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The U.S. pushback on minimum corporate tax rates may test the limits of bilateral tax treaties with EU Member States

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In recent weeks the tax world gave a lot of attention to how President Trump blew up some serious advancements in international tax law, long in the making. One of those advancements was the introduction of a minimum tax on profits of the largest multinational corporations, ensuring that they pay at least 15% in taxes on profits from their worldwide activities.

After initial consensus on a global minimum effective tax rate had been reached back in 2021 with over 130 jurisdictions, the agreement signed was never ratified by the U.S. Congress.

We should be willing to admit that President Trump was correct in stating that a minimum tax may lead to extraterritorial taxation when other countries levy additional taxes to cover for low or no taxation in some other parts of the world. (The U.S. itself already had some experience with this.) The EU was one of the frontrunners when introducing the Minimum Tax Directive (2022/2523) at the end of 2023. Extraterritorial taxation will effectively start later, covering profits from 2025 onwards.

One elephant in the room is the tension between international law and European law. Many EU Member States have bilateral tax treaties with the U.S. that regulate the division of taxing rights on corporate profits. Ratification of the multilateral agreement would have been necessary to infringe upon those pre-existing divisions, despite attempts from the Organization for Economic Co-operation and Development (OECD), the G20 and the EU to play down the necessity of such changes to comply with international law.

If the European Commission would start enforcing the Minimum Tax Directive and expect EU

Member States to indeed tax the profits of U.S. multinationals if needed, these Member States might find their own courts turning against them given the pre-existing bilateral agreements.

A textbook solution would be to amend such pre-existing agreements in a way that they are brought in line with EU Law, but this would require both countries to agree in order to avoid a contentious treaty override. As this is not likely to happen anytime soon (if ever), the EU might in theory force EU Member States to terminate their agreements.

The problem is that bilateral tax agreements cover much more than just corporate taxation. It is often business that is the driving force behind concluding bilateral agreements, but individuals benefit from them as well. Personal income taxes and taxes on personal property are also regulated by the same agreement to avoid double taxation. Having a large network of bilateral tax treaties is a necessity open economies can hardly do without, as they are of vital importance to businesses operating cross-border and to citizens who work or live abroad.

So the question is: what the EU will do next? Keeping a minimum tax in place with respect to jurisdictions that did not ratify the multilateral agreement will inevitably lead to legal challenges by the taxpayers involved, simply based on domestic and international law. It is just a matter of time and this will not be limited to the U.S.. (On a side note, the sheer complexity of implementing the minimum tax as it stands today would warrant a reconsideration anyway.)

The European Commission should stay clear of interfering with bilateral tax treaties, even though Article 4(3) TEU and Article 351 TFEU could provide it with a basis to try and do so when the effectiveness of the Minimum Tax Directive would be threatened. But as bilateral tax treaties cover so much more and are mostly in the realm of the exclusive competence of Member States, this is not the time to start testing the limits of said Articles.

In the grand scale of things, minimum taxation is just a minor part of the realm of both personal and corporate taxation. Not that it is unimportant, to the contrary, but when the Minimum Tax Directive was adopted Member States did not intend to give up the remainder of their sovereign rights either.

The necessity of having bilateral tax treaties adapted to single nation needs and business taxation being an inextricable part thereof, may lead to quite a different end result than the bilateral Open Skies-agreements that were scrutinized by the EU's Court of Justice back in 2002. The fundamental freedoms are not directly at stake and the EU has no competence of its own to regulate direct taxation internationally. On balance the EU's interests here are far more limited compared to the infringement on reserved rights that are of crucial importance to any sovereign

Member State. But can we afford to wait how this plays out in the various courts or will someone play another trump card in between?

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