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OECD Pillar 2 Is a Bad Deal for America

To the Editor:

As a member of the U.S. House Committee on Ways and Means, my colleagues and I are charged with creating responsible tax policy that finances the federal government. Tasked with this responsibility, it is my obligation to raise structural and substantive concerns with the OECD pillar 2 agreement. The current agreement is unacceptable to my colleagues in Congress and will be opposed by Democrats and Republicans unless it is changed.

To understand how we arrived at the present situation, it is crucial to look at the past. My initial policy interest in international tax coincided with the development of the Tax Cuts and Jobs Act but before the proliferation of foreign digital services taxes directed at U.S. businesses, both of which came about in the aftermath of the original OECD base erosion and profit-shifting project.

As Congress undertook the process of tax reform in 2017, we recognized that profit shifting and base erosion were legitimate issues that needed to be confronted. We created global intangible low-taxed income — the world's first global minimum tax — and the base erosion and antiabuse tax regime to address these issues. GILTI and BEAT ensure that companies, both foreign and domestic, pay a minimum level of tax. After more than five years, we can confidently say that our system works: Corporate tax revenue has increased, even with a lower rate, and there has not been a single U.S. corporate inversion in this time frame.

While implementing the TCJA, I became concerned about numerous foreign countries considering the imposition of unilateral DSTs on large digital multinational enterprises. Most countries structured their DSTs to target U.S. companies while exempting their domestic firms. These unprecedented taxes threatened American innovation and jobs while creating a confusing patchwork of tax laws around the world. Recognizing that the rapidly changing digital economy creates a global challenge for policymakers, I encouraged the administration and other countries to work with the OECD to develop a multilateral solution for this new arena of our global economy. This was the basis for U.S. involvement in the BEPS 2.0 project, which was announced in 2019.

Arriving back in the present, the current structure of the inclusive framework is unrecognizable from where we started. Pillar 1, which was supposed to address DSTs, has been pushed to the side in favor of pillar 2, a framework that attempts to implement a series of complicated global minimum tax rules. This shift in focus was aided by the armchair academics in the Biden administration, specifically in the Department of the Treasury, that has never met a tax it did not want to raise.

From my perspective, which is widely shared by my colleagues, Treasury negotiated pillar 2 in a manner intended to handcuff Congress's ability to exercise its constitutional taxwriting authority in the future. By consenting to the OECD process and failing to defend the current U.S. tax code and our existing multilateral tax treaties, Treasury thinks that Congress will be forced to go along with its plan to radically change our international tax regime; otherwise, U.S.-based MNEs would be hit with punitive taxes from foreign countries.

We can deduce this thinking from several key negotiating points to which Treasury agreed. The first is the undertaxed profits rule, an enforcement mechanism to pillar 2, which allows other countries to impose an extraterritorial tax on U.S. companies if they determine that their U.S. profits are not taxed at 15 percent. To put a finer point on this, Treasury has agreed to let foreign countries tax U.S.-based income, to which they may have no economic nexus, if they determine that the effective tax rate of a company is below 15 percent. This is a direct surrender of U.S. sovereignty and creates a new taxing right for foreign countries that violates tax treaties. If implemented, this will cause endless litigation and economic tumult as countries and MNEs dispute the amount of tax due in each country.

These views were expressed to Treasury in a letter that former Ways and Means Chairman Kevin Brady, R-Texas, myself, and the rest of the Republicans on the Ways and Means Committee sent to Treasury in December of last year. Treasury's response indicates it is extremely worried about this but is attempting to manifest treaty compliance out of thin air.

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The treatment of U.S. tax credits under pillar 2 reveals another negotiating mistake by Treasury. Under the framework, tax credits are treated unfavorably unless they are refundable. This presents a massive issue for the United States, as most of our general business credits are nonrefundable. In late stages of the negotiation, Treasury made some effort to protect its favored nonrefundable tax credits, including green energy credits and the low-income housing tax credit, but it failed to garner any protection for other important credits, specifically the research and development credit.

The R&D credit is essential to economic growth. While other countries were able to protect their R&D regimes, Treasury decided not to defend our current tax code in favor of getting a deal done. In Treasury's previously mentioned response, and in an exchange with Rep. Randy Feenstra, R-Iowa, Treasury Secretary Janet Yellen indicated that she was willing to work with Congress on an R&D credit that would be "more effective." In our view, this is a euphemism for a refundable R&D credit that would increase the cost to the taxpayer. Or in other words, Treasury wants Congress to change the U.S. tax code in a way that reduces U.S. revenues and runs counter to bipartisan policy objectives, all to advance the taxing scheme it concocted with the OECD.

Another issue that Treasury mishandled was the ordering of taxation regarding the qualifying domestic minimum top-up tax (QDMTT) and GILTI. In this framework, a QDMTT is applied before GILTI, allowing countries to have first taxing rights on U.S. subsidiaries. This structure presents two issues, depending on whether QDMTT qualifies as an allowable foreign tax credit. If QDMTT triggers an FTC, this will reduce the amount of tax GILTI collects, significantly reducing U.S. tax revenues. If it does not, or if U.S. companies are in an excess FTC position, there is a risk of double taxation.

When asked about declining GILTI revenue during her testimony before the Ways and Means Committee in March, Secretary Yellen was confident that U.S. tax revenue would increase if pillar 2 was enacted. Yet she also said she wanted to raise the GILTI rate to 21 percent. While Treasury's green book estimates that the United States will collect $1 trillion in new taxes over the next 10 years with the adoption of pillar 2, its modeling rules cannot take into account speculative changes in other countries' tax codes. With the aforementioned interaction between QDMTT and GILTI, it is more likely than not that these estimates are wildly unfounded in reality.

Treasury could have avoided all of these negotiation errors and omissions if it actually sought meaningful congressional consultation. While Treasury has claimed to have kept Congress informed about OECD developments, we have most often learned of these decisions after they had been made through press releases to the general public.

We have also asked for data from Treasury about the economic impact and the worldwide distribution of pillar 2 tax implementation, with no meaningful response. As the United States has a large majority of the most profitable companies in the world, we may lose the most from pillar 2 implementation. Treasury refuses to provide congressional taxwriters with any economic impact data, raising doubts that this will be a good deal for the U.S. economy, U.S. companies, and U.S. workers.

So where do we go from here? My colleagues in the House of Representatives and I are already working to revoke funding for the OECD. We should not be the largest funding source for an organization that wants to collude to steal away U.S. jobs and tax revenues. Additionally, because the pillar 2 framework is a threat to the interests of the United States, I am working with Ways and Means Chair Jason Smith, R-Mo., on legislation to protect against unfair tax practices enacted by any country against American workers and businesses. After the threat of discriminatory taxes is removed, I believe that the United States and the OECD can come to an agreement that treats the current U.S. tax code in a fair manner.

Rep. Ron Estes, R-Kan.
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Ron Estes, one of only a handful of engineers in Congress, worked in the aerospace, energy, and manufacturing sectors before representing Kansas's 4th Congressional District since 2017. He is a fifth-generation Kansan and former state treasurer, and he serves on the House Committee on Ways and Means, Budget Committee, and Education and the Workforce Committee. ■

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