Kluwer International Tax Blog

The Made in America Tax Plan: What's in store for other countries?

Maarten de Wilde (Erasmus School of Law, PwC) · Monday, April 26th, 2021

Maarten de Wilde*

Summary
On March 31, 2021, U.S. President Biden released his 'American Jobs Plan', an ambitious proposal for large scale public investments in infrastructure and other priorities. That same day the American President announced plans to offset the costs of these investments with U.S. corporate tax increase proposals: the 'Made in America Tax Plan'. To ensure that the tax measures envisaged would not weaken the competitive position of American businesses overseas the rest of the world is expected to tag along and join in on the envisaged American rate hikes. The Biden Administration sees an opening for pushing its agenda at the tax policy discussions taking place within the Inclusive Framework of the OECD on the so-called Pillar One and Pillar Two proposals, the Blueprints of which the OECD published in October 2020. This paper discusses the 'Made in America Tax Plan' and its implications for the European Union and its member states, the author's home country the Netherlands as one of these, and other countries, that is, if the U.S. tax plans were to see the light of day.

Introduction

On March 31, 2021, U.S. President Biden released his 'American Jobs Plan', an ambitious proposal for large scale public investments in infrastructure, the production of clean energy and the care economy, among others. The White House Fact Sheet (available on whitehouse.gov) speaks of an amount of public expenditure of around $2 trillion in the upcoming 8 years. That same day, as part of this, the American President announced plans for reforming (read: increasing) the U.S. corporation tax, the 'Made in America Tax Plan' (available on home.treasury.gov). The revenues of the envisaged corporate tax bill increases are sought to offset the costs of the proposed public expenditures in 15 years and should continue to generate revenue on a permanent basis to help reduce federal budget deficits. The proposals were already part of Biden's 'Build Back Better' plans during his campaign for the U.S. presidency. The Made in America Tax Plan expresses the intention of increasing the corporate tax rate from the current 21% to 28%. In addition, it is planned to tighten the tax rules for internationally operating businesses that were introduced with the Tax Cuts and Jobs Act (TCJA) as of 2018. It is proposed to strengthen the 'Global Intangible Low Taxed Income' (GILTI) regime introduced at that time, to abolish the 'Foreign Derived Intangible Income' (FDII) regime and to replace the 'Base Erosion and Anti-Abuse Tax' (BEAT) with an alternative measure. In this context, the Biden Administration has indicated that it will commit to reaching global agreement within the OECD Inclusive Framework on the measures currently being discussed there: a redistribution of income tax base across countries towards marketing/content-user jurisdictions (Pillar One) and a globally aligned minimum level of business income taxation and top-up taxation by countries to that level where other countries do not conform (Pillar Two). On April 8, 2021, the U.S. Department of the Treasury presented its intentions and plans to do so at a meeting of the Steering Group of the Inclusive Framework. The slide deck with the title 'Steering Group of the Inclusive Framework Meeting; Presentation by the United States, April 8, 2021', can be found on politico.com. The Biden Administration also wants to tighten the U.S. anti-inversion rules, remove incentives to shift investments overseas, introduce a minimum corporate tax on 'book income', abolish tax subsidies for the fossil fuel industry, and tighten enforcement by reserving more funds for the U.S. Internal Revenue Service (IRS). The American Jobs Plan includes climate and energy transition-related tax subsidies and tax subsidies for domestic investments. The plans could potentially change the world of international corporate tax in an unprecedented way. In this paper I discuss the question of what the American plans encompass and what their possible implications would be for the European Union, the author's home country the Netherlands, and other countries should the U.S. tax plans become a reality.

The Made in America Tax Plan and what it means

Public investments and the financing of these

The Biden Administration wants to spend public resources on a large scale. That's why the American Jobs Plan: *"The American Jobs Plan will invest in America in a way we have not invested since we built the interstate highways and won the Space Race"* (The White House, Briefing Room, FACT SHEET: The American Jobs Plan, March 31, 2021). The U.S. government wants to raise the necessary funds from business by increasing corporate tax burdens, and therefore the Made in America Tax Plan: *"[T]he President is proposing to fix the corporate tax code so that it incentivizes job creation and investment here in the United States, stops unfair and wasteful profit shifting to tax havens, and ensures that large corporations are paying their fair share"* (*ibidem*). To achieve that, the rest of the world needs to move along with the U.S. rate hikes: *"President Biden's reform will also make the United States a leader again in the world and help bring an end to the race-to-the-bottom on corporate tax rates that allows countries to gain a competitive advantage by becoming tax havens"* (*ibidem*). To this end, the Biden Administration is tying up with the ongoing discussions within the Inclusive Framework on Pillar One (base redistribution) and Pillar Two (global minimum level of taxation) in which the ambition is to reach a global political consensus by the middle of this year. The United States is on board (again) and thus the movement from Trump's 'Make America Great Again isolationism' to Biden's 'Build Back Better self-interest driven multilateralism'. I think it would be good to keep the interests here sharp, especially considering the possible implications for the EU and the Netherlands, amongst others, as well as other countries, should these plans become a reality. The French Government is enthusiastic and has announced that it intends to use the French EU Presidency in the first half of next year to adopt an EU directive for this purpose, as I recently read on politico.com: 'France to push for embedding global minimum corporate tax in EU law by mid-2022'.

Losing control on the corporate tax base

The Made in America Tax Plan states that the United States in fact has lost control over its corporate tax base. The report says that the effective U.S. corporate tax rate that U.S. companies pay on their American profits is now 7.8%. Federal tax revenues as a percentage of gross domestic product (GDP) have fallen from 20% to 16% over the past two decades. In the tax mix, the corporate tax share has been declining for years and the share of labor-based taxes has been rising for just as long (see Tax Plan, figure 1). Corporation tax as a percentage of GDP in the United States is 1% (in 2019) while for an average OECD country it is around 3% (see Tax Plan, figure 3).

Prior to the TCJA, this was still 2%. The corporate tax rate reductions from 35% to 21% that came with the enactment of the TCJA as from 2018 have mainly benefited shareholders (often also foreign), as windfall gains in the form of dividends and buybacks. In any case, it has not encouraged large businesses to make significant additional investments in the United States. The GILTI and FDII measures were even found to encourage the diversion of fixed asset investments from the United States abroad. Moreover, despite the TCJA, the U.S. tax system still allows large-scale income tax base shift: *"As a result, of the top 10 locations for U.S. multinational profit in 2018, seven were tax havens"* and *"[d]espite attempts to rein in profit shifting, tax havens are as available today as they were prior to the 2017 tax reform"*.

Incentives in TCJA

To be able to properly set forth the implications of the plans, it is perhaps worthwhile to first clarify how the U.S. tax system has worked since the TCJA. Prior to the TCJA, the U.S. corporate tax functioned as an import-neutral territorial system due to the tax deferral possibilities it allowed (the so-called deferral issue and the 'Dutch cv/bv piggy bank-at-seastructure' and its Luxembourg et cetera likes). As of 2018, the TCJA effectively transformed the U.S. corporate tax rate for U.S. businesses into a kind of quasi-export-neutral dual tax system. Since then, profits from domestic production and sales (i.e. within the United States) are taxed at 21%. Profit from 'rest-of-the-world' production and sales (i.e. outside the United States) are taxed at, say, half of that (the so-called GILTI rate, which moves between 10.5% and 13.125%). In addition, a flat-rate return of 10% on depreciable fixed assets held abroad (on a consolidated basis), the so-called 'qualified business asset investment' (QBAI), is exempt from U.S. taxation. The same return on the same fixed assets domestically held – even if utilized for production for exports – is taxed at the regular 21% rate. This system was created by the confluence of the GILTI regime and the FDII regime. The GILTI regime concerns a CFC-like income inclusion rule (IIR) similar to that proposed in the OECD's Pillar Two Blueprint, but on a global blending basis and with GILTI ETR calculations being based on US tax accounting rules while Pillar Two resorts to commercial accounting for this purpose. The FDII regime concerns an export subsidy – taxation at the GILTI rate – for profits from domestic production activities for export abroad.

Wisman and I wrote in an IBFD-paper in 2019 that the United States can afford this dual tax system because of their large internal market and geopolitical position, or at least seem to bet on it on the basis of the functioning of their tax reforms (See M. de Wilde & C. Wisman, *OECD Consultations on the Digital Economy: "Tax Base Reallocation" and "I'll Tax If You Don't"?*, in Taxing the Digital Economy: The EU Proposals and Other Insights sec. 1.10. (P. Pistone & D. Weber eds., IBFD 2019), Books IBFD). We also wrote in that paper that we thought that, for example, the Netherlands and many other countries, including the other EU Member States, might not be able to afford such an additional charge for geopolitical and tax competitive reasons. Such a system, after all, encourages the relocation of production and assets abroad, such as QBAI assets amongst others in the case of the United States. In the U.S. case a diversion of these abroad, after all, means taxation in the United States at the GILTI rate or an exemption of tax, rather than taxation at the regular headline rate. Moreover, a low minimum rate in combination with 'global blending' are likely to be quite ineffective when it comes to tackling tax competition and will therefore not do as much more than the BEPS 1.0 measures have already done. Wisman and I wondered in that same paper whether the national economy of any country that would adopt such a system would actually be sizeable enough to sustain any such tax rate differentials and competitive responses these incentivize. Because if not, what then would happen? *"Should the GILTI rate then be raised closer to the standard 21% rate, or the standard rate reduced to bring it closer to the*

GILTI rate?" It has become the former.

Reclaiming control on the corporate tax base

The Biden Administration has devised several measures to regain control over the corporate tax base. It is proposed to increase the headline corporate tax rate to 28%. It is also proposed to adapt the GILTI regime on 3 parts. The GILTI rate goes up to 21%, a switch is made to a 'per country blending model' equal to that in the Pillar Two Blueprint, and the QBAI scheme will be abolished. The Biden Administration also plans to remove the FDII regime and replace it with a direct funding of R&D activities. It is also proposed to replace the BEAT, rated as ineffective, with an undertaxed-payments-like rule (UTPR) similar to that proposed in the OECD's Pillar Two Blueprint, i.e. a deduction-limitation measure for intra-group payments to group entities in low-taxing jurisdictions abroad; SHIELD ('Stopping Harmful Inversions and Ending Low-tax Developments'). The other measures are quite specific American indigenous ones and I leave these for that reason unspoken here. Worth noting is the 'minimum corporate tax on book income', i.e., a minimum business income tax for large profitable companies of 15% on commercial accounting profits, to prevent situations in which companies simultaneously present large commercial profits and low or no corporate taxable income and in consequence pay little or no corporation tax.

With the rest of the world's assistance and cooperation

President Biden may have been advised that such a further move toward export neutrality as planned will not be possible without a multilateral coordination of corporate tax rates. After all, an export-neutral tax system weakens the local competitiveness of domestic industry overseas, and that is exactly what the American plans do. That, incidentally, is also the reason why the Netherlands, and many other countries for that matter, currently operate import neutrality-promoting participation exemption regimes while only levying top-up taxes on foreign portfolio income of multinational firms engaging in aggressive tax planning structuring operations under their CFC-rules. However, the American's weaker competitive position in relative terms upholds only if and to the extent that other countries do not follow the United States. A well-designed highly placed global minimum rate in combination with a properly devised 'per country blending' mechanism (in the context of a supply side oriented tax base division system) will be quite effective when it comes to tackling tax competition, but only if it is done so at a global level.

This explains the Biden Administration's move toward 'multilateralism', at least the campaign to push the U.S. tax plans forward globally within the Inclusive Framework. And hence the presentation of U.S. Treasury at the Inclusive Framework Steering Group of April 8, 2021. The idea is to move the whole world around and have the American reform plans taken over. After all, only then will the United States save itself from weakening its competitive position for American businesses abroad. And only then will the Biden Administration's intention to fund the American Jobs Plan with corporate tax increases be likely to succeed. Point of U.S. attention, however, still is the Pillar One proposal and all those unilaterally emerging digital services taxes (DSTs), e.g. in France, United Kingdom, Italy, Spain, (EU?), et cetera, all of which operate to the disadvantage of the big American tech companies and for the reason of which the United States is trying to smother these with (contemplated) retaliatory tax measures. The United States still opposes these unilateral moves toward DSTs, and in the Treasury's slide deck it can be read that: *"Stabilizing the architecture requires, among other steps, addressing the proliferation of unilateral measures that gave rise to Pillar 1* [which] *[r]equires a "standstill and rollback" workstream* [since] *the United States cannot accept any result that is discriminatory towards U.S. firms"*. The United States has nevertheless indicated its willingness to participate in a Pillar One solution in the form of a more generic redistribution of income tax base towards sales jurisdictions, without distinction along sectoral lines and therefore no tax ring-fencing along the lines of automated digital services (ADS), consumer facing businesses (CFB) and business-line segmentation. Moreover, the generic tax base redistribution should apply only to the 100 largest multinationals, which would then have to be identified by reference to quantitative turnover/profit margin-oriented threshold tests. Some months ago, the United States abandoned the idea of Pillar One as a 'safe harbor' (i.e., as an optional regime for U.S. big tech firms).

What this would mean

If all this becomes a reality, then the consequence of this will be a convergence of global effective corporate tax rates, or even a convergence of corporate tax systems to be precise. A minimum rate as high as the 21% proposed by the Americans will effectively usher in the impossibility for countries to continue to instrumentalise their corporate income tax systems to attract or sustain domestic investment (read: investment climate considerations/fiscal autonomy/tax competition). For traditionally tax competitive countries such as the Netherlands, for example, such a move will mean that the country will see its company tax system transformed into a surtax or surcharge, or "subtax" if the Dutch effective company tax rate were found to be below the global minimum. The competitive distinctiveness of the company tax of the country – and with that its commercial value – will be off, I estimate. The same will also apply, for example, to the Irish, Swiss, Luxembourg and Singaporean corporate taxes. Of course, that is the whole purpose of the operation. This nevertheless said, in addition to this, the cost of capital would probably rise with the increase in effective company tax rates. That could produce additional economic inefficiencies and a decrease, ceteris paribus, in investment worldwide. I think it is important to continue to realise that tax increases, company tax increases included, will have to come from somewhere. Where a corporate tax reduction may turn out to produce a windfall benefit for a company's shareholder, this does not in any way mean that that same shareholder will just accept a capital cost increase and will not try to pass it on to, for example, the consumer (price increase) or the (blue collar) worker (wage moderation).

It is important to see that if we were to go along with the movements now proposed, we would introduce export neutrality at a global level according to the American model. At the same time, countries would effectively give away their sovereignty in the field of corporate income taxation. Whether we want to go down that route is ultimately a political choice of course. However, I think it is important to keep this in mind, also because I sometimes find some contradictions in expressions in this regard, for instance from the government of the Netherlands. In a piece on the Dutch news site ad.nl, I recently read that our Secretary of State 'wants to get away from the dark side in order to combat tax avoidance, that the Netherlands needs to take the lead more often in order to achieve a fairer tax system at European level, and that the debate on sovereignty is a "mock debate"' (in Dutch: ''…weg wil van de dark side om belastingontwijking tegen te gaan, Nederland vaker de leiding moet pakken om Europees tot een eerlijker belastingstelsel te komen, en het debat over soevereniteit een schijndebat is.''). On the Financial Times site I read that our Secretary of State sees in the American plans "*a huge step towards finding global solutions and developing effective rules*", "*fully in line with the efforts made by the Netherlands to modernise the international tax system*", and that "*this will certainly contribute to our government's efforts to counter international tax avoidance by companies and harmful tax competition between states*". Not that long ago, however, I read in Dutch parliamentary documents that the Dutch Cabinet, because of the national tax autonomy to be considered quintessential to the Netherlands, is very critical of the European Commission’s plans to replace the EU member states’ vetoes in EU decision making in tax matters with qualified majority voting (Dutch Parliamentary Papers, House of Representatives, 2018/19, 22 112, no. 2772). And, notably, on December 8, 2019, the Dutch House of Representatives passed a motion asking the Dutch government to bring to expression within the EU’s Council that the abandoning of the unanimity requirement in EU decision making in taxation is “unspeakable” for the Netherlands (Dutch Parliamentary Papers, House of Representatives, 2018/19, 21 501-02, no. 1920). Worth noting here, on top of this, is the non-paper of March 23, 2021, of the Dutch and Spanish governments, devised as a contribution to the wider discussion in the EU on strategic autonomy and which also covers tackling tax avoidance and achieving fair and effective taxation (‘Spain-Netherlands non-paper on strategic autonomy while preserving an open economy’, as attached to the report accompanying the letter from the Dutch Minister of Foreign Affairs of March 25, 2021, Dutch Parliamentary Papers, 21 501-02, no. 2301). The Dutch-Spanish non-paper calls for an examination of the areas in which the unanimity requirement in EU decision making could be abolished: *“Strengthening the ability of the EU to defend its public interests and increasing its open strategic autonomy calls for effective decision-making mechanisms. It could therefore be useful to explore in which areas the extension of qualified majority voting is possible, limiting – where possible and desirable- the instances where unanimity hampers the EU’s capability to act”*. At the same time , however, the now outgoing Dutch Government has expressed to Dutch Parliament that it is not committed to amending the EU treaties, in order to keep the debate practical and to stay away from a more institutional discussion (Draft Report of the General Affairs Council of April 20, 2021), (in Dutch: ‘Conceptverslag Raad Algemene Zaken dd 20 april 2021’, available on tweedekamer.nl). I think that all this is rather difficult to reconcile.

What it will take for the American plans to succeed

For the plans to become a reality, the Biden Administration will need to get virtually all house Democrats and all 50 Democratic Senators on board, including the moderate Democrats. Later this year, tax increases under the budget reconciliation procedures will also have to be discussed. That forms another hurdle to overcome here, I understand, also in the light of the American budgetary discussions and the politics in this regard. Worth noting here is the reform plan building on Biden’s proposals that Senate Finance Democrats Wyden, Brown and Warner presented on April 5, 2021, titled ‘Overhauling International Taxation; A framework to invest in the American people by ensuring multinational corporations pay their fair share’.

On top of that, the countries of the Inclusive Framework, including all EU Member States, will need to be on board as well. That could prove to be an uphill battle. The U.S. plan, like the Pillar Two Global Anti-Base Erosion Proposal (GloBE) proposal, is mainly about addressing those malign hub jurisdictions – that is, relatively small countries that have relatively much to gain from a competitive company tax system and have been successful in doing so in recent decades. The commitment to export neutrality is particularly interesting for the classic export neutrality pursuing (read: large and rich) countries, and an opportunity to get on with it towards these hubs (BEPS 2.0) after the successful targeting of classic tax havens in the BEPS 1.0 project. On ft.com I read ‘Europe’s low-tax nations braced for struggle over US corporate tax plan’. For the capital-importing developing countries, the U.S. proposals will also likely not be yielding much as any additional tax revenue will probably not end up there: ‘Developing countries likely not be helped out with minimum rate of income tax’ (in Dutch: ‘Ontwikkelingslanden zijn niet geholpen met minimumtarief winstbelasting’), Dr. Mosquera noted on the Dutch news site fd.nl on April 19, 2021. And on Moneycontrol.com I read this week that ‘India is unlikely to go along with US’ global minimum corporate tax proposal'.

By the way, what we see the Biden Administration doing here actually has a name in game theory: 'Stackelberg competition', that is, the game where the followers (here: the rest of the world) will follow the dominant 'Stackelberg leader' (here: the United States). However, this game is not without risk. To be successful, the leader must be sure in advance that he indeed will be followed. Because if he does not, he will lose the game and then he would have been better off taking on the role of the follower and – translated into taxation – to continue the path of playing along the tax competition game. If this will turn out to be the case, this will mean that the Biden Administration will have to find another way to fund the Jobs Plan. The risk for the Biden Administration lies in the strong incentive for countries not to comply with the Pillar Two measures, or to withdraw from them at some point in the future and thus continue to focus on tax competition – the reality of recent decades. Non-moving 'candidate followers' could accordingly undermine the long-term stability of the system. Moreover, this could also be initiated from the United States itself, for example if the Republicans were able to take the reins again at some point and if the measures were subsequently to be reversed. Just as Democrats are now reforming Trump's TCJA today, Republicans may at the end of the day be able to do the same with Biden's Made in America Tax Plan tomorrow. If matters will then turn out such that we will have a 'Made in America EU Directive' within the EU at that point, a Directive that can only be changed on the basis of unanimous decision making because of the importance of the EU member states' tax autonomy, such could then suddenly turn out to have some serious consequences for the global competitiveness of European businesses. This may be even more so since individual EU Member States, unlike non-EU countries, cannot move towards strategically intervening in their domestic economies through direct subsidies for certain sectors and industries, because of the EU State aid rules that prohibit this. Then EU member states' aids policies in this regard should also be organised on an EU-wide basis. These, too, seem to me to be factors to consider and to strategise on in countries' political decision-making in the coming period.

Closing remarks

We're heading for closure. Will the 'Made in America Tax Plan'' turn out as a tax game changer or as a blow? I'm afraid to venture into a prophecy here to be honest. The fact that we are standing here today could very well also have had something to do with, for example, the shift to a 50-50 seat distribution in the U.S. Senate after Democrats won the two runoff elections in Georgia on January 5, 2021. That, after all, created a majority for Democrats with the decisive vote of Democratic Vice President Harris and thus securing Democrat control in the U.S. Congress. Either way, times ahead will be quite exciting. All things considered, one last question lingers with me. How can it be that the United States only raises 1% of GDP as corporate tax revenue, where the OECD average is around 3%? Maybe I am comparing apples and oranges here, that could very well be the case and if so I would be quite curious on that. But if this is ultimately the real problem facing the United States at the end of the day, could it not be the case that the United States is simply a little less successful vis-à-vis other countries when it comes to protecting the domestic corporate tax base? If this were to be the case, would it then not perhaps be more appropriate to first look around at how the other OECD countries manage to extract 3% of corporation tax revenue from their economies? This, instead of immediately moving towards urging the rest of the world to embrace one's own model? We're going to see.

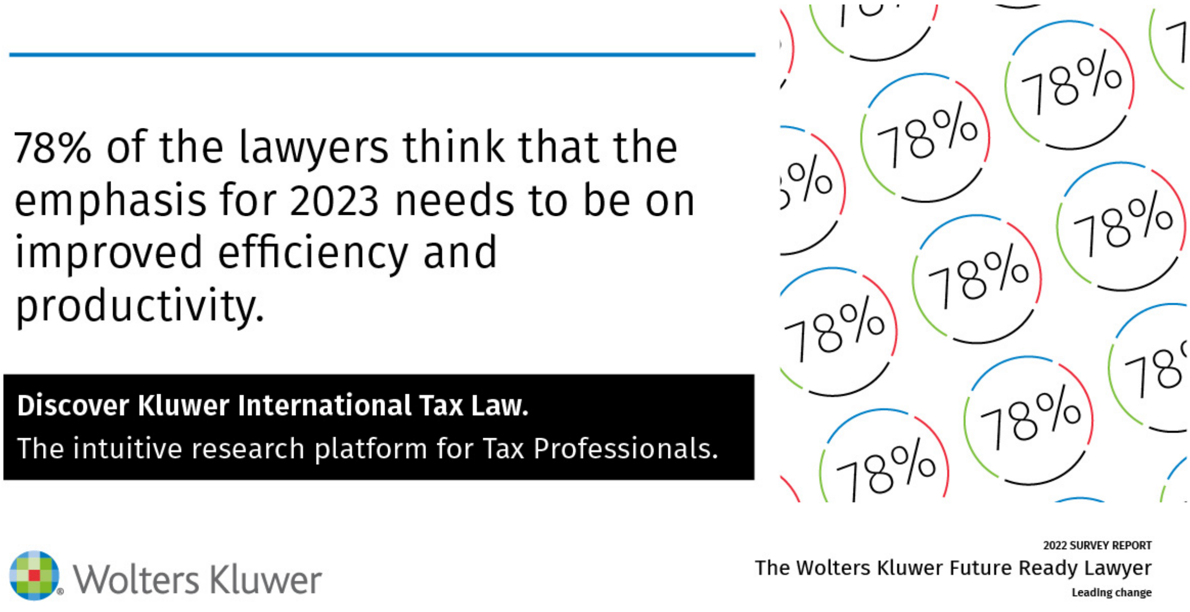
* Prof. Dr. M.F. de Wilde is on the staff at Erasmus University Rotterdam, the Netherlands, and PwC, The Netherlands.

To make sure you do not miss out on regular updates from the Kluwer International Tax Blog, please subscribe here.

Kluwer International Tax Law

The **2022 Future Ready Lawyer survey** showed that 78% of lawyers think that the emphasis for 2023 needs to be on improved efficiency and productivity. Kluwer International Tax Law is an intuitive research platform for Tax Professionals leveraging Wolters Kluwer's top international content and practical tools to provide answers. You can easily access the tool from every preferred location. Are you, as a Tax professional, ready for the future?

Learn how **Kluwer International Tax Law** can support you.



This entry was posted on Monday, April 26th, 2021 at 2:32 pm and is filed under EU/EEA, Made in America Tax Plan, Netherlands, United States
You can follow any responses to this entry through the Comments (RSS) feed. You can leave a response, or trackback from your own site.