Putting American Interests First at the OECD

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Key Takeaways

- TCJA created new international tax policies to protect the U.S. tax base and increase international tax competition. These policies will begin to phase out along with many other critical TCJA provisions at the end of this year.
- The U.S. has been involved in global tax deal negotiations with the Organization for Economic Cooperation and Development (OECD) which is developing what it calls a "Two Pillar Solution" to international tax issues. Both Pillars would result in significant revenue loss for the U.S. without the most basic benefits that were originally expected for the U.S..
- If President Trump seeks to continue his advocacy for U.S. interests in the international tax space, he can do so by leaving the OECD discussions entirely or pushing for an approach that would be more favorable to the U.S. than the Biden Administration's approach.

Introduction

President Donald Trump is still within the first few months of his second term and is already showing a commitment to addressing international tax issues. On day one, President Trump signed an executive order addressing the ongoing Organization for Economic Cooperation and Development (OECD) global tax deal negotiations and the failure of the prior administration to advocate for American interests. The executive order instructs the new administration to explore options to respond to countries that have implemented discriminatory taxes. Discriminatory taxes are also discussed in a separate executive order dealing with trade policy.

With the impending expiration and phasing out of many provisions of the Tax Cuts and Jobs Act (TCJA) of 2017 at the end of 2025, the future of our international tax system remains uncertain. TCJA implemented groundbreaking reforms such as the creation of the world's first global minimum tax and ultimately had the impressive result of stopping corporate inversions entirely. Yet, unlike other parts of the tax code where inaction by Congress would result in the reversion to prior policy, the international tax landscape will continue to evolve regardless of U.S. action as other countries implement the global tax deal.

We have put together a list of further options for the new administration to consider as well as a primer on what has happened thus far. Overall, President Trump's change of direction is a welcome development in the international tax landscape.

International Tax Policy in Trump's First Term

TCJA created new international tax provisions to protect the U.S. tax base and increase international tax competition. Among those provisions was the world's first global minimum tax, known as the Global Intangible Low-Taxed Income (GILTI) tax. GILTI applies to certain foreign income of a U.S. parent company at a rate of 10.5%, with an effective rate of 13.125% when combined with partially creditable foreign tax credits.

GILTI works alongside TCJA's other international tax policy levers, including the Foreign-Derived Intangible Income (FDII) tax and the Base Erosion and Anti-Abuse Tax (BEAT). FDII is a tax of 13.125% on export income from U.S.-based intangible assets, and BEAT is a tax of 10% minimum tax applied when related companies engage in cross-border payments for profit-shifting purposes. All three of these international taxes will undergo a rate increase as many TCJA provisions phase out.

As Congress and President Trump came to an agreement on U.S. international rules, the Trump Administration also entered the U.S. into formal negotiations at the OECD on international tax rules. The OECD negotiation included Pillar One to address digital services taxes (DSTs) and taxation rights and Pillar Two to establish a global minimum tax. DSTs are discriminatory taxes levied mainly against U.S. tech companies and were mainly started by France, against which President Trump threatened to retaliate with tariffs.

More specifically, Pillar One would reapportion a portion of the profits of multinational companies to other countries if the company has more than 20 billion Euros ($21.3 billion) in global revenue and a profit margin greater than 10%. In exchange for this reapportionment, it was understood that countries should eliminate their Digital Service Taxes. Pillar Two is a global minimum tax of 15% on the foreign income of multinational companies that have annual revenues above 750 million Euros (approximately $800 million). Pillar Two would be mainly enforced by the Undertaxed Payments Rule (UTPR), which allows a country to impose an additional tax on a multinational company if the company has an effective tax rate of less than 15% in any other country where it operates.

As President Trump left office, discriminatory DSTs proliferated, and global leaders agreed to continue negotiating the Pillars.

International Tax Policy under President Joe Biden

Just before leaving office, the Trump Administration had worked to protect American interests at the OECD by ensuring American companies were not singled out or discriminated against under Pillar One and advocating for GILTI's inclusion as an acceptable global minimum tax under Pillar Two.

Early in President Biden's term, proposals released by the U.S. Department of the Treasury signaled a different approach. Biden's Treasury made more concessions to other countries in negotiations which Senate Finance Committee Ranking Member Mike Crapo stated failed to adhere to established tax principles and would unfairly target American firms.

In addition, the Biden Administration proposed changes to GILTI that would raise its rate to 21%, well above the OECD's minimum tax rate of 15%, and calculate it on a country-by-country basis instead of averaging a company's tax rate across jurisdictions. The Biden Administration also proposed eliminating FDII, which would remove the incentive for firms to keep intellectual property within the U.S.

Throughout the entirety of President Biden's term, Republicans in Congress raised concerns about the administration's failure to advocate for U.S. interests in the negotiations. Pillar One as negotiated by the Biden Administration unfairly targets the U.S. tax base as the vast majority of profits to be reallocated to other taxing jurisdictions would be from U.S. firms. Former Treasury Secretary Janet Yellen suggested implementing this without approval from Congress, where the Senate must ratify any treaties at a 60-vote threshold.

Pillar Two fails to "grandfather" GILTI as an acceptable global minimum tax despite the U.S being a first-mover in the creation of minimum taxes, and fails to treat U.S. tax incentives like the nonrefundable research and development (R&D) tax credit as favorably as European refundable tax credits. It is also problematic in terms of its complexity, its approach to dispute resolution, and its ability to be circumvented through refundable tax credits.

Both Pillars would result in significant revenue loss for the U.S. without the most basic benefits that were originally expected for the U.S., such as elimination of DSTs.

How Will Trump Move Forward?

Pillar One is at a standstill at the moment, with the OECD missing a June 2024 deadline for all countries to sign the agreement, which would need to be ratified by the U.S. Senate before implementation. Pillar Two is moving forward separately, with at least 45 countries already legislating a global minimum tax. Importantly, Congress would also need to legislate any changes to the U.S. global minimum tax GILTI, which phases out beginning in 2026.

President Trump's campaign promises and his prior actions at the OECD give insight into his path forward for both the OECD and GILTI. If President Trump seeks to continue his advocacy for U.S. interests in the international tax space, he can do so by leaving the OECD discussions entirely or pushing for an approach that would be more favorable to the U.S. than the Biden Administration's approach.

Leaving the Table

It is clear that the deal that has been negotiated at the OECD will be unacceptable for the incoming Trump Administration. It is also unacceptable for the majority of Republicans in

Congress, some of whom have called for defunding the OECD in response. Even Democrats are opposed to DSTs, which Pillar One fails to adequately address. Given that Pillar One will remain unimplemented without U.S. action, and the U.S. stands to lose revenue regardless of whether it implements Pillar Two alongside the rest of the world, there is a clear and easy path to leaving the negotiating table at the OECD.

Unfortunately, U.S. inaction would likely result in continued implementation of DSTs in other countries and implementation of the UTPR which would be used as an extraterritorial tax against U.S. firms. If the Trump Administration decides to leave the table entirely, it will have to negotiate with countries unilaterally to address these concerns.

Keep Negotiating

The U.S. could instead stay at the negotiating table and demand changes to the current agreement that better reflect the U.S. interests that Trump's first administration tried to preserve.

Pillar One includes Amount A, which is the reallocation of taxing rights, as well as Amount B, which is an agreement on transfer pricing. The Trump Administration can stay at the negotiating table to come to a consensus around Amount B.

Creating new transfer pricing rules would result in tax stability and simplicity in this area, yet U.S. business leaders have raised concerns that Amount B in its current form as a limited and optional provision would not provide the intended benefits. As of now, Amount A and Amount B do not depend on each other, therefore the administration could theoretically move forward with one separately.

The Trump Administration can also continue negotiating Amount A, but should only do so if it intends to prioritize the elimination of DSTs and any similar national-level taxes, including diverted profits taxes (DPTs), offshore receipts tax (ORT), and multinational anti-avoidance laws (MAALs). Amount A in its current form would reduce the U.S. tax base without securing the total elimination of discriminatory DSTs. Amount A could be made more palpable if the share of U.S. profits to be reallocated was reduced relative to the share of profits shifted from other taxing jurisdictions and if the agreement resulted in the elimination of DSTs.

Trump can also continue negotiating Pillar Two, the global minimum tax. This approach should prioritize grandfathering in GILTI as a compliant global minimum tax. This would help shelter U.S. companies from the extraterritorial reach of the UTPR. The Trump Administration can also advocate for a more limited version of the UTPR, previously known as the Under-Taxed Payments Rule. If they decide to continue negotiations, the administration should take the advice of the domestic business community and address concerns regarding safe harbors and dispute resolution.

Republicans in Congress may also wish to make changes to GILTI, FDII, and BEAT in light of their changes beginning with TCJA expiration in 2026. For example, Tax Foundation has recommended changing the way GILTI interacts with Foreign Tax Credits (FTCs). While the OECD would like to see the U.S. make other changes to GILTI, such as calculating it on a country-by-country basis, there are concerns that this would result in minimal benefit with an extremely high compliance cost. The Trump Administration can factor in any changes it may wish to make to TCJA's international tax provisions while negotiating with the OECD.

Retaliation

President Trump has already signaled his intent to implement retaliatory tariffs on other countries in response to a host of issues. He takes credit for France pausing its digital services tax in 2020 after the threat of imposing tariffs on champagne and other goods under Section 301 of the Trade Act of 1974. The pause may have been sensible at that time in the context of the upcoming 2020 U.S. presidential election and ongoing OECD negotiations. However, when OECD negotiations failed to resolve the situation, France reinstated its tax and later announced plans to double it.

The path forward is challenging. While President Trump will likely have authority to levy tariffs in response to either Pillar One or Pillar Two, and may have the backing of Congress, doing so would be a blow to American taxpayers. If unilateral tariff threats failed to achieve their intended goals, the resulting U.S. tariffs would interrupt trade and cause a price spike on many consumer goods, and given the amount of countries implementing parts of the OECD deal, retaliatory tariffs could impact much more than sparkling wine. Replacing President Biden's spending-fueled inflation with "tarifflation" would be the worst path forward for the Trump Administration. For example, Section 301 tariffs imposed on China have cost the equivalent of more than $1,700 per household so far while failing to change that country's harmful policies.

President Trump can also use tax levers to retaliate against foreign countries that use DSTs or the UTPR against American businesses. Section 891 of the tax code specifically provides that the president can double the tax rate on citizens and businesses of countries that impose extraterritorial taxes on U.S. citizens or companies. This retaliatory option has been identified by former U.S. Treasury officials, members of Congress, and thought leaders. Using Section 891 would hurt foreign citizens who pay American taxes but would have much less impact on the American economy as a whole than retaliatory tariffs.

Conclusion

While the rest of the world clamors for a piece of the American tax base through the OECD negotiations, it is the job of our government to advocate for the interests of our taxpayers. The Biden Administration failed to bring certainty to the public or Congress throughout the negotiations.

Continuing negotiations could be beneficial to some U.S. policy goals such as eliminating DSTs, but it would be unacceptable to remain at the negotiating table if the issues are not properly addressed. Lawmakers must also factor in expiring business and international tax provisions of the TCJA, which will require a reflection on the benefits of those reforms.

President Trump is in a strong position to make demands on behalf of American taxpayers, but he should not jeopardize their prosperity with retaliatory tariffs in the process. It would be wise to re-enter discussions from the place he left off, protecting American interests, rather than continuing the track of the prior administration.

There are still many issues to resolve in the international tax negotiations which will require significant time and discussion. The OECD should consider pursuing an agreement that halts DSTs and Pillar Two implementation while these discussions are ongoing.