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OECD'S GLOBAL TAX REFORM 2021

In connection with the OECD's Base Erosion and Profit Shifting Project ("**BEPS**"), a group of 140 countries have made commitments to radically modify the international tax system.

Under BEPS Action 1, Pillar 1, it was agreed to adopt new profit allocation and *nexus* rules so that 25% of large multinational enterprises' residual profits are redistributed to the countries in which consumers are located. Market jurisdictions would then have a taxing right over those residual profits. While this is a major shift away from the requirement for a physical *nexus* to confer jurisdiction to tax, in today's digital world with its absence of physical presence, there is a principled basis for shifting to a market-based approach.

What is more troubling, however, is Pillar 2, under which the group of 140 countries seeks to impose a 15% minimum corporate tax on large multinational enterprises (having annual revenues of at least €750 million). In the case of Canada, this would mean that a Canadian-based MNE would face an additional 15% tax on top of its regular corporate tax of 26.5%, to the extent that any foreign affiliate faced a local income tax of less than 15% in its home country.

As a practising tax lawyer and former Tax Policy Officer in the Department of Finance, Canada, I am very troubled by the endorsement by the Government of Canada of the OECD's initiative to implement Pillar 2.

The following information from the OECD itself refutes the claim that Canada (or for that matter any other member of the OECD) is suffering the loss of corporate tax revenue resulting from a so-called "race to the bottom", which purports to justify this new tax.

The OECD's global corporate tax statistics database reports that average corporate tax revenues have risen from 12.3% of total revenues in 2000 to 15.3% in 2018. Corporate taxes collected as a per cent of GDP have increased from 2.7% to 3.2%- a gain of 20%.

For over 46 years, Canadian international tax policy has been to foster capital export neutrality, so that an expanding Canadian firm can make its business decisions based on good business practices and not on lower taxes. The method for doing so was the establishment of an international tax system anchored in the creation of a notional account called "exempt surplus" in a foreign affiliate that carried on an active business in a country with which Canada has a tax treaty or a tax information exchange agreement. If that corporate group paid less tax on foreign earnings than would have been the case if it had only operated domestically in Canada that was seen as a positive result, permitting the Canadian-based multinational to compete and expand.

The result would be increasing wealth for the Canadian parent, its shareholders and other stakeholders in Canada.

This system also recognized that good international tax policy tries to reduce barriers to entry, and so if a Canadian-based MNE wished to expand into Europe, Canada would not impede its decision to run its active foreign affiliate through Ireland where the corporate tax rate was 12.5% versus Germany where the corporate tax rate was 30%.

However, by imposing a minimum tax of 15% on this corporate group, the Government of Canada would be launching a direct assault against that positive international tax policy, without a justifiable rationale, as demonstrated by the OECD’s own statistics.

Such a policy constitutes a “soak the rich” tax grab, in the absence of real world, principled, fiscal policy justification, and would cause serious harm to Canada’s corporate sector, to the detriment of all Canadians.

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