, as Keen (2019, p 22) argued, may invite inefficient “tangible” investment in order to avoid the application of the Income Inclusion Rule.

(Note 4) OECD (2020c) proposed “Formulaic substance-based carve-out.” The carve-out amount is equal to the sum of the payroll component and the tangible asset component. (paras paragraph 332-370)

(Note 5) Add monetary threshold would contribute to further simplify the application o the rule and limit the application only where tax base erosion is identified: A de minimis rule should be added in order to ensure overkilling or the rule.

---

[34] See Avi-Yonah (2004, p. 9) at V-2 (2) above.

[35] Under the CFC rule, retained profits of foreign subsidiary (which has no Permanent Establishment in Japan) is taxed at its shareholder. In a court case (The judgement of the Supreme court, 1st Petty Bench, October 29, 2009) in which whether the application of Japan’s CFC rule breach treaty obligation, the court admitted there may be the room to question the possibility that the CFC rule as a substantial violation of the treaty. However, in Japan’s tax law, if foreign subsidiary has the substance of an independent company and has sufficient economic rationality to carry out business in the country where it is located, CFA rule will not be applied.Therefore the court said that the Japan’s CFC rule is reasonable and not breaching the treaty obligation. Judgement of Supreme Court (1st petty bench), October 29, 2009, https://www.courts.go.jp/app/files/hanrei_jp/118/038118_hanrei.pdf. (See Appendix1-2)

[36] A comment submitted by the BEPS monitoring group (a global network of independent researchers on international taxation) at the OECD public hearing in December 2019 stated as follows: (1) welcomed the GloBE proposal as “a measure would reduce the incentive for taxpayers to engage in profit shifting, establish a floor for tax competition among jurisdictions, and act as a brake on the ‘harmful race to the bottom on corporate taxes, which risks shifting the burden of taxes onto less mobile bases” (p. 2); and, (2) opposed the introduction of carve-out” In our view, carve-outs are not appropriate, as explained in section 1.1, for fundamental policy reasons. In addition, any carve-outs would increase complexity, add compliance costs especially for tax administrations, and create undesirable incentives for MNE lobbying for tax preferences. Hence, they would defeat the aims of the GloBE proposal.” (p. 14) https://www.oecd.org/tax/beps/public-comments-received-on-the-global-anti-base-erosion-globe-proposal-under-pillar-two.htm.

## Appendix 3 OECD/G20 Discussions (Timeline)

2013: After call from G20 to address aggressive tax planning, the BEPS Action Plan is launched (with digitalisation as key component)

2015: Final BEPS Action Reports are released, including actions on BEPS and VAT, but does not address broader direct tax challenges arising from digitalisation

2018: Interim Report is released with further analysis of the broader direct tax challenges, but no agreement on solution

January 2019: Policy note released, proposing a two-pillar approach as foundation for a consensus-based solution to broader tax challenges

May 2019: Adoption of a Programme of Work (PoW) to develop a solution for each Pillar

January 2020: Inclusive Framework adopts Outline of a Unified Approach on Pillar One, and a Progress Note on Pillar Two – Adoption of the “new measures” discussed in this paper. OECD (2020a)

July 2020: G20 Finance Ministers calls on Blueprints to be delivered in October 2020

October 2020: The Inclusive Framework on BEPS agreed and released ‘Blueprints’ on Pillar One and Pillar Two. The new deadline is set by mid-2021.—OECD (2020b), OECD (2020c)

・January 2021: OECD Consultation on International Tax Reform Blueprints

・January 2021: OECD/G20 Meeting of the Inclusive Framework on BEPS[37]

(Source) OECD TAX TALKS (12 October 2020) p. 9 https://www.oecd.org/tax/oecd-tax-talks-presentation-october-2020.pdf, and 11th meeting of the OECD/20 Inclusive Framework on BEPS（January 2021）

## References

Aaronson, Grahah QC. (2011), GAAR Study: A study to consider whether a general anti-avoidance rule should be introduced into the UK tax system.

Avi-Yonah, Reuven S. (2004), “International Tax as International Law”, *Law & Economics Working Papers, University of Michigan Law School.*

Avi-Yonah, Reuven S. (2016), “Full circle? The Single Tax Principle, BEPS, and the New US Model.” *Global Tax’n 1, pt.1 (2016) pp. 12-22,* https://repository.law.umich.edu/articles/1820.

Freedman, Judith (2019), “The UK General Anti-Avoidance Rule: Transplants and Lessons” *Bulletin for International Taxation June/July 2019.*

[37] Secretary-General Angel Gurria warned, in his remarks at the Inclusive Framework meeting that, if the OECD/G20 “do not deliver a solution by mid-2021, over 40 countries are considering, or will move ahead, with a Digital Services Tax (DST). He also welcomed the remark by the new US Secretary of the Treasury, Janet Yellen (at the confirmation hearings in Jan 2021). Dr. Yellen stated that the USA is committed to the cooperadive multilateral effort to working to resolve the digital taxation disputes.

GAO (2004), International Taxation: Large U.S. Corporations and Federal Contractors with Subsidiaries in Jurisdictions Listed as Tax Havens or Financial Privacy Jurisdictions. United States Government Accountability Office, https://www.gao.gov/new.items/d09157.pdf.

Gravelle, J. (2015), “Tax Havens: International Tax Avoidance and Evasion.” *Congressional Research Service Report* 7-5700.

Guttengtag, J & Avi-Yonah, R (2005), “Closing the International Tax Gap” https://repository.law.umich.edu/book_chapters/70/.

Hines, J & Rice, E.(1994) “ Fiscal Paradise: Foreign Tax Havens and American Business” *The Quarterly Jaournal of Economics,* 109 (1) pp. 149-182.

HM Revenue & Customs (2018), Diverted Profits Tax: Guidance, https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/768204/Diverted_Profits_Tax_-_Guidance__December_2018_.pdf.

Imamura, Takashi (2019), “Avi-Yonah kyoujyu no Kokusai Ho to Shite No Kokusai Kazei wo Yonde”. (Reading Avi-Yonah’s International Tax as International Law), *Houmu Kenkyu Nihon University law review* (in Japanese).

IMF (2019), “Corporate Taxation in the Global Economy” *Policy Paper No. 19/007,* International Monetary Fund, https://www.imf.org/en/Publications/Policy-Papers/Issues/2019/03/08/Corporate-Taxation-in-the-Global-Economy-46650.

Ito, Kimiya (2015), *Kokusai sozeihou ni okeru teishiki haibunhou no kenkyuu* (A study on the e of formula method in international tax law) Chuo Keizai sya, Tokyo (in Japanese).

Kaneko, Hiroshi (2019), *Sozeihou* (tax law) Koubundo, Japan (in Japanese).

Keen, Michel (2019), “Corporate Taxation in the Global Economy” *Sozei Kenkyuu,*August 2019 (in Japanese).

Masui, Yoshihiro; Miyazaki, Yuko (2019), *Kokusai Sozei Hou* (International Tax law).Ver. 4, Tokyo Daigaku Syuppankai, Tokyo (in Japanese).

Monsenego, Jérôme (2019), “The Dependent Agent PE Rule in the French Google Case: A Case for a Google Tax?” *International Taxation in a Changing Landscape,* Kluwer Law International, 2019, p. 205-219.

Morinobu, Shigeki (2019), Degtal keizai to zei (Tax and digitalisation of economy), Nihon Keizai shinbunsya, Japan. (in Japanese).

Nakazato, Minoru (2015). “BEPS Projects ha docomade jitsugen sareruka” (To what extend the BEPS projects will accomplish? *Jurist* August 2015 (in Japanese).

OECD (1998), Harmful tax competition: An Emerging Global Issue, OECD Paris.

OECD (2015), Measuring and Monitoring BEPS, Action 11 - 2015 Final Report, OECD Paris.

OECD (2019a) *Public consultation document: Secretariat Proposal for a “Unified Approach” under Pillar One,* OECD, Paris, https://www.oecd.org/tax/beps/public-consultation-document-secretariat-proposal-unified-approach-pillar-one.pdf.

OECD (2019b), *Public consultation document Global Anti-Base Erosion Proposal (“GloBE”)*

*(Pillar Two)* OECD Paris, https://www.oecd.org/tax/beps/public-consultation-meeting-global-anti-base-erosion-proposal-pillar-two-9-december-2019.htm.

OECD (2020a), Statement by the OECD/G20 Inclusive Framework on BEPS on the Two-Pillar Approach to Address the Tax Challenges Arising from the Digitalisation of the Economy – January 2020, OECD/G20 Inclusive Framework on BEPS, OECD, Paris, www.oecd.org/tax/beps/statement-by-the-oecd-g20-inclusive-framework-on-beps-january-2020.pdf.

OECD (2020b), Tax Challenges Arising from Digitalisation – Report on Pillar One Blueprint: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project, OECD, Paris.

OECD (2020c), Tax Challenges Arising from Digitalisation – Report on Pillar Two Blueprint: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project, OECD Paris.

Oka, Naoki (2019a), "The Digital Economy and Our Vanishing Tax Base" https://www.tkfd.or.jp/en/research/detail.php?id=666 (accessed 2020-10).

Oka, Naoki (2019b). "Toward an International Agreement to Tax the Digitalized Economy: Deciphering the BEPS Policy Note," https://www.tkfd.or.jp/en/research/detail.php?id=675 (accessed 2020-10).

SEO Amsterdam Economics (2018) *The Role of Investment Hubs in FDI, Economic Development and Trade,* https://investmentfacilitationforum.org/wp-content/uploads/2018/05/The-Role-of-Investment-Hubs.pdf.

Shiga, Sakura (2011), *Theory and practice of international taxation* (Kokusai-sozeiho no riron to jitumu), Minji Zeiho Kenkyuukai, Tokyo Japan (in Japanese).

Sullivan, Martin A. (2020a), "U.S. Multinationals book at least $230 Billion in Tax Havens" *Tax Notes International*, January 6, 2020. pp. 11-17.

Sullivan, Martin A. (2020b), "Are Royalties Paid to Tax Havens Indicators of BEPS?" *Tax Notes Federal*, February 10, 2020.

Surry, Stanley (1978), "Reflections on te Allocation of Income and Expenses Among National Tax Jurisdictions" *Law & Policy International Business* , p. 414.

Tørsløv, Thomas; Wier, Ludvig; and Zucman, Gabriel (2020). *The Missing Profits of Nations*, http://gabriel-zucman.eu/missingprofits/ (accessed 2020-10).

UNCTAD (2015) *World Investment Report 2015: Reforming international investment governance,* United Nations Publication, Geneve, Switzerland, https://worldinvestmentreport.unctad.org/wir2015/.

Vann, Richard J. (1998). *International Aspects of Income Tax. Tax Law Design and Drafting*, volume 2; International Monetary Fund: 1998; Victor Thuroni, ed., Chapter 18.

Zimmer, Frederik (2002). 87a: "Form and substance in tax law IFA" 2002 General Report.

Zucman, Gabriel (2015). *The Hidden Wealth of Nations* . University of Chicago Press. Kindle.