Pillar Two a likely revenue loser for US, JCT says

Enactment of new international minimum tax rules known collectively as Pillar Two could cost the US fisc $122 billion in lost revenue over the next decade if the rest of the world moves ahead with the agreement being led through the OECD and the US stays on the sidelines, the Joint Committee on Taxation (JCT) revealed this week in an analysis requested by congressional Republican taxwriting leaders. And even if the US does in 2025 implement the global agreement—which the Biden administration signed in 2021 and nearly 140 other countries have adopted and pledged to implement—the domestic loss still could amount to $56.5 billion, the congressional scorekeepers said.
URL: https://www.finance.senate.gov/imo/media/doc/118-0228b_june_2023.pdf

Roadblocks on Capitol Hill

Pillar Two, which calls for jurisdictions to impose a minimum tax of 15 percent and includes several backstop rules to ensure the world's largest multinational entities (MNEs) pay at least that level of tax on all income worldwide, is being advanced by many countries but has hit a roadblock on Capitol Hill.

During the 117th Congress—when the House and Senate were under Democratic control—many Democrats, led by Treasury Secretary Janet Yellen, hoped to include provisions in the Inflation Reduction Act of 2022 (P.L. 117-169), which was enacted last August with no support from the GOP, that would have brought US tax laws more in line with the new system. (They likewise sought to include similar provisions in their "Build Back Better" legislation—the predecessor to the Inflation Reduction Act that cleared the House in 2021 but ultimately stalled in the Senate.) With Democrats holding the narrowest possible majority in the Senate and unable to afford a single defection among their 50 members, however, those proposed changes proved to be a bridge too far and were not included in the legislation that was eventually signed into law.
URL: https://www.taxnotes.com/research/federal/legislative-documents/public-laws-and-legislative-history/inflation-reduction-act-of-2022-%28p.l.-117-169%29/7dybc

In the current Congress—with control of the House and Senate split between Republicans and Democrats, respectively—House Republicans, led by Ways and Means Committee Chairman Jason Smith, R-Mo., have been especially vocal in decrying the OECD agreement, and Smith has said implementation has "no path forward in Congress."

Revenue scenarios

Pillar Two does not require every jurisdiction to implement a Pillar Two-compliant minimum tax, but if the US does not do so, affected US-based MNEs will be subject to new taxes in other countries rather than in the US. This dynamic accounts for the difference in the JCT's estimates this week: according to the committee's analysis, the US will lose significantly more revenue if it stays outside the system while other countries adopt it.

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“The implementation of Pillar Two in a significant number of jurisdictions will affect federal tax receipts in two ways,” the JCT analysis states, “first, by countries other than the United States taxing foreign-source income (mostly of [controlled foreign corporations]) that might otherwise be taxed in the United States; and second, by taxing US-source income (mostly of US corporations, whether US MNEs or US subsidiaries of foreign MNEs).”

Under a scenario in which Pillar Two is implemented only by the approximately 45 countries that have already enacted or proposed legislation to do so (including Australia, Canada, Japan, South Korea, the UK, and all the EU member nations), the JCT provided an extremely broad range of revenue effects on the US, based on projected corporate profit-shifting responses. At the lower bound, the US could lose $174.6 billion over the next decade, while at the upper bound, the domestic gain could be $224.2 billion. Using a modified baseline that falls in the middle of this range, the JCT then looked at the estimated impact of the rest of world joining implementation, both with and without the US.

GOP taxwriting leaders react

In a June 20 statement responding to the JCT analysis, Ways and Means Chairman Smith and the Senate Finance Committee’s top Republican, Mike Crapo of Idaho, called Pillar Two a “lose-lose deal negotiated by the Biden administration.”

“Not only does the OECD’s global tax code undermine US sovereignty to enact its own tax policy and vault foreign countries ahead by encouraging a subsidy race to the bottom, but this ‘America Last’ policy shifts jobs and—as this analysis makes clear—tax revenues out of the United States,” the GOP taxwriting leaders said.

Republicans have been particularly critical of Pillar Two’s final backstop rule some jurisdictions plan to enact, known as an undertaxed profits rule (UTPR). In late May, the 25 GOP members of the Ways and Means Committee introduced legislation that would impose retaliatory—and annually increasing—taxes on the US income of foreign entities and individuals from countries implementing a UTPR or similar measure. (For prior coverage, see *Tax News & Views*, Vol. 24, No, 19, May 26, 2023.)
URL: https://gop-waysandmeans.house.gov/wp-content/uploads/2023/05/Defending-American-Jobs-and-Investment.pdf
URL: https://dhub.blob.core.windows.net/dhub/Newsletters/Tax/2023/TNV/230526_2.html

Among the jurisdictions currently planning to adopt a UTPR, generally beginning in 2025, are Canada, Switzerland, and the EU.

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