

TAX

The G7 Finance Ministers' Global Tax Agreement (or are tax havens dead?)

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As has been fairly widely reported with a great deal of fanfare on the international television news stations and also in the financial pages, earlier this month the G7 finance ministers came to, what has been referred to variously as an historic or a seismic agreement on global tax reform.

This agreement is pursuant to the OECD's ongoing initiative towards reforming the worldwide tax system and reducing tax avoidance and evasion. There have been a number of developments over the past few years, including the programme relating to BEPS (base erosion and profit shifting) and the various initiatives that accompany this, and these two decisions relate to, what the OECD has called, Pillars One and Two.

Pillar One

This initiative is aimed primarily at the very large tech companies operating in the digital economy. As we all know, it is relatively easy to be located in, and provide one's services and products, from a low tax jurisdiction, to customers located in high tax jurisdictions, without having any sort of discernible taxable presence in the latter, and therefore not paying tax in those countries.

In latter years this has caused a considerable amount of disgruntlement, including among the advanced economies of the world, such as in western Europe, and some of them have gone so far as to introduce unilateral measures to extract some of the taxes in these circumstances, such as the digital services tax in the UK.

The agreement now reached should, in principle at any rate, eliminate the need for such unilateral action, and its focus is to ensure that these companies do not merely pay tax where they are resident and have their head office, but also pay tax in the countries where they operate and from whose residents and citizens they derive their profits.

The proposed rules will tax the following form:

- They will apply to global groups with a profit margin of at least 10%.
- Then, 20% of any profit above that 10% margin will be reallocated to the countries in which that company operates, and be subject to tax in those countries.

Pillar Two

Under this proposal every country in the world will have to have a corporation tax of at least 15%.

This will clearly not go down well with a number of offshore jurisdictions where the tax rate is zero, including jurisdictions such as in the Channel Islands, Isle of Man, Liechtenstein, Cayman Islands, Seychelles, and many others.

On the other hand, having a headline rate of 15% is one thing: having an effective tax rate of 15% is another story altogether. And it does not take too much imagination to introduce provisions into one's tax laws that have the effect of reducing the headline rate of 15% to an

effective rate of a couple of percent.

Conclusion

One can debate the appropriateness or otherwise of Pillars One and Two having regard to the inequities in the world economy and having regard to other considerations, such as free trade and the like. And one can debate whether these are populist moves or are seriously justified.

But whatever view one takes of the matter, it is clear that, in the case of both Pillar One and Pillar Two, this is just the beginning of a very long road. It is one thing to express a principle in a few lines, as appears above. It is altogether different to put in place a comprehensive set of rules, with all the checks and balances and all the measures to prevent loopholes, which can be adopted in a way that is sufficiently the same in each of the relevant countries, and which does not itself create tax competition among countries.

And then, of course, comes the challenge of ensuring that the offshore jurisdictions who introduce their minimum corporation tax of 15% do so in a way that meets a minimum standard of acceptability to the large economies of the world.

In the subtitle to this article the question was asked whether tax havens are dead. Well, maybe their death sentence has been pronounced in relation to their current form, but all one has to do is make oneself sufficiently more attractive, fiscally speaking, compared to another country such that there will be a significant saving of taxes, and one can continue to thrive in that sphere.



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