February 26, 2021

Dear Clients and Friends

Re: Janet Yellen's International Tax Policy – Will It Affect You?

Dr Janet Yellen is a very important person who was appointed Secretary of the US Treasury on January 26, 2021. At the US Senate Finance Committee hearing on her nomination 5 days earlier, Janet Yellen answered an array of questions, providing useful insights about her positions. So what does Janet Yellen stand for? How will it affect US persons and international business? Following are extracts from her hearing.

Yellen's remarks:

Yellen said that the Biden administration has proposed to tax the investment income of families making more than $1 million at the same rate they pay on their wages and to tax some previously untaxed capital gains on the final return of wealthy taxpayers. These reforms would remove biases in the US tax code that "favor wealth over work". The administration will not ask families making under $400,000 per year to pay more in taxes.

On the US corporate side, the Biden administration proposes raising the corporate tax rate to 28 percent -- which is the midpoint of the pre-2017 level and the rate imposed after Trump's Tax Cuts and Jobs Act.

The administration proposes reducing the estate-tax exemption amount from the current level of approximately $11.5 million to $3.5 million ($7 million for a couple), with an increase in the top estate-tax rate from 40 percent to 45 percent.

On the international side, Yellen commits to "vigorously engage" in the OECD/G20 negotiations to reform the international tax system. A global minimum tax agreed to at the OECD would stop the destructive global race to the bottom on corporate taxation.

Currently, the OECD is in the midst of multilateral negotiations on tax challenges arising from digitalization. Negotiations thus far have centered upon two OECD "pillars". The Trump Administration was at first extensively involved in the negotiations with the OECD, then put the negotiations on pause in 2020.

Instead of waiting for US-OECD agreement, a number of countries have chosen to unilaterally implement their own digital services taxes (DSTs). As of January 15, 2021, over a dozen countries have already imposed DSTs, with many more countries having either published proposals to enact a DST (including Austria, Spain, UK, France, India, Italy and Turkey). The DST policy frequently discriminates against non-resident businesses and imposes double taxation. Yellen believes that businesses should be able to recover their costs so that the income tax taxes net income and not gross receipts.

If such disputes were not resolvable through international negotiations, Yellen would work with the United States Trade Representative i.e. use the Trump administration's policy of imposing trade tariffs – carrot and stick.

What are the OECD pillars Yellen referred to?

In October 2020, the OECD published blueprints for reform income tax reform which aim to raise extra taxes of $100 billion annually.

Pillar 1 proposes to allocate profits according to formulas to the "market" country where consumers are. Two amounts would be allocated by multinational groups to such countries, Amounts A and B.

Amount A might perhaps be 20% of residual (=excess offshore) profits exceeding 10% of sales turnover, for groups with global revenues above EURO 750 million, perhaps. But Amount A would only relate to profits from: (1) automated digital services, and (2) consumer facing businesses.

Amount B might perhaps be a fixed profit margin on "baseline marketing and distribution costs" which would vary depending on industry and region.

Pillar 2 proposes to impose a home country top-up tax on multinational parent corporations with global turnover above EURO 750 million – perhaps a 12.5% minimum tax on income from each market country after excluding 10% of payroll and depreciation expenses. This is referred to as an Income Inclusion Rule (IIR). To stop shenanigans with expenses, there would be a back-up tax on undertaxed payments.

None of the above is final yet.

Made in America?

President Biden's "Made in America" proposal includes a 10-percent penalty on goods and services imported by U.S. companies from foreign affiliates. Yellen explained that The President's objective is to create incentives for American companies to create and maintain jobs at home. President Biden's Offshoring Tax Penalty is aimed at those who offshore manufacturing and service jobs to foreign nations in order to sell goods or provide services back to the American market when those jobs could have been done by U.S. workers. Many countries await details e.g. China, Israel.

Cryptocurrencies:

Yellen thinks it important to consider the benefits of cryptocurrencies and other digital assets, and the potential they have to improve the efficiency of the financial system, while curtailing their use for malign and illegal activities.

Concluding remarks:

E-commerce taxation will soon become exceedingly complex.

Anyone doing international business over the internet should take advice on how to avoid multiple taxes in multiple countries. Don't leave it all to Janet Yellen.

We are geared up to help you.

Please contact us for advice.

As always, c*onsult experienced tax advisors in each country at an early stage in specific cases.*

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