How the Global Tax Deal Will Impact US-India Trade Relations?

Rarely do you have global consensus between the representatives of almost 140 countries who can find common ground on most issues, let alone on taxes, a contentious issue by itself. But, earlier this month, the Organization for Economic Cooperation and Development (OECD) did just that. In their meeting on October 8, the OECD was able to bring together such a consensus on how companies around the world should be taxed in a jurisdiction where they do not have any domicile status or a physical place of doing business. Following years of intensive negotiations to bring the international tax system into the 21st century, 136 jurisdictions (out of the 140 members of the OECD/GROUP OF 20 (G20) Inclusive Framework on Base Erosion and Profit Shifting (BEPS) joined the Statement on the Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalization of the Economy.

Today, Digitization is transforming lives in many aspects as well as how our economy functions. Technology has permeated across various sectors, creating sub-sectors of technology, like FinTech, EdTech and MedTech. However, with these new sectors, technology also enabled a sense of location agnosticism and the overnight implementation of a digital world that most of us have lived in since the onset of the pandemic.

The ease of virtual operations today can create a lack of defining where a business is based out of, often leading to complexities establishing policies such as domestic or overseas tax laws. Many countries, including India, introduced unilateral measures to tax such multinational companies (MNCs).

At that point, the OECD orchestrated an inclusive framework to bring together policy makers from around the world, setting the stage for a new global taxation regime. The same technology that helped businesses break international boundaries also prompted nations to bring parity in tax laws across borders.

Four months of intense deliberations between the Group of Seven (G7) members led to an upcoming agreement on a 15 percent global minimum corporate tax. Now, a whopping136 nations, including India, have endorsed the proposal.

For India specifically, the real challenge is to get rid of the unilateral levy famously called the Equalization Levy. The levy has often been a topic of deliberation by large economies and mostly by the U.S., given that most oftech multinationals are headquartered stateside.Because of location, India and the US have often tried to come to terms on how and when profits of such companies should be taxed. With a new global consensus, there is now a pathway to mitigate these delicate conversations.

The move will also enable efficient tax planning by leading multinational companies which do businesses across multiple continents and different countries leading to more predictable and transparent tax compliance. For decades, nations around the world have used a lower tax rate as a means to attract investments from multinational corporations, with some even dropping it to a level of zero. A multilateral deal will put an end to this race to the bottom.

Specifically for India, experts say that the country should benefit by Pillar One, which hopefully will ensure a fairer distribution of profits and taxing rights among countries with respect to the largest

and most profitable multinational enterprises. It will re-allocate some taxing rights over MNEs from their home countries to the markets where they have business activities and earn profits, regardless of whether firms have a physical presence there.

Pillar Two,on the other hand, introduces a global minimum corporate tax rate set at 15 percent. The new minimum tax rate will apply to companies with revenue above EUR 750 million (USD 870 million) and is estimated to generate around USD 150 billion in additional global tax revenues annually. Further benefits will also arise from the stabilization of the international tax system and the increased tax certainty for taxpayers and tax administrations. India has various deductions and exemptions including deduction incorporated in the Indian Financial System Code and anticipates that the existing deductions and exemptions will be grandfathered.

While the world awaits contours of the tax deal, the OECD in its statement has called the deal as a win-win for all, countries, and companies. Many developing countries remain sceptical about the gains from the deal, particularly under Pillar One. India will surely ascertain its own benefit from the deal before implementing it from the targeted year 2023.

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