G7 Global Corporate Tax Deal

Why in news?

- The Group of Seven (G7) countries have backed the proposal to impose a common global corporate tax.
- It is aimed at preventing multinational businesses from evading taxes and also squeezing the havens which attract tax evaders due to the low-rate jurisdictions.

What are the decisions taken?

- The tax proposal endorsed by the G7 countries (US, UK, Germany, France, Canada, Italy and Japan) has two parts.
- The agreement made will now be discussed in detail at a meeting of G20 financial ministers and central bank governors in July 2021.
- **First part** - Countries around the world should tax their home companies' overseas profits at a rate of at least 15%.
- This 15% of global minimum corporate tax would deter the practice of using accounting schemes to shift profits to a few very low-tax countries.
- Often, these tax havens are the Caribbean Islands such as Bahamas or British Virgin Islands.
- Or at times, it is countries like Ireland where the corporate tax rate is as low as 12.5%.
- **Second part** - This allows countries to tax a share of the profits earned by companies "that have no physical presence but have substantial sales."
- For instance, this could be though selling digital advertising.

What is the rationale?

- The G-7 statement echoes an earlier US proposal.
- The US had urged the world’s 20 advanced nations to move in the direction of adopting a minimum global corporate income tax.
- It urged countries to tax part of the earnings of the largest and most profitable companies if they are doing business within their borders.
- It also supported awarding countries the right to tax 20% or more of profit exceeding a 10% profit margin.
- The decision to ratify the 15% floor rate follows from the same route to deal with low-tax jurisdictions around the globe.

- It is also to address the low effective rates of tax shelled out by some of the world's biggest corporations.
- These include digital giants such as Apple, Alphabet and Facebook, as well as major corporations such as Nike and Starbucks.

Who will benefit?

- The proposal works well for the US government at this time.
- The same holds true for most other countries in western Europe.
- This is true even as some low-tax European jurisdictions and some in the Caribbean rely largely on tax rate arbitrage to attract MNCs.
- The second part of the G7 proposal is expected to impact companies that rely on the digital medium to drive their profits.
- However, after the imposition of a common global corporate tax, countries are advised to revoke their respective digital services taxes.
- This is would end up benefitting the Silicon Valley companies.
- [The US considers those unilateral digital taxes to be unfair trade measures that single out the American tech companies such as Google, Amazon and Facebook.]

What are the problems with the plan?

- There are challenges in getting all countries to agree for the proposal.
- This is especially because it impinges on the right of the sovereign to decide a nation's tax policy.
- A global minimum rate would also take away a tool that countries use to push policies that suit them.
- For instance, in the backdrop of the pandemic, developing countries with less ability to offer mega stimulus packages may experience a longer economic hangover than developed nations.
- A lower tax rate is a tool they can use to alternatively push economic activity.

What does it mean for other countries?

- **China** is not likely to have a serious objection with the US call.
- But an area of concern for Beijing would be the impact of such a tax stipulation on Hong Kong.
- Hong Kong is notably the seventh-largest tax haven in the world and the largest in Asia.
- Also, China's strained relationship with the US could be a deterrent in negotiations on a global tax deal.

- **India** - In a bid to revive investment activity, the FinMin, in 2019, announced a sharp cut in corporate taxes for domestic companies to 22%.

- And for new domestic manufacturing companies, it was brought to 15%.
- The cuts effectively brought India's headline corporate tax rate broadly at par with the average 23% rate in Asian countries.
- India is likely to look into the pros and cons of the new proposal as and when it comes and the government will take a view thereafter.

Source: The Indian Express