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Commentary

Taxation Without Representation: the heavy burden of the OECD's global minimum business tax

November 2023

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About the author

Matthew Sinclair is an economist and policy analyst. He led the TaxPayers' Alliance think tank including its award-winning tax policy research and campaigns; has served as an economic adviser in 10 Downing Street; and has supported a broad range of corporate and public sector clients as a consultant.

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Executive Summary

As Chancellor of the Exchequer, Rishi Sunak agreed for the UK to join a global agreement imposing a minimum effective corporate tax rate (the average percentage of pre-tax income paid) of 15% with 137 other countries in 2021. In-scope multinationals will pay additional taxes if their effective tax rate falls below that rate, based on detailed rules agreed at the OECD. The UK is now moving to implement this minimum tax early, before almost all of the other signatories to the agreement and before those OECD detailed rules are finalised.

We should reject this agreement in principle. Higher corporate taxes in general are economically harmful, diminishing investment and thereby wages. Harmonisation will undermine the democratic accountability that should limit those economic and social harms. Earlier ministers recognised this and David Gauke, former Treasury Minister, for example responded to a proposal for a minimum EU corporate tax rate in 2015 that:

> *"Any form of EU minimum tax rates would undermine our sovereignty and we therefore would block it."*

Diminishing UK sovereignty could create practical obstacles to plans that senior MPs have promoted as central to their economic vision. This includes: cuts to the statutory rate of Corporation Tax proposed by the current chancellor and other candidates in recent Conservative leadership campaigns; tax reforms proposed to address structural problems with Corporation Tax; and reliefs to address specific needs — such as the recent super-deduction. There is a fundamental tension in leaving the EU in order to recover UK sovereignty and then giving sovereignty away in an area that Ministers of all parties defended it when the UK was an EU member state.

All of this would be true if the UK were moving to implement the minimum tax at the same pace as other countries, but the planned **early implementation and the lack of an underpinning treaty framework means additional economic risks.**

- **Administrative costs** will be higher because companies will need to adjust their systems repeatedly as other countries implement, responding to OECD processes that are still being finalised. The Government's impact assessment is unrealistic to the point that its estimated total compliance costs could plausibly be exceeded by some individual firms.
- **Excessive taxes** due to the lack of an underpinning treaty, leading to inconsistent enforcement. This is alongside specific risks in the insurance sector, with a thus far incomplete process taking place to address the risk that legitimate reliefs and the normal flow of funds are not accounted for in calculations for the effective tax rate.
- **Lost international competitiveness** with:
  - firms potentially facing double taxation and having to rely on whether the UK will enter a dispute with the US if — as currently appears likely — that country's implementation is not completed; and
  - low-tax jurisdictions being able to lower their tax rate on out-of-scope companies while collecting the revenues the UK hopes to extract from in-scope companies.

All of that means **revenue is likely to be overstated**, with the economic impact and response from other countries undermining the revenue gains from moving ahead early.

Policymakers have a range of options now, from a fundamental rethink on what is a departure from a longstanding commitment to UK tax sovereignty, to giving themselves more room for manoeuvre through urgent tactical changes to the UK implementation. Future governments could and should reassert UK sovereignty over tax policy.

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Economic and democratic costs of a minimum corporate tax rate

Introduction: the OECD minimum tax

The Organisation for Economic Co-operation and Development (OECD) published an agreement in 2021 to implement a global minimum tax rate of 15% for in-scope (large) companies. This was agreed by 137 countries (including then Chancellor of the Exchequer Rishi Sunak for the UK) and is part of a package including two Pillars:

- Pillar 1: Changing transfer pricing rules to allocate profits to the location of customers.
- Pillar 2: A global minimum effective tax rate of 15%.

The UK signed up to the agreement with no debate or vote in Parliament.

Crucially, the minimum effective rate of 15% means that the proposal will be important for businesses even in countries like the UK where the statutory rate (the rate normally discussed in policy debates over the appropriate corporate tax rate) is well above 15%. The effective rate will be achieved through a "top-up" applied to businesses paying less.

A global minimum tax will create a wide range of impacts for businesses where the OECD proposals do not fully replicate reliefs in the current corporate tax system and for all in-scope businesses to the extent they need to comply with new tax rules and associated compliance requirements.

In the rest of this paper, the intention is to explore the costs associated with that proposal, stepping through why successive governments have defended UK tax sovereignty, the practical consequences for business and how those might aggregate up to impacts on the UK economy as a whole.

Mitigating the potential for unwarranted disparities in effective tax rates on corporate income is a legitimate consideration in designing the corporate tax regime (and/or implementing targeted changes). However, there is a huge difference between careful domestic tax design (which could be harder with this measure) and a largely additional global rule. Existing tools such as transfer pricing rules, diverted profits tax and the controlled foreign companies regime, while they each have their own merits and challenges, are intended to address the challenge of profits being shifted from one jurisdiction to another.

The OECD minimum tax as a whole is bad for the UK; rushing its implementation before other jurisdictions will create even more unnecessary additional costs.

Corporate tax sovereignty matters

Lower Corporation Tax is generally better

Corporations do not themselves ultimately pay tax. The burden of corporation tax (its incidence) falls upon a company's shareholders (ultimately hurting ISAs, pension funds and other personal savings), customers, and particularly its workers (reducing their wages). Desai, Foley and Hines found in 2007 that the "baseline estimate for the share of the burden borne by labor is 57 per cent, and estimates vary between 45 and 75 per cent, depending on the sample period and specification".[1] The OECD minimum tax would therefore be a global tax on British workers.

The mismatch between how corporate taxes are normally described (taxes on business) and the reality (that they are largely taxes on workers) is harmful both in reducing overall accountability for public spending but also by creating a disconnect between the output workers contribute to and their earnings. This can undermine social cohesion and increase strife in labour relations alongside other purported business taxes with an incidence on labour, such as employers' national insurance contributions.

That impact on wages is a reflection of an impact on business investment, which should support improvements in productivity and thereby higher wages. Recently, some commentators (most prominently the IPPR)[2] have sought to dismiss this effect by pointing to the UK time series in recent years: statutory corporate tax rates fell and business investment did not rise. This did not consider the UK trend in effective corporate rates and is very weak evidence (given the wide range of other factors driving UK business investment) compared to either country-level panel data studies or firm-level analysis. The OECD's own firm-level research has found that higher effective corporate taxes are associated with lower investment, particularly among firms that are profitable but marginally so (firms that are either not profitable, or very profitable, respond less). The research found that overall a five percentage point increase in the effective marginal tax rate is associated with a 0.6% decrease in the investment rate.[3]

Despite its incidence on labour (already taxed through Income Tax), Corporation Tax exists — as the Mirrlees Review put it — because it is simpler to tax the profits of a business than its potentially large number of shareholders and out of concern that, if it did not exist, people could shelter income in businesses.[4] There is naturally a risk though that, while the tax might prevent some sheltering income and paying tax at the point of taking the income out of the business (in order to spend) this could mean that others are paying even higher marginal rates than the income tax and national insurance rates suggest. It can also introduce distortions, such as favouring debt over equity. An IMF working paper found that the bias in favour of debt was increasing over time and a "country with a [corporate income tax] rate of 36 per cent that would fully eliminate the corporate tax advantage of debt would see the average corporate debt-asset ratio fall by 10 per cent, e.g. from 50 to 40."[5]

All of this means that corporation tax is an opaque tax, hurts wages both now and over time through its impact on productive investment and distorts corporate behaviour creating further economic harms. All else being equal, there is therefore reason to be sceptical of initiatives that aim to buttress higher corporate tax rates. Beyond that, however, there are distinct problems with achieving higher rates through international alignment, which have meant UK ministers have rejected such proposals in the past.

Tax harmonisation is a bad idea that ministers have rejected before

Proposals to align corporate tax policy internationally have often been promoted with claims that they will either:

- reduce the potential for tax avoidance, particularly by multinationals; and/or
- increase efficiency, reducing the need for businesses to comply with multiple rulesets across multiple geographies.

The most prominent attempt at this before Brexit was EU proposals for a Common Consolidated Corporate Tax Base (CCCTB). The Conservatives opposed this at the time. David Gauke — then a Treasury Minister — said that:[6]

> *"Any form of EU minimum tax rates would undermine our sovereignty and we therefore would block it."*

This view was bipartisan, at least in terms of ministers in government. Gordon Brown reported to the House of Commons in 2007 about an upcoming meeting of European economic and finance ministers (ECOFIN):[7]

> *"There will be an orientation debate on the CCCTB. The UK does not believe that the competitiveness of the EU would be helped by a harmonised company tax base and remains sceptical about both the principles and the practicalities."*

The same objections can be raised to the OECD minimum tax proposal, with two crucial differences.

First, whereas the EU CCCTB was proposed by an organisation that, in principle, could legislate for genuinely common rules, the OECD cannot and there is no underpinning treaty for the minimum tax that would create a means to resolve disputes. There are therefore distinctive costs and risks for jurisdictions that implement these rules ahead of progress in other jurisdictions that do not exist in a bloc where ("gold plating" and other important differences in implementation aside) there can be a single law. There are also ongoing risks of excessive taxation for companies to the extent that countries differ in their implementation and enforcement. Multinationals will be caught in the crossfire, with no overarching structure to resolve the dispute.

Second, the CCCTB aimed to improve the efficiency of the tax system through standardisation. Whether this would have been practical, and whether that would have been worth the resulting inflexibility, is open to question, but the OECD minimum tax, leaving the wider tax base in place in each country, will not even have that effect.

The Conservatives relaxing their opposition to minimum tax rates is particularly striking in light of the Brexit vote. There is clearly a tension between a general proposition that it is right and in the interests of the UK to maintain the flexibility and independence that comes with leaving the EU and signing up to a new measure that will constrain ministers on a key part of economic policy. More generally, it is hard to reconcile this measure with the conservative attachment to the nation state and distrust of supranational governance. Corporation tax, like all taxes, is extractive and requires proper accountability — taxation should go hand in hand with representation. Sir Roger Scruton described why this link exists in practical terms:[8]

> *"Accountability is not brought into being merely by declaring that it exists, nor even by setting up institutions that theoretically enshrine it. It is brought into being when citizens are active in enforcing it. This requires the ability to mobilise opinion against the rulers, in such a way as to remove them from power. That in turn can occur only if citizens stand up for one another's right of protest, and recognise a common interest in allowing a voice to op-*

position. Citizens must co-operate in maintaining the institutions that will subject political decision-making to the scrutiny of a free press and a rule of law.

National loyalty is the rock on which all such attitudes are founded."

The OECD minimum tax would prohibit real, practical options for UK ministers

In this case, limiting the options of future governments, and implicitly binding future parliaments, is not just a theoretical concern. The commitment contradicts recent proposals by senior politicians, tax reform proposals and existing public policy. There are three kinds of measures that would be made harder by a proposal of this kind:

1. Cuts to the overall statutory rate.
2. Tax reforms to improve corporate tax overall.
3. Reliefs to address economic needs.

Combinations of these measures would be particularly challenging. For example, a more competitive corporation tax rate *and* maintaining the current patent box for intellectual property (IP) might no longer be viable.

Cuts to the statutory rate

The higher the statutory rate, the less likely that the minimum effective rate will be binding and therefore the less likely businesses are to pay more tax than is intended with the prevailing reliefs and allowances. And vice versa.

Whether or not a cut in the statutory rate will lead to more firms facing a top-up will depend on the wider structure of reliefs and allowances. However, there have been proposals in recent years from prominent policymakers that would almost certainly not be compatible with these proposals:

- Following the Brexit referendum, then Chancellor of the Exchequer George Osborne proposed reducing the rate to 15%.[9]
- In the Conservative leadership campaign in Summer 2022, Jeremy Hunt and Sajid Javid both pledged to reduce the rate to 15%, immediately and over 5 years respectively.[10]

The Chancellor implementing the tax now would be ruling out his own proposal from a recent leadership campaign.

Tax reforms to improve corporate tax overall

There are tensions in having two tax systems: one for corporate and one for labour income, where there are often inconsistencies between the two systems. Earlier reviews of the tax system have proposed changes that aim to ease those tensions.

Much of the burden of corporate tax falls on workers but this is obscured by Corporation Tax. This will distort attitudes to the tax and changes in rates. The 2020 Tax Commission, set up by the Taxpayers' Alliance and Institute of Directors, argued for a system that taxed returns paid to shareholders (an "s-base") instead, to facilitate a more transparently similar system between labour and capital income.[11]

At the same time, the structure of corporate taxes can introduce biases in corporate behaviour. The most prominent of these is an incentive to use debt rather than equity financing. This can increase the risk of companies going out of business, putting people out of work. In response to this the Institute for Fiscal Studies' Mirrlees Review proposed an allowance for corporate equity.[12] This would reduce overall corporate taxes absent other changes.

While it may be possible to design either or both of these reforms in ways that would meet the OECD minimum tax proposal's requirements, this could be through a higher overall rate, and the potential for top-ups that punish specific businesses would be greater. The standardisation explicit in both pillars in the OECD reform necessarily limits the scope for innovative tax policy that might improve the corporate tax system overall.

Reliefs to address specific economic needs

Ministers often want to increase the rewards to certain kinds of business behaviour:

- Rewarding investment overall — in practical terms this might mean the super-deduction that was recently in place for investment in equipment (which allowed companies to cut their tax bill by up to 25p for every £1 they invested).[13] This could be treated as a deferred tax liability subject to recapture if the asset's depreciable life is longer than five years.[14] Any incentives to investment might be pointless if they are vulnerable to the operation of a UK minimum tax, or other countries taxing a perceived shortfall resulting from those incentives. This is one of the reasons for congressional scepticism in the US, which it is working to address with the OECD behind the scenes, and the UK should have similar concerns. At the time it was implemented, then Chancellor of the Exchequer, Rishi Sunak, cited the importance of a measure that will now no longer be available to future chancellors:

    > *"The super-deduction is the biggest two-year business tax cut in modern British history – driving our economy by helping businesses to invest, grow and support our Plan for Jobs."*

- Rewarding investment in particular geographic areas — Tyler Goodspeed argues in a paper for the Adam Smith Institute that:[15]

    > *"Though carve-outs in the new minimum tax rules for cost recovery on investments in tangible assets should exempt the enhanced allowances for investment in machinery and buildings from minimum tax liability, the same cannot be said of the investment zone exemptions from business rates and stamp duty. Moreover, because the Pillar Two rules permit a carve-out from included income equal to 5% of eligible payroll costs — including payroll taxes paid by the employer — the interaction of the new tax rules with investment zone incentives could perversely result in higher top-up tax liability owing to lower payroll costs in the zones. This would tend to disincentivize investment and employment in investment zones and freeports."*

    Given local institutions' positive response to the Investment Zone proposal and the potential for the tax component to unlock needed planning liberalisation, this would be a loss as an option for future policymakers.

- Rewarding investment in specific assets, particularly those that have a distinctive economic or strategic value over time — e.g. accelerated cost recovery for IP investment in the UK. Governments may have to rely on subsidy programmes which, while equivalent in principle, may be more dependent on bureaucratic delivery, reducing the overall quality of governance in industrial policy.

While businesses pay a range of taxes (e.g. business rates), not all of which are subject to the minimum rate, corporate tax addresses incentives to invest and is therefore often where reliefs will most directly address policymakers' priorities. As noted above, the minimum tax will often interact in disruptive ways with other taxes.

The UK will pay a high cost for moving first

A crucial challenge with the OECD minimum tax is that it lacks an underpinning treaty framework that allows for the resolution of disputes. We still do not know how the peer review or other process will be carried out to determine whether a given country's rules get the seal of approval or not, or who will make that decision. This is a significant undertaking and it does not seem likely that complete reviews could be undertaken prior to implementation, leaving a risk of "provisional approval" which could then be withdrawn on full examination, meaning lots of prior period adjustments.

Even after implementation, countries will differ in how they implement the rules in ways that will be subtle but important for specific businesses. Any discrepancy will mean additional administrative costs as companies cannot build consistent systems and excessive taxes as companies are caught between different interpretations and expected to pay taxes based on both. This can even extend to companies facing additional taxes due to the exchange rate and different currencies being used in different countries.

All of this means that UK firms will pay a high cost with a heavy administrative burden and risks of excessive taxation. The UK, as a result, will pay an economic price in lost competitiveness.

Administrative cost

The current HMRC estimate puts the cost of compliance at £13.2m in one-off adjustment costs and £8.2m in annual costs. It is likely that this materially underestimates the cost of implementation. For some corporate groups it will mean tens of thousands of data points, each requiring work to generate the required information and reflect in financial reporting. Given that scale, it seems likely that some *individual companies* will incur more than that total in compliance costs.

The reason the administrative task is so significant is that the OECD proposals require a shift from tax to accounting measures of profit, based on the accounting principles in the relevant country. But accounting standards are not perfectly aligned globally. If a UK multinational, for example, has a subsidiary that operates in the United States then it will need to reconcile US GAAP (Generally Accepted Accounting Principles)-compliant accounts for that subsidiary with UK GAAP. For some subsidiaries this may be a modest exercise, to the extent that they are larger businesses with relatively good data. However, for smaller subsidiaries in geographies where there are relatively material differences in accounting standards, it could require a substantial project to generate and process the required information.

While the OECD is still confirming possible Pillar 2 safe harbours, and the extent firms will be able to use data already generated for country-by-county reporting, regardless of the outcome multiple sets of records and calculations will have to be maintained to manage calculations that may often not result in any additional revenue. Some multinationals may need to overhaul their financial reporting and maintenance systems. It would only take a small number of the 387 multinationals that are UK-headquartered to require significant transformation projects for the total cost to be considerably higher than expected in the impact assessment.

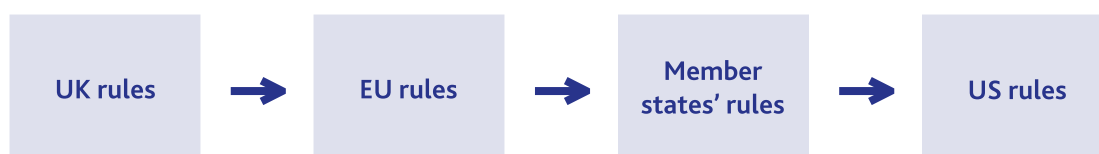
Crucially those costs are not just an inevitable outcome of the minimum tax proposal, but magnified by the UK implementing the measure early, meaning that firms may need to adapt more than once as the scheme is confirmed.

- First, they will need to comply with the UK rules, based on the current OECD agreements and a best guess at how other jurisdictions will act.
- Second, they will need to adjust their compliance to respond to the final rules implemented by the EU.

- Third, they will need to adjust their compliance as that EU ruleset is translated into implementation by EU member states.
- Fourth, they will need to adjust to the ruleset in the US.

All of this will take place alongside, and be shaped by, the ongoing process to finalise the rules at the OECD. This will create its own uncertainties for firms as they do not have a final view on how, for example, disputes between states will be resolved. It will be complicated to the extent that multinational organisations are complicated, with particular challenges around mergers and acquisitions, for example, and how new firms' minimum tax liabilities are recognised.

OECD finalising rules



In principle, these rules should be broadly aligned. For some businesses, the differences between the EU rules and their implementation in member states, for example, may not create significant challenges. For others, however, subtle differences in how different activity is treated might have a significant impact on the information required and/or their tax liabilities. Multinationals in scope for the minimum tax will need to plan for the worst and, with the most substantial divergence likely late in the process via US implementation (if this happens at all) that will mean preparing for substantial potential changes.

The earlier the UK implements, the longer and more material the uncertainty. Unlike in other areas of policy, early implementation here increases, rather than decreases, policy risk. Moving fast means many companies may need to act quickly (potentially in months) to identify the potential impact in their accounts and work to create what will effectively be new, parallel accounting systems.

In some cases, the best way for those businesses to manage the costs and risks associated with these repeated changes may be to avoid activity in the UK. That way they can limit their exposure to early iterations of the rules. By design, the activity that is most affected by the minimum tax is highly mobile, that is part of why a global agreement is felt to be necessary in the first place. We should assume a greater-than-normal response to these taxes with more firms shifting more activity to other jurisdictions than would be the case for a typical corporate tax change. This will particularly be the case in instances where in addition to the additional administrative burden there is also a risk of excessive taxation.

Excessive taxes

In principle, these rules should work to top multinationals up to a 15% tax rate overall. However, this may not be the case in practice, particularly in the insurance sector where the proposals do not fully account for the flow of funds.

The initial problem is that an insurance company might typically have two components:

- The insurance company: the consumer-facing business that collects premiums, pays out claims.
- An investment company (a "fund") that takes the premiums and invests them until the money is needed to pay claims.

To simplify, the problem is that the same return might be taxed at the insurance company and the investment company because they are required to include gains and losses in their investment companies on a mark-to-market basis.

This has been addressed through tweaks to the proposed implementation, with a new "elective method" for how to account for investment income, but in a way that is incomplete. In a submission to the OECD, the Global Federation of Insurance Associations argued for a range of further changes including extending a "testing period" for insurance investment entities; enabling life and health insurance companies to more fully use the new rules; taking full account of the different group structures within insurance companies; and a range of clarifications.[16]

Implementing early means that the UK increases the risk that this process is incomplete, or that there are lasting issues for the insurance sector, despite that sector being particularly important to the UK economy.

Outside of insurance, the risks will be where reliefs are working as intended, but are not reliably counted as qualifying under the Pillar 2 rules and their implementation by country — where different interpretations lead to different estimates of appropriate minimum tax. For example, if the "rollover relief" used to enable companies to reinvest in new IP is not recognised across countries. In principle, this kind of discrepancy should be limited, but in practice this is another source of uncertainty for affected businesses, particularly in industries where reliefs are common (and which are particularly important to overall UK economic performance) such as life sciences and the creative industries.

Loss of international competitiveness

Particularly in the event that the UK moves more quickly than its peers, it will impose additional administrative and tax costs on UK businesses, reducing the overall competitiveness of the UK economy. While the impact will vary by company, the likely pattern is an incentive to relocate to the United States in the short-term and low-tax jurisdictions in the medium-term.

United States

The US implemented a 15% minimum tax in the 2022 Inflation Reduction Act. However, unless it changes its Global Intangible Low-Taxed Income (GILTI) rules to align with the OECD Pillar 2 rules being implemented in the UK and elsewhere, there will be a potential for double taxation. It is unclear how, when, or if it will do so. A recent report by the Joint Committee on Taxation argued that the US would lose $60-120bn of tax revenue, depending on the scenario, and this reflects and is likely to cement congressional opposition.

Businesses could therefore be subject to a top-up tax under the new OECD rules and a liability under GILTI because the two rulesets will give different countries the right to tax the same activity. If they instead relocate to the US, then they might avoid this risk to their competitiveness. In theory this might be mitigated by being counted against their US tax liability, but in practice this will give other countries an opportunity to gather revenue at the expense of the US against which it could push back diplomatically through a diverse range of measures.

In addition to that potential for double taxation, the GILTI regime operates on a blended jurisdictional basis, whereas the OECD requires a tax calculation in each jurisdiction. This will give US firms more flexibility and a reduced administrative burden which would give them a further competitive advantage.

Firms trying to plan for this therefore need to consider two scenarios:

- Scenario A: the UK implements its top-up tax on US firms.
- Scenario B: the UK does not implement a top-up tax.

Given that the UK will continue to have a range of strategic and economic interests in maintaining a good relationship with the US, there are reasons to think that Scenario B is more likely. Regardless, companies will need to plan for this potential outcome, weighing its likelihood against the costs associated with relocating. Given the administrative changes required, early implementation could also act as a trigger point, bringing into focus other changes in the UK (such as the rising statutory rate of corporation tax) and leading firms to reconsider whether it remained the best location for their business overall.

Low-tax jurisdictions

Devereux, Vella and Wardell-Burns (2022) have argued that, with the potential to collect a top-up tax on in-scope countries, low-tax jurisdictions now have an incentive to further lower rates on out-of-scope companies "perhaps even all the way to zero".[17] This means that the UK, with its now higher statutory rate and relatively broad corporation tax base, will become less attractive as a location for those smaller, out-of-scope businesses. This could further undermine the revenue associated with the minimum tax over time and reduce UK economic growth directly.

Crucially, these out-of-scope companies also have a role in the competitiveness of the multinationals that are in scope. If lower tax jurisdictions become more attractive to those out-of-scope companies, that will affect the network of suppliers, distributors and financial and professional services available. The competitiveness of the UK as a whole could be affected by some of those networks shifting to lower-tax jurisdictions, resulting in an additional reduction in net revenues and UK economic growth.

Impacts in smaller businesses and adjacent sectors

Concerns about the minimum tax may be concentrated among larger businesses in the most affected sectors, where they are likely to face the greatest direct administrative burden or increase in their tax liabilities. However, it is worth bearing in mind that those impacts will cascade to smaller businesses and businesses in adjacent sectors.

If a reinsurance business relocates activity from the UK, this will affect its suppliers (from consultancy to real estate to information technology) and its customers (insurers, who will have a less convenient relationship with their reinsurers). This complements and is analogous to the impact of lower-tax jurisdictions attracting out-of-scope businesses as described above.

Revenue is likely to be underwhelming

Given the wider pressure on the public finances, ministers may see this measure as indispensable as a means to ease other hard choices over tax and spending priorities. More than that, they may take the view that this is simply revenue that the UK would otherwise leave "on the table" for other countries to collect.

HM Treasury expects the minimum tax to raise nearly £2.3bn a year by 2027-28. The final outturn will depend on the wider business cycle context, but is likely to be reduced to the extent that:

- Any activity that shifts to other jurisdictions will mean a loss of expected corporate tax revenues and revenues from other taxes.
- Other countries (particularly low-tax jurisdictions) can intervene to secure any additional revenue from in-scope companies.

Crucially, these two effects could interact in a particularly pernicious way for the UK: losing some revenue to other jurisdictions (principally the United States, as described above) and not getting the upside expected from those businesses that do remain. Ultimately the risk of the UK losing out would only occur at the point other countries implement (i.e. 2025) and rests on if and how that wider implementation takes place.

Economic activity shifting to other jurisdictions

Any economic activity that shifts to other jurisdictions will mitigate the revenue gains, with the Exchequer losing out both on:

a. the Pillar 2 associated revenues; and

b. other taxes on that activity.

The scale of this impact will depend on the economic impact described above. However, the size of some of the most affected sectors means that any loss in activity could result in a minimal or even negative net impact on revenue. Association of British Insurers research suggests the insurance and long-term savings industry contributed around £17.2bn in taxes in 2021-22, for example.[18]

Other countries intervening

Other countries may act to gain the revenue. Under the Qualified Domestic Minimum Top-Up Tax (QDMTT) low-tax jurisdictions can implement their own top-up taxes to collect revenue from in-scope multinationals. As Tyler Goodspeed put it: "In other words, if a 15% minimum tax is going to be levied on large MNE's anyway, then from the perspective of the low-tax jurisdiction, they might as well collect that top-up tax themselves." They can maintain low rates for out-of-scope companies at the same time and attract those smaller businesses, exacerbating the potential shifting of activity from the UK.

Options

There are a range of steps that the Government could take to address the costs and risks associated with the OECD minimum tax. These range from the best option of scrapping the policy, avoiding the limitations it places on future governments and asserting the UK's ongoing sovereignty in tax policy, to, at a minimum, more targeted measures to ensure that ministers have the tools needed to avoid disproportionate sectoral economic harms.

Scrap the policy

The Government could scrap the measure entirely, particularly in the event that Pillar 2 is not implemented in the US. This would clearly be a moment at which a range of countries would need to consider whether they are comfortable proceeding unilaterally given the importance of US multinationals. It would also show a commitment to UK sovereignty as a principle.

In the interim, the Government could announce that, in the spirit of the earlier announcement, its implementation of Pillar 2 would be contingent on the US making material progress towards finalising changes in the GILTI regime. Other economies have already announced a delay to 2025, pending progress in the OECD process: Singapore, Hong Kong and Thailand.

Ultimately, only scrapping the policy will maintain the UK's sovereignty and an effective rate of 15% unavoidably rules out policy choices that senior ministers have recently promoted. Unless this was fundamentally renegotiated, a 15% rate is going to put a practical constraint on UK policymakers, not just the behaviour of multinationals as it has often been portrayed.

Scrapping the planned implementation would ensure that future policy choices are not constrained by an agreement that ministers signed up to without a Parliamentary debate or vote. It would reflect that the commitment does not bind the UK to implementation.

Review potential impacts of early adoption

While the Government has consulted on Pillar 2 implementation overall, there is a case to urgently test the impacts of implementing early and/or if the US does not go ahead. In its summary of responses, "the Government expects that the US will continue to make progress towards meeting its commitments to reform the GILTI in line with the October Statement".[19] This expectation seems increasingly unrealistic.

There are a range of questions on which ministers might either push for a reconsideration within government and/or look to consult further:

- Whether there are plausible scenarios where revenue will materially underachieve against its expectations, given wider uncertainty over how Pillar 2 is finalised and implemented in other jurisdictions.
- How the Government might specifically mitigate the administrative costs of early implementation and/or the risk of firms relocating.
- The medium-term impact of the US not aligning its rules with Pillar 2 and/or low-tax jurisdictions materially reducing their tax rates on out-of-scope businesses.

Introducing policy flexibility

In the event that ministers see early steps to implement Pillar 2 as important in principle, they might still introduce flexibility that could reassure the most affected businesses. This could include:

- An allowance for a delay in the legislation, giving ministers options in the event that there is an apparent cliff edge and potential disruption for UK multinationals.
- Going ahead, with a proviso that the measure will be reconsidered or amended in the event that policy choices in the US or other jurisdictions do not match the Government's expectations.

Sectoral relief

The Government could go further to ease concerns in the insurance industry and other particularly affected sectors.

This could include specific steps to clarify the status of selected incentives and addressing some of the issues raised by the insurance industry with the OECD (described earlier). This would reflect an extension of existing policy, where the Government has sought to take some steps to reassure affected businesses.

It could also include a more general provision for amendments to ensure that tax reliefs function as intended over time, as other countries develop rules both directly in the implementation of Pillar 2 and in related policy (e.g. corporate tax for out-of-scope companies, non-tax subsidies).

Reassert UK tax sovereignty

The Government has argued that the legal basis for it being able to sign the treaty was that the UK is not compelled to implement the measure, which means current and future parliaments are not bound by that ministerial commitment. This implies there may be the potential for future governments to reassert sovereignty in this area by amending or abolishing its UK implementation. This is likely to be particularly practical to the extent that the US has not fully implemented the change and could be part of a broader range of measures addressing areas where accountability is weakened by a shift away from domestic policy.

Conclusions

The OECD minimum tax is a bad idea in principle and an unwelcome departure from a longstanding, bipartisan commitment to maintain the UK's sovereignty over its tax affairs. Ministers have previously defended this both in principle, as a freedom that the UK should guard, but also as an important practical measure to ensure that we can get the right corporation tax for the UK.

If the change is implemented at all, it should be done carefully, not in a hurry reflecting a push to increase revenue and address the UK's fiscal position. Otherwise there is a risk that it might prove counterproductive in fiscal terms and create an unnecessary hostage to fortune as other governments move at a slower pace and the OECD process itself is incomplete.

There are options that ministers and parliamentarians can push for to mitigate the risks. Ideally that should mean a principled rejection of the minimum tax and the departure from UK tax sovereignty it represents. Or it could be a more limited but still important attempt to mitigate the economic risks and administrative costs early implementation could create for the businesses that we need to thrive here in the UK. If not, future governments should reassert sovereignty, particularly if the minimum tax goes ahead in an incomplete form in the US.

There is work to be done in avoiding the immediate risks created by the minimum tax. Over the longer-term, politicians should champion the flexibility and accountability that comes with independent tax policy.

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LEGATUM INSTITUTE
11 Charles Street
London W1J 5DW
United Kingdom

t: +44 (0) 20 7148 5400
www.li.com

November 2023