TAX INCENTIVES AND THE GLOBAL MINIMUM TAX

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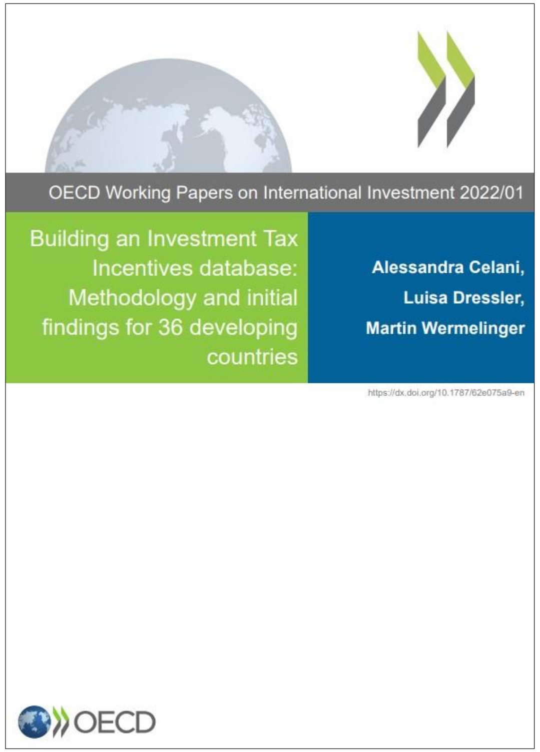
DES POLITIQUES MEILLEURES POUR UNE VIE MEILLEURE

OECD INVESTMENT TAX INCENTIVES DATABASE

OECD Investment Tax Incentives Database

- **OECD Investment Tax Incentives Database** compiles information on corporate income tax incentives.
  - Currently covers **48 developing countries**
- For each tax incentive, it includes information on:

Design features	Eligibility conditions	Governance
How does the incentive reduce taxation?	Which investors and projects qualify?	How is the tax incentive governed?


OECD Working Papers on International Investment 2022/01
Building an Investment Tax Incentives database: Methodology and initial findings for 36 developing countries
Alessandra Celani, Luisa Dressler, Martin Wermelinger
https://dx.doi.org/10.1787/62e075a9-en
OECD

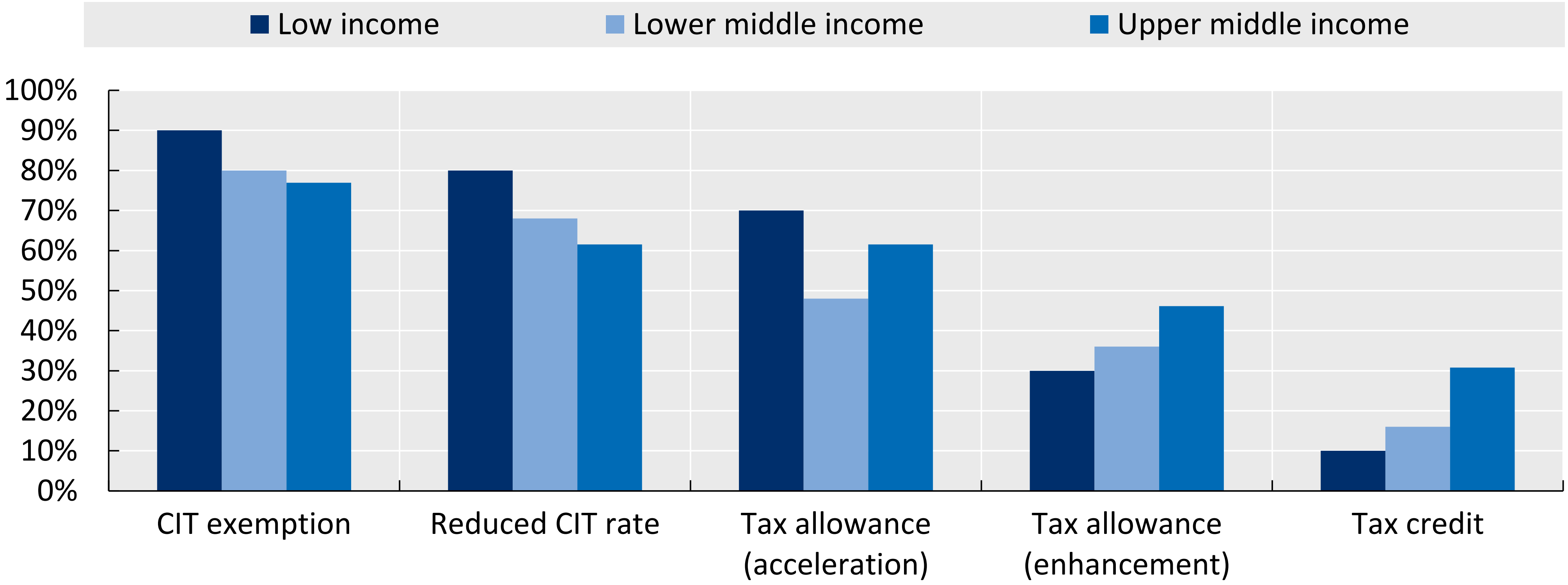
- Countries provide a range of different types of tax incentives with different design features and different targeting strategies

Source: Celani, A., L. Dressler and M. Wermelinger (2022), "Building an Investment Tax Incentives database: Methodology and initial findings for 36 developing countries", OECD Working Papers on International Investment, No. 2022/01, OECD Publishing, Paris, https://doi.org/10.1787/62e075a9-en.

Widespread use of tax incentives

Especially among developing and emerging economies

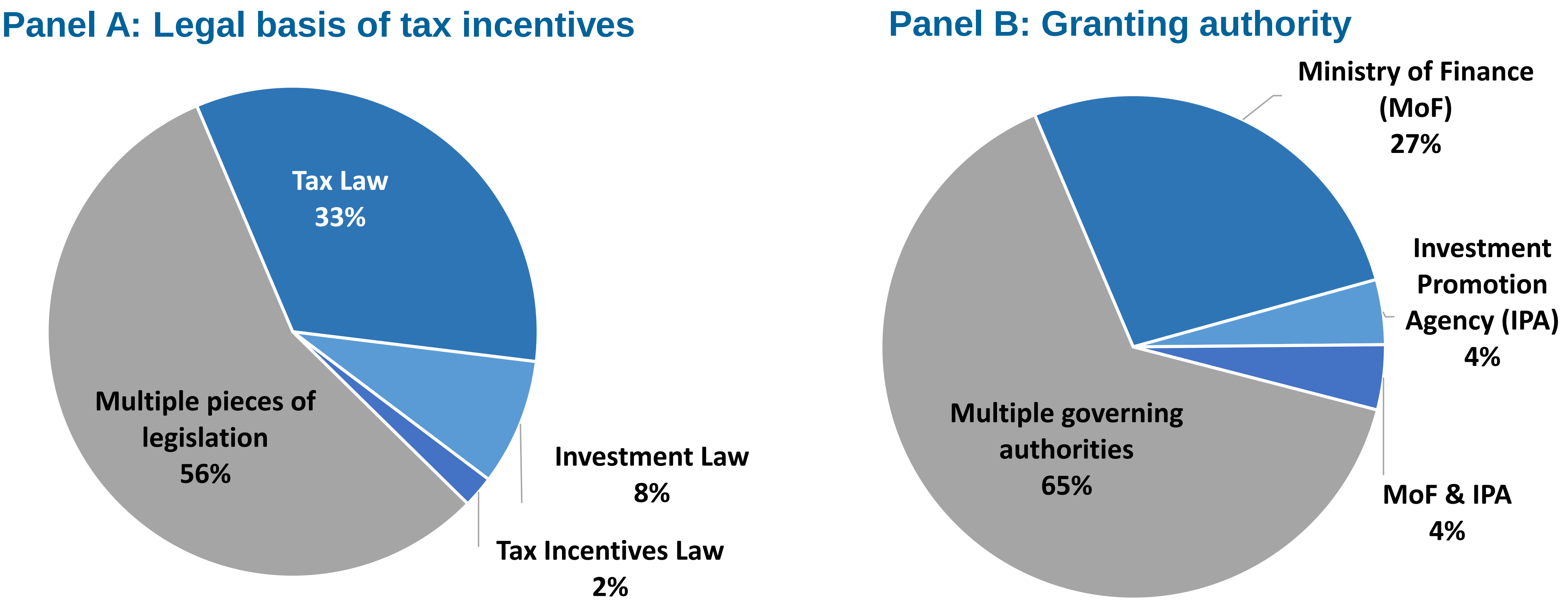
Tax exemptions, reduced rates and accelerated depreciation are the most commonly used instruments among developing economies



Source: [OECD Investment Tax Incentives database](), July 2022 version, based on information for 48 countries (9 low income, 26 lower middle income and 13 upper middle-income countries) and 387 entries of CIT incentives available on 1 January 2021.

Governance of investment tax incentives is complex

Investment tax incentives are often legislated through several laws and granted by multiple authorities



Source: [OECD Investment Tax Incentives database](), July 2022 version, based on information for 48 countries, i.e. 427 corporate income tax incentive entries.

TAX INCENTIVES & THE GLOBAL MINIMUM CORPORATE TAX

OECD Report on Pillar Two and Tax Incentives

- Pillar Two will be a **‘game-changer’ for tax incentives**
- Where a tax incentive reduces **a firm’s effective tax rate (ETR) below 15%, top-up tax will be due**
- This means that countries need to **review and evaluate their incentives**
- This report outlines **options for action** for policymakers with a **focus on developing countries**

Pillar Two

Overview

Most recent estimates are that Pillar Two would raise more than **USD 150 billion** in additional annual revenues

GloBE rules

- Domestic law provision
- Common approach
- Based on Financial Accounts
- 15% effective tax rate test
- Applies on a jurisdictional basis
- Substance-based income exclusion
- Co-ordination rules

Subject to tax rule

- Treaty provision
- Can be requested by developing countries
- Base eroding payments
- 9% Adjusted nominal tax rate test
- Applies on a transactional basis
- Covered taxes for GloBE purposes

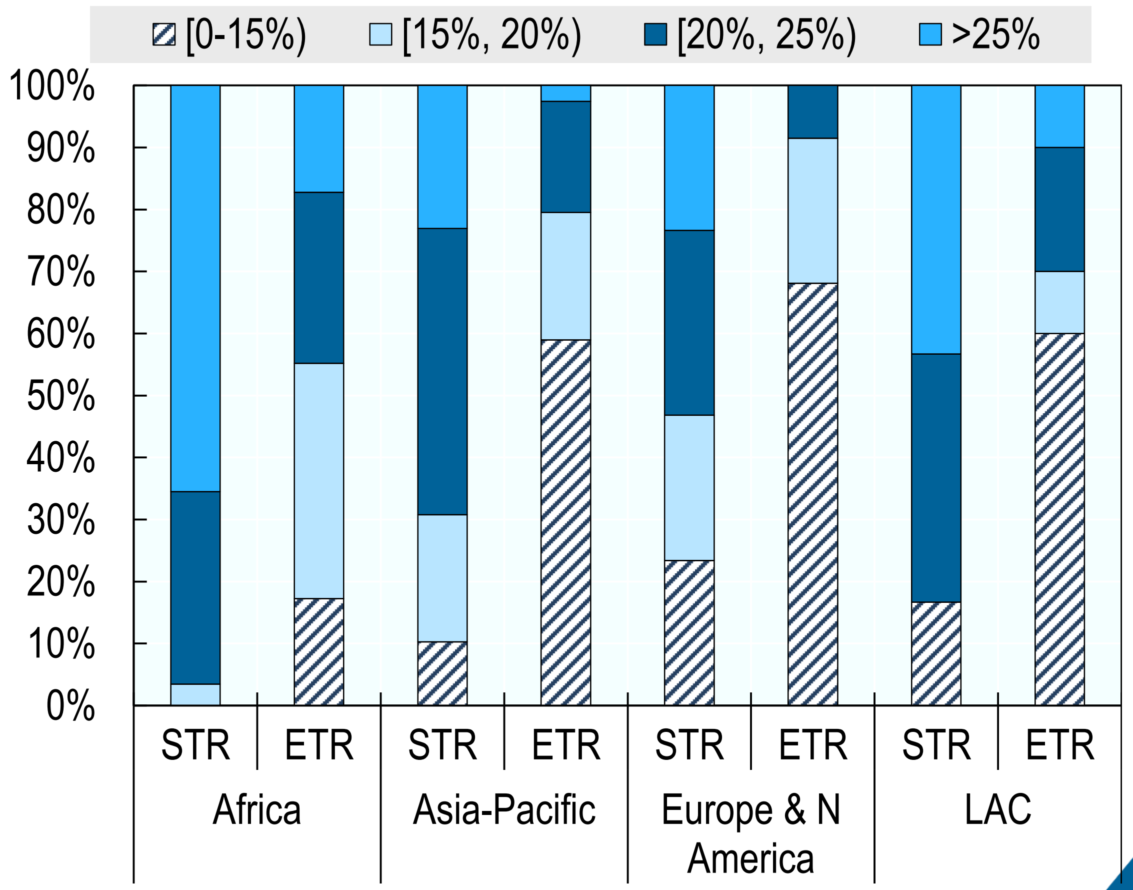
Why is Pillar Two relevant for developing countries?

- **Revenue forgone can be substantial** although less visible (Redonda et al., 2022)

- **Developing countries** are more exposed to **profit shifting** risks
  - Greater reliance on CIT revenues: ~20% of total tax revenues in Africa (OECD, 2022)
  - More limited administrative capacity

- **Widespread use of tax incentives** is one of the reasons ETRs are often low

Average tax rates of foreign affiliates of MNEs with revenues over EUR 750m, 2018



Source: OECD Country-by-Country Report data

How do the GloBE Rules affect tax incentives?

Different impacts at the jurisdiction, entity and tax incentive level

Jurisdiction Level	Entity Level	Incentive Level
- **Baseline CIT systems** - **Other international provisions** (e.g. CFC rules)	- Whether entities are **part of an in-scope group** - The nature of **the entities' activities**: substance and income mix in the jurisdiction	- **Eligibility conditions** - **Scope** of the incentives (narrowly or broadly targeted) - **Tax instrument design** interacts with GloBE Rules

Interactions are complex as they are jurisdiction-, MNE- and incentive-specific:

There is no "one-size-fits-all" conclusion

Impact of GloBE will differ by incentive design

More likely affected	Less likely affected	Unlikely affected
• **Full exemptions** (e.g. tax holidays) • Reduced tax rates or partial exemptions • Tax allowances • Tax credits	• Accelerated depreciation for short-lived intangibles • Qualified Refundable Tax Credits	• Accelerated depreciation or immediate expensing for tangible assets • Immediate expensing of R&D expenditures

- **Other design factors matter for the impact of the GloBE Rules**, e.g. ceilings, substance requirements such as minimum number of jobs
- **Expenditure-based tax incentives** will be more likely to benefit from the substance-based income exclusion (SBIE)

GUIDANCE FOR POLICY MAKERS

Time to revisit and reconsider tax incentives

- **The benefits of using certain tax incentives may change due to the GloBE Rules**
  – No ‘one-size-fits-all’ conclusion
- **Pillar Two should provide impetus for tax reform**
  – Failing to act could mean that countries forego vital tax revenues that will be collected by other countries anyway and could leave them with tax incentives that are ineffective
- **Options will vary by jurisdiction**
  – Reform should be based on jurisdiction-specific analysis, identifying and assessing the tax incentives most likely to be impacted by the GloBE Rules
  – Adopting a “whole-of-government” approach will be important

Importance of considering tax incentive design

- **Narrowly-targeted incentives** (to certain categories of income or expenditure) may be less affected, as may incentives with ceilings or caps
- **Income-based incentives** may be more strongly affected than expenditure-based incentives, particularly for very profitable investments
- **Expenditure-based tax incentives** targeted to payroll or tangible assets may be more protected by the SBIE
- **Incentives based on timing differences** are less likely to be affected, e.g. expensing or accelerated depreciation (for certain assets) or **extended loss carry-over**
- **Qualified refundable tax credits** may be less affected. However, jurisdictions should consider the revenue consequences of refundable tax incentives

Practical guidance for countries

1. **Assess** whether the jurisdiction is at **high, medium of low-risk** of being affected by the GloBE Rules.
2. **Analyse** the impact of the **GloBE Rules on tax incentives** offered
3. **Measure the uptake of tax incentives** and **revenue forgone**
4. **Rank tax incentives based on the risk of top-up taxes** being paid and revenue forgone to establish reform priorities
5. **Study the impact** of existing **bilateral investment treaties investment agreements** and any fiscal stabilisation arrangements
6. **Evaluate** the **efficiency and effectiveness** of **tax incentives** post-GloBE

Possible short-term responses

- **Care should be exercised** in implementing new incentives or when considering entering into new investment agreements or contracts
- **Qualified Domestic Minimum Top-Up Tax (QDMT)** will be an important option for many countries, but it will unlikely be a substitute for a thorough country-specific re-evaluation of tax incentives
- **Pillar Two Revenues** can support DRM and improve investment climate
  - Revenues will support domestic resource mobilisation (DRM)
  - Additional revenues could be invested in ways that support a more attractive investment environment (e.g. investments in skills development and infrastructure)
- **The OECD stands ready to provide technical assistance to developing and emerging economies as they implement Pillar Two and review their tax incentives**

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