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19 July 2023

Ways & Means Subpanel Asks Treasury About Pillar Two Design

The Republican majority of the House Ways & Means Tax Subcommittee July 19 challenged Michael Plowgian, Deputy Assistant Treasury Secretary for International Tax Affairs, to defend the OECD-led BEPS 2.0 global minimum tax project, US support for the project and how the government has negotiated various aspects of the global minimum tax rules. Members also criticized the Biden Administration for not regularly consulting with Congress and, specifically, the Committee as the negotiations have moved forward. They specifically questioned the constitutionality and global legal framework for allowing other nations a potential share of US taxes through the Undertaxed Profits Rule (UTPR) and why the US R&D credit isn't treated under the global system in the same way as refundable R&D credits provided by other countries.

Republicans took particular aim at the Joint Committee on Taxation analysis suggesting the United States stands to lose over $120 billion in tax revenues if the rest of the world adopts Pillar Two in 2025 as clear evidence that the Treasury has failed in negotiating a good deal for the United States. While Plowgian did not dispute the estimate, he did note several times that the JCT analysis provided a range of estimates based on several different scenarios, and that the US may actually see an increase of revenue through implementation of Pillar Two.

In an opening statement, Chairman Mike Kelly (R-PA) asserted that the United States would continue to be a revenue target for digital services taxes (DSTs) and, "This Administration has called for additional business taxes to fund their domestic spending agenda. So then why would Treasury negotiate an OECD deal that surrenders over $120 billion in US tax revenues to foreign countries? It makes no sense."

Ranking Member Mike Thompson (D-CA) defended the project, saying in an opening statement, "American workers and taxpayers have paid the price for a system that rewards large multinational corporations that do business in one country and park their profits in the country with the lowest tax rate they can find. Republicans' desperate attempts to preserve this system is more of the same: sparing the largest, most profitable companies from paying their fair share while honest taxpayers are left with the bill. The global minimum tax is designed to level the playing field and put an end to underhanded profit shifting." For Subcommittee Democrats, a key argument was that the US Treasury should not walk away from the negotiating table on Pillar Two because that would leave no one to support the US and US companies.

Panel 1 featured Plowgian alone, who said in testimony that Pillar One and Pillar Two can only be implemented in the US with the support of Congress, and Treasury stands ready to work with lawmakers: "We hope to have a complete Pillar 1 package soon and intend to continue to seek input. Similarly, with respect to Pillar 2, we stand ready to work with Congress to enact the reforms proposed in the President's Budget to implement Pillar 2, which would increase U.S. revenue and strengthen our tax system. We will also continue to work with Congress to prioritize issues for interpretive guidance."

Select questions and answers are paraphrased in the following table.

Chairman Kelly – USMCA was reopened and renegotiated at the direction of members. Are you willing to go back	Plowgian – Only Congress has authority to implement or not implement changes to law. We have received input

to the negotiating table and address issues important to members of the Committee? Why is Congress denied information when they try to find out how it was negotiated? I would like to see this go back. I don't like an Administration taking an end run around Congress.	and we take input very seriously and we would like to continue to take that into the discussions.
Ranking Member Thompson – Can you provide more detail on issues Treasury negotiated to protect the US and US companies? The OECD is going to forge ahead, and the US cannot put its head in the sand and pretend this isn't happening. Estimating the revenue effects of adopting or not adopting Pillar Two is very difficult.	Plowgian – Many provisions including relief related to accelerated depreciation and issues related to GILTI. On Monday, the UTPR safe harbor was unveiled in guidance that also protects transferable credits in the IRA.
Dave Schweikert (R-AZ) – What is happening with R&D credits?	Plowgian – US R&D credits generally are nonrefundable and that would reduce the ETR and could make the taxpayer subject to top-up tax.
Lloyd Doggett (D-TX) – Since joining the Committee 20+ years ago, I have been seeking to shut down the use of tax havens, which are still being used. International tax dodging shifts the burden to small business and middle-income taxpayers. The Biden administration has been a leader in this important tax deal.	Plowgian – Conforming GILTI could involve a country-by-country calculation. Doing so makes the US more competitive because a country-by-country GILTI calculation deters shifting of profits to lower-taxed jurisdictions.
Jodie Arrington (R-TX) – You just said that US companies will be more competitive if we tax them at a higher rate? Democrats had full control of the Congress and White House last year, did you raise the GILTI tax? What you are doing is a backdoor strategy to force Congress to raise taxes, or risk other countries taxing US companies. I think the most outrageous aspect is the fact that the tax base will be ceded to other nations, but we will also undermine our sovereignty. If a company takes their liability lower than 15% due to WOTC, etc., they are penalized because of the top-up tax. This thing is completely off the rails and upside down.	Plowgian – Pillar Two levels the playing field for US MNCs, ensuring everyone is paying a global minimum tax.
Drew Ferguson (R-GA) – Why do you think you can override the Constitution to write tax policy? Why would you allow countries to have more advantageous treatment of R&D credits? How can you justify sending US tax dollars to foreign jurisdictions?	Plowgian – We believe a level tax playing field will allow US businesses to compete and win.
John Larson (D-CT) – Would Pillar Two go away (with inaction by the US)?	Plowgian – No, South Korea and Japan have already taken steps to implement Pillar Two; all EU states are obligated to implement Pillar Two this year under the EU directive; and the UK, Canada, Australia are also moving forward … We need to be at the negotiating table representing US interests.

Jason Smith (R-MO) – Administration doesn't have authority to write tax policy on its own. Smith went on to request Treasury respond in writing relating to specific circumstances in which it consulted with Congress on various aspects of Pillar One and Pillar Two, including whether Congress was consulted before Treasury negotiators agreed to the UTPR, agreed to not grandfather GILTI as it stands under current law, and agreed to the scope of Pillar One profit allocation rules to exempt foreign MNEs.	 Plowgian – Consistently said that Congress was consulted and agreed to respond back in writing to the Chairman's request. He pointed out several times that he was not part of the Treasury negotiating team when certain matters were negotiated and said that foreign MNEs are not exempt from the scope of Pillar One.
Kevin Hern (R-OK) – Why haven't you responded to letters from lawmakers requesting Treasury's revenue analysis of Pillar One?	Plowgian – Pillar One can't be implemented without Congress. We have been concerned that estimates wouldn't provide Congress a complete picture because numerous aspects of Pillar One have not been finalized. Once we resolve issues, we plan to follow up with estimates.
Linda Sanchez (D-CA) – Republicans are demonstrating their commitment to shielding corporations from paying their fair share of taxes. Democrats recognize we must remove profit-shifting incentives from the tax system. There has been favorable guidance on the treatment of transferable credits. Can you describe the negotiations on this issue and why there is a favorable result.	Plowgian – We received a lot of input from Congress and business about treatment of credits. Many countries initially opposed treatment of transferable credits as refundable. Changing that view has been multi-prong: Sec. Yellen explained the importance of the issue to her counterparts, as did others in the Administration. The guidance was very favorable.
Ron Estes (R-KS) – Do you think US businesses should pay more taxes to other countries? JCT projected Treasury would lose $120b. Why didn't Treasury focus on getting credit for R&D, GILTI, BEAT, etc.	Plowgian – Pillar Two levels the playing field. One of the things that is clear from the original Pillar Two blueprint is a common tax base was needed, and that's why a financial accounting tax base was adopted. We are engaged in ongoing discussions on all these issues.
Suzan DelBene (D-WA) – Regarding the LIHTC, how would that be treated under P2? Last week it was announced countries will refrain from DSTs, except Canada.	Plowgian – The Administration has been able to secure administrative guidance in February that such incentives that are part of tax equity financing transactions should be protected, referring to flow-through tax benefits in the February guidance. This is a critical issue. Treasury is engaged with Canada at all levels to dissuade them from implementing a DST, which would undermine Pillar One negotiations. We are exploring all options.

Rep. Randy Feenstra (R-IA) questioned how the project moves forward if it can't get through Congress. He also asked whether Treasury recognized the harm of the UTPR given that the US doesn't have a refundable R&D credit. Rep. Gwen Moore (D-AL) asked whether GILTI isn't compliant because it allows blended rates, which also allows companies to place profits in low-tax jurisdictions.

Panel 2

Witnesses were:

- Mindy Herzfeld, Professor of Tax Practice, University of Florida Levin College of Law
- Adam Michel, Director of Tax Policy Studies, CATO Institute
- Anne Gordon, Vice President, International Tax Policy, National Foreign Trade Council
- David Schizer, Dean Emeritus and Professor of Law and Economics, Columbia Law School
- Peter Barnes, International Tax Advisor and Of Counsel, Caplin & Drysdale

In testimony, Herzfeld, who generally took a negative view towards Pillar Two, and said options for the US going forward include legislation modifying its domestic rules so that they conform to Pillar Two, including modifying its tax credits or by enacting its own qualified domestic minimum top up tax. However, she noted doing so is unlikely to make up the revenue lost due to other countries' adoption of QDMTTs, while modifying the U.S. regime for business credits could also end up as a revenue loser. The US could also threaten other countries with retaliation in order to get them to drop or scale back implementation of Pillar Two.

Michel said, "Congress should lower the corporate tax to the OECD and Biden Administration's agreed-upon rate of 15 percent and make full expensing for all new U.S. investments permanent, including structures. Rather than adopting the OECD foreign tax rules, Congress should finish converting the U.S. corporate tax to a full territorial system that entirely disregards both foreign profits and foreign taxes."

Gordon said, "The breadth of issues still remaining with a 'nearly complete' Pillar Two agreement, as well as its ongoing implementation in countries that are major U.S. partners, is unsettling." Citing the reopening of the USMCA to address members' concerns years ago, she said, "We urge Congress to continue working with the OECD, Department of the Treasury negotiators, and foreign counterparts to create a regime that works with the U.S. tax code, protects U.S. companies and workers from an unlevel playing field, and encourages investment and economic growth in the U.S."

Shizer said in joining the Pillar Two agreement in October 2021, the Biden Administration has strayed from US principles that taxes must be imposed by Congress, not the President, and the tax policy of the United States should be set by the United States, not by other countries. "Proceeding without congressional approval, they have given other countries significant influence over our tax system," he said.

Conversely, Barnes encouraged US participation: "The choice facing the US, both the government and its corporate taxpayers, is binary: adopt the proposal (with the financial and administrative benefits, plus the opportunity to continue to influence the direction of the legislation), or step away from the table, with the attendant consequences. I urge this committee and Congress to enact legislation to align the US tax rules with Pillar Two. That will continue our country's leadership in developing sound international tax practices that benefit our companies and their ability to drive economic growth."

During Q&A, Rep. Hern said Pillar Two rules favor refundable tax credits and asked whether this creates a new competition for tax subsidies. Herzfeld said the rules shift competition for incentives, so countries can compete with credits and other incentives blessed under the rules. She said the rules quash certain incentives and encourage others, and companies and countries are creative. Under a question from Hern about sovereignty, Shizer said it shouldn't be the case that a President can partner with an international organization to circumvent Congress.

Ranking Member Thompson said Republicans have made their concerns on sovereignty known, but don't all the countries have the right to enact legislation on Pillar Two? Barnes said the OECD agreement provides flexibility for countries, and that's why modifying GILTI rules may be sufficient for the US.

Kustoff asked about compliance burdens. Gordon said companies have reported needing more personnel and spending a great deal of money to comply.

Testimony is at https://waysandmeans.house.gov/event/39854592/

Chairman Kelly's opening statement is at https://waysandmeans.house.gov/tax-subcommittee-chairman-kelly-hearing-on-bidens-global-tax-surrender-harms-american-workers-and-our-economy/

Rep. Thompson's opening statement is at https://democrats-waysandmeans.house.gov/media-center/press-releases/thompson-opening-statement-tax-subcommittee-hearing