OECD Tax Proposals - Implications for India

Why in news?

India and the majority of the members of OECD-G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS) have joined a new two-pillar plan to reform international taxation rules.

What is it about?

- The OECD recently issued a statement indicating consensus amongst 130 nations (out of 139 participants) on the two-pillar plan.
- The announcement marks the culmination of international negotiations since the BEPS (Base erosion and profit shifting) 2015 reports.
- [It has overcome the shock due to the previous US administration withdrawing from the Inclusive Framework discussions.]
- The key objective is to ensure that large Multinational Enterprises (MNEs) pay tax where they operate and earn profits.

What are the key features?

- **Pillar One** will ensure a fairer distribution of profits and taxing rights.
- This will be among countries, with respect to the largest Multinational Enterprises (MNEs), including digital companies.
- It would re-allocate some taxing rights over MNEs from their home countries to the markets where they have business activities and earn profits.
- This will be regardless of whether the firms have a physical presence there or not.
- **Pillar Two** seeks to put a floor on competition over corporate income tax.
- It does this through the introduction of a global minimum corporate tax rate.
- The countries can use this minimum tax to protect their tax bases.
- OECD further claims that the two-pillar package would provide much-needed support to governments.
- It will help those looking to raise necessary revenues to repair their budgets and their balance sheets.
- It will also invest in essential public services, infrastructure and the measures necessary to help optimize the quality of post-COVID recovery.

How will India be benefitted?

- The consensus adds much-needed certainty and stability to the international tax system.
- For India, the outcome is crucial because of its active engagement in the OECD-led deliberations.
- India had strongly advocated greater taxing rights to source or market jurisdictions.
- This has indeed been the demand of most developing countries.
- Because new-age MNEs have figured out the basis to limit their global tax incidence.
- They work through innovative tax structures and invisible presence due to digital technologies, within the framework of the current treaty principles.
- The Indian law-makers will now have to make a refined and nuanced direct taxation law.

What are the concerns for India?

- **Application** - The proposals include complex rules.
- It includes applying formulas to data relating to global business revenue of the MNE group.
- Also, its application requires real-time information sharing and conjoint implementation by the tax-authorities across the globe.
- Despite the policy level alignment of the participating countries, achieving such shared tax-assessment in practice is challenging and uncertain.

- **Limited scope** - By design, the two pillars cover a small class of taxpayers.
- - MNEs which have a global turnover above 20 billion euros and net profitability above 10% for Pillar One.
- Given that the coverage is limited, the disputes and differences in approach are likely to continue for taxing smaller players.
- **Net benefit** - Accepting the two-pillar solution brings taxing rights for the participating nations.
- Simultaneously, it implies foregoing the taxing rights for others.
- In other words, it is a trade-off, of taxing the big to spare the poor.
- This sounds wise on a progressive-taxation scale and horizontal equity ideal.
- But it may not be fair since it is not necessary that the biggest MNEs earn from India more.
- It also discounts the possibility of taxing the smaller MNEs who earn big from India.
- So, who will have the net benefits from applying these rules remains a question.
- Specifically for India, accepting the two-pillar solution implies it being under pressure.
- It has to undo its new international tax measures, particularly the

equalisation levy, and possibly modify its nexus-based Significant Economic Presence.

Source: Financial Express

Quick Fact

OECD

- OECD - Organisation for Economic Co-operation and Development
- OECD is an international organisation that works to build better policies for better lives.
- The OECD brings together Member countries and a range of partners that collaborate on key global issues at national, regional and local levels.

BEPS

- BEPS - Base Erosion and Profit Shifting
- It refers to tax planning strategies that exploit mismatches and gaps that exist between the tax rules of different jurisdictions.
- It is done to minimize the corporation tax that is payable overall.
- It is done by either making tax profits ‘disappear’ or shift profits to low tax jurisdictions where there is little or no genuine activity.
- In general BEPS strategies are not illegal. They just take advantage of different tax rules operating in different jurisdictions.

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