Repurposing Pillar One into An Incremental Global Tax for Sustainability: Some Blue Sky Thinking in the Midst of Global Crisis

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Repurposing Pillar One into an Incremental Global Tax for Sustainability: A Collective Response to a Global Crisis

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This article proposes to repurpose the OECD/IF Pillar One Blueprint from a taxing rights reallocation mechanism into an incremental global tax for sustainability. With a common goal and DST-like feature for simplification, the proposal aims to ease the negotiation of essential and drastic simplifications required to deliver a workable solution.

1. Introduction

Our world is facing an unprecedented climate, social and economic crisis. There is literally no "Planet B".[1]The COVID-19 pandemic reveals the pre-existing fiscal and other vulnerabilities of nations. The climate crisis is "a global fight".[2]Sustainable development is a common goal of humankind.[3]No country alone has the political power or the economic means to solve global problems. No sustainable development agenda can be achieved without business.[4]It is incumbent upon the global community to work together and enable corporations to contribute more to solving social and environment problems. This was clearly stated by the G20 Finance Ministers on 7 April 2021: "[T]ackling climate change and promoting environmental protection are increasingly urgent for our economies and societies", and "mobilizing sustainable finance is essential for global growth and stability and for promoting the transitions towards greener, more resilient and inclusive societies and economies".[5]

In the midst of global crisis, the issue of how to fairly tax the world's largest and most profitable multinational enterprises (MNEs) (the winners of globalization in a digitalizing economy) has received unprecedented attention by political leaders,

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1. United Nations, Department of Economic and Social Affairs, UN Secretary-General and top business leaders agree on steps to scale up investment in sustainable development", 14 October 2020 (UN Newsletter), available at https://www.un.org/development/desa/en/news/financing/global-investors-for-sustainable-development-alliance.html (accessed 2 May 2021)
2. The White House, "Remarks by President Biden in Address to a Joint Session of Congress", 28 April 2021, available at https://www.whitehouse.gov/briefing-room/speeches-remarks/2021/04/29/remarks-by-president-biden-in-address-to-a-joint-session-of-congress/ (accessed 2 May 2021) (hereinafter "President Biden's Remarks").
3. In 2015, all 193 United Nations (UN) member states unanimously committed to achieving 17 SDGs by 2030. The SDGs are: (1) end poverty in all its forms everywhere; (2) end hunger, achieve food security and improved nutrition and promote sustainable agriculture; (3) ensure healthy lives and promote well-being for all at all ages; (4) ensure inclusive and equitable quality education and promote lifelong learning opportunities for all; (5) achieve gender equality and empower all women and girls; (6) ensure availability and sustainable management of water and sanitation for all; (7) ensure access to affordable, reliable, sustainable and modern energy for all; (8) promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all; (9) build resilient infrastructure, promote inclusive and sustainable industrialization and foster innovation; (10) reduce inequality within and among countries; (11) make cities and human settlements inclusive, safe, resilient and sustainable; (12) ensure sustainable consumption and production patterns; (13) take urgent action to combat climate change and its impacts; (14) conserve and sustainably use the oceans, seas and marine resources for sustainable development; (15) protect, restore and promote sustainable use of terrestrial ecosystems, sustainably manage forests, combat desertification, and halt and reverse land degradation and halt biodiversity los; (16) promote peaceful and inclusive societies for sustainable development; and (17) provide access to justice for all and build effective, accountable and inclusive institutions at all levels (hereinafter the "UN SDGs").
4. *See* H. Clark, at the time head of the UN Development Programme (UN News Centre, 2015).
5. Italian G20 Presidency, Second G20 Finance Ministers and Central Bank Governors meeting, Communiqué, 7 April 2021 (hereinafter the "Communiqué"), available at https://www.g20.org/2nd-finance-ministers-and-central-bank-governors-meeting.html (accessed 2 May 2021).

business leaders, academia, non-profit organizations and the general public. Impressive proposals[6]have been crafted by the G20/OECD Inclusive Framework in the form of the Pillar One Blueprint[7](reallocation of taxing rights over residual profit derived from automated digital services or ADS and consumer facing businesses or CFB) and the Pillar Two Blueprint (a global minimum tax on large MNEs)[8]as well as by others.[9]And yet, these tax debates seem to be happening in a virtual isolation from the global crisis.

While aiming to improve fairness, fortify the existing international tax system and reallocate taxing rights,[10]the Pillar One Blueprint (hereinafter the "Blueprint") shows tremendous progress in approaching MNEs' profit on a group basis, using a formulaic method in allocating residual profit attributable to market (hereinafter the "market-based profit"), and creating a multilateral tax certainty process. On the other hand, the Blueprint has created a level of technical complexity and legal challenges in implementation that may make it difficult to win international consensus.[11]Uncertainty about "winners" and "losers" if the Blueprint were to become reality affects political and fiscal sensitivities of different countries differently. The recent proposal[12]by the United States to broaden the scope of activities covered while reducing the number of MNEs covered by the Blueprint may offer some opportunities for simplification and greater chance of broader political support, but also add new areas of complexity, such as sourcing of sales revenue for business-to-business services. Even though a high-level political consensus may be achieved in mid-2021, the devil is in the detail. Turning the Blueprint into a reality will be challenging.

What is absolutely certain is that governments need revenue to fight the global crisis. This is particularly true during and immediately after the COVID-19 pandemic. What is also certain is that the world's largest and most profitable MNEs, while increasingly committed to shouldering social responsibilities, are also perceived as not paying their fair share of taxes.[13]Recent studies continue to demonstrate that the larger the MNE, the lower the effective tax rate.[14]As explained by the economic study supporting the G20/OECD BEPS Project, this is because "MNEs can take advantage of international differences in corporate tax systems to reduce their tax burden."[15]The launch of the G20/OECD BEPS Project in 2013 and the efforts of tax reform through Pillar One and Pillar Two are testaments to the existence of a consensus on the need for better internationally coordinated tax rules that require MNEs to pay their fair share of taxes.[16]No MNE that submitted public comments on the Blueprint[17]objected to the need for better international rules.

While almost everyone prefers a global solution, there is a reasonable doubt as to if, and when, such solution can materialize to bring about tax revenues for governments and create a level playing field for businesses. Many countries have introduced a digital services tax (DST) and some are planning to introduce one if no global consensus is reached in the near future.[18]In other words, some governments are prepared to do it alone, even in the face of potential trade conflicts with the United

6. For an overview and evaluation of the proposals, *see* R. Collier, M.P. Devereux & J. Vella, "Comparing Proposals to Tax Some Profits in the Market Country", available at https://oxfordtax.sbs.ox.ac.uk/publications (accessed 11 May 2021) .
7. OECD, *Tax Challenges Arising from Digitalisation – Report on Pillar One Blueprint* OECD/G20 Base Erosion and Profit Shifting Project (OECD 2020) (hereinafter the " *Pillar One Blueprint Report"*).
8. OECD, *Tax Challenges Arising from Digitalisation – Report on Pillar Two Blueprint* OECD/G20 Base Erosion and Profit Shifting Project (OECD 2020).
9. For example, article 12B added to the UN Model in April 2021 permits the source state to impose withholding tax on income from automated digital services arising in that state, available at http://www.un.org/development/desa/financing/sites/www.un.org.development.desa.financing/files/2020-08/TAX%20TREATY%20PROVISION%20ON%20PAYMENTS%20FOR%20DIGITAL%20SERVICES.pdf (accessed 2 May 2021).
10. OECD, "Cover statement" in *Pillar One Blueprint Report* , *supra* n. 7 .
11. OECD, Tax Challenges Arising from Digitalisation: Public Comments Received on the Pillar One and Pillar Two Blueprints, available at https://www.oecd.org/tax/beps/public-comments-received-on-the-reports-on-pillar-one-and-pillar-two-blueprints.htm (accessed 2 May 2021) (hereinafter the "Public Comments"); M. J. Graetz, *A Major Simplification of the OECD's Pillar 1 Proposal* (2021) Tax Notes Int'l 199-210; J. Li, *The Legal Challenges of Creating a Global Tax Regime with the OECD Pillar One Blueprint* , 75 Bull. Intl. Taxn. 2 (2021), Journal Articles & Opinion Pieces IBFD.
12. J. Martin, "Leaked copy of US proposal for Pillar One and Pillar Two multinational group tax reforms available", available at https://mnetax.com/leaked-copy-of-us-proposal-on-multinational-group-tax-reforms-available-43379 (accessed 2 May 2021) (hereinafter the "US Proposal").
13. The notion of "fairness" is further discussed in section 4.6.1. Whether an MNE is paying its fair share of taxes may be determined by reference to the mismatch between the level of activities in a country and the level of taxable profit reported in that country. Information obtained from country-by-country reporting suggests that the mismatch is real and significant in some cases: the level of profit reported in investment hubs exceeds that of activities in those jurisdictions. *See* , for example, A. Fortier-Labonte and C. Schaffter, *Indicators of profit shifting by multinational enterprises operating in Canada,* Statistics Canada, Catalogue No. 11-621-M, 18 June 2019. Other studies found MNEs shifting profits to tax havens: *see* , for example, K.A. Clausing, *How Big is Profit Shifting?* (17 May 2020), available at http://dx.doi.org/10.2139/ssrn.3503091 (noting that USD 4.2 trillion in offshore earnings revealed by the US Country-by-country data, USD 3 trillion of which is in known havens or countries with effective tax rates below 10%) (accessed 11 May 2021).
14. Report commissioned by the Greens/EFA on the Effective Tax Rate for Multinational companies in the EU, available at https://www.greens-efa.eu/files/doc/docs/356b0cd66f625b24e7407b50432bf54d.pdf) (accessed 11 May 2021).
15. OECD (2017), "Tax Planning by Multinational Firms: Firm-level Evidence from a Crosscountry Database", Economics Departments Working Papers, No. 1355, at para. 1, available at https://www.oecd.org/economy/public-finance/Tax-planning-by-multinational-firms-firm-level-evidence-from-a-cross-country-database.pdf (accessed 11 May 2021).
16. OECD (2013), Action Plan on Base Erosion and Profit Shifting, OECD Publishing, Paris, available at https://doi.org/10.1787/9789264202719-en (accessed 11 May 2021).
17. Public Comments, *supra* n. 11 .
18. *See* section 3.1.

States[19]and violations of bilateral tax treaties.[20]MNEs are faced with the burden of complying with multiple national tax regimes.

At this moment, we have a global consensus on fighting the climate crisis (Paris Agreement)[21]and achieving sustainable development goals set by all nations of the United Nations (UN SDGs)[22]on the one hand, and a lack of consensus on the taxation of MNEs on the other hand. What can be done to mobilize national governments to act together on the tax front? In this article, we seek to tackle this question.

First, we propose to instill some values into the heart of the tax debates by linking taxation of MNEs to the global fight in achieving sustainable development, climate control and economic recovery post-pandemic (hereinafter collectively referred to as "sustainability"). A global fight requires global efforts, which should not be bogged down by some technical details.

Second, we propose to repurpose Pillar One as described in the Blueprint from a mechanism of reallocating tax base under existing corporate income tax (CIT) to an incremental global tax on the largest and most profitable MNEs' market-based profit. As a new, standalone tax on MNEs – tentatively referred to as "Tax for Sustainability" – this proposed tax will define taxpayers and tax base in a way that is similar to those under the Blueprint, but will provide simpler computation and administration methods and, like a DST, will be separate from the existing CIT.

Our proposed Tax for Sustainability is an evolved version of the Blueprint pivoted in a new, collective-oriented direction to achieve two inter-connected objectives: (i) like the Blueprint, it would clearly establish the right of market jurisdictions to tax a portion of an MNE group's market-based profit; and (ii) more significantly, it would create a common instrument for all governments to tax MNEs in order to finance the common expenditures on sustainability.

The analogy of all countries collectively owning the Earth (*see* section 2.1.) helps explain this pivotal shift in thinking about taxation of MNEs. Our proposal builds on the idea of a new rent for MNEs to recognize the fact that they profit from the global market infrastructure and should contribute more to its sustainability.

In tax jargon, the proposed Tax for Sustainability is a new incremental tax on the global profit of MNEs that will help finance the common expenditures on sustainability and climate change. For ease of implementation, this tax will apply only to the largest and most profitable MNEs. It can be imposed in a manner similar to a DST. In the future, it can further evolve into a comprehensive regime for taxing MNEs when countries can agree on a formulary apportionment system.

In terms of technical design, the adoption of a DST-type delivery mechanism could be achieved through a conversion formula (*see* section 4.3.1.). In essence, an adjustable tax rate applicable directly to sales (i.e. like a DST) can replicate the effect of a CIT rate applicable to net profit. This offers the advantage of developing further simplification options, but, most importantly, it will help untangle the new tax from the complex transfer pricing rules that would be necessary to prevent double taxation under the existing CIT system.

The Tax for Sustainability could also be delivered through a CIT-type mechanism (and would contain the necessary elements to potentially become a comprehensive system of taxing MNEs on formulary apportionment). We propose a small step at the moment and recommend the DST-type delivery mechanism without foreclosing the use of the CIT-like option, and a credit/ exemption system in exceptional cases.

The immediate benefit of our proposal is to, hopefully, break any potential deadlock in negotiation of essential (and sometimes drastic) simplification required for the Blueprint to deliver a workable solution that countries can agree to. It can generate new revenue for all participating governments, thereby removing the need for balancing the interests of potential fiscal winners and losers as a result of reallocation of taxing rights under the Blueprint. All participating governments are potential winners under our proposal as achieving sustainability is the common goal. MNEs, especially those that are large and profitable, will contribute to the common cause as global corporate citizens, which can certainly help improve their image and reputation.

Through repurposing Pillar One into a global tax for sustainability, we hope governments and businesses can seize upon a unique opportunity to create a global tax instrument that is fit for a digitalizing global economy and capable of assisting in the global fight against climate change and social and economic insecurity. Governments can even develop concrete ways to commit the new tax to achieving their sustainable development goals.

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19. Office of the United States Trade Representative, "USTR Announces Next Steps of Section 301 Digital Services Taxes Investigations", 26 Mar. 2021, available at https://ustr.gov/about-us/policy-offices/press-office/press-releases/2021/march/ustr-announces-next-steps-section-301-digital-services-taxes-investigations (accessed 2 May 2021).
20. Articles 5 and 7 of bilateral tax treaties typically do not allow the source country to tax business profits of an enterprise resident in a treaty country in the absence of a permanent establishment located in the source country.
21. The Paris Agreement (UN 2015) is a legally binding international treaty on climate change; it binds all nations into a common cause to undertake ambitious efforts to combat climate change and adapt to its effects: available at https://unfccc.int/sites/default/files/english_paris_agreement.pdf (accessed 2 May 2021).
22. *See* UN SDGs, *supra* n. 3 .

In the rest of the article, we will first explain why repositioning the tax debates is important at this moment (*see* section 2.) and why our proposal is grounded in the momentum built up thus far (*see* section 3.). We then present the nature, purpose and guiding principles of the proposed tax (*see* section 4.) as well as the technical system design (*see* section 5.) to show how it is repurposed from the Blueprint and offers simplicity and certainty. We make a case for taking the proposal seriously at this juncture and keeping the common goal and big picture in mind when tackling technical details (*see* section 6.).

2. Why Repurposing Pillar One?

2.1. An analogy: Common crisis demanding a collective response

Imagine the world as our home: a large and wonderful condominium building of mysterious design. In this building, each state owns its own individual part, to use it or lease it to individuals and businesses for personal or commercial use. New technologies have allowed large businesses to expand into the common space around the building and to become commercially connected to more units without increasing their physical presence there. Meanwhile, they continue to enjoy the building's general infrastructure and services.

In the past, the co-owners agreed to respect each other’s sovereignty, appointed some common agents to oversee some common issues and created mechanisms for dealing with emergency situations, such as peacekeeping and disaster relief. Some owners chose to set a high rent to cover the expenditure needs in their unit, and others chose to charge a low rent. They all agree that the basis for charging the rent is use of the unit space. In recent years, however, the building’s roof is on the verge of collapsing, the ground floor is tilting, the air ventilation is broken and there are leaks in the water pipes, polluting the water. As if this were not enough, deadly viruses are spreading throughout the building, and everyone is affected.

The unit owners therefore agreed in 2015, through the UN SDGs and Paris Agreement, to deal with these common problems and set up specific goals. Each unit owner has been relying on its own fiscal resources to address these common problems.

Since 2013, many unit owners desired to revisit the issue of rent they can charge to the MNEs to reflect the new realities. At the same time, leaders of these MNEs are increasingly aware that the long term success of their business depends on the unit-owners getting together to fix the common areas and building infrastructure that have been awfully neglected over the years; they too want to contribute to fixing the building.

Aided by the technical expert advice from the OECD and led by some of the largest unit owners, the co-owners decided that a new basis for charging unit rent to those MNEs should be created, but have not yet agreed on exactly how the new type of rent (hereinafter the “new unit rent”) should be quantified and not doubly charged on the same MNE also renting a commercial space in particular units.

In the actual world, this coincides with the level of progress evidenced by the Blueprint regarding a new taxing right over market-based profit. The general understanding of the new taxing right (i.e. the analogous new unit rent) is based on the MNEs’ use of the market of a jurisdiction, physically or remotely. But, under the Blueprint, the assumption is that the new taxing right in market countries is not a new tax, but merely a reallocation of a taxing right from one country to another. If the countries whose taxing rights are reallocated away to market jurisdictions do not provide relief, the Blueprint considers that there will be double taxation (i.e. double charging of a rent). Determining which of the entities within the MNE group are earning the profit that has been reallocated to market countries (and hence which countries should provide relief) is complex, mainly due to its interaction with existing CIT rules (such as the arm’s length principle and its associated transfer pricing rules). The consolidated profit of the MNE which forms the basis for the new tax has, under the Blueprint, to be “de-consolidated”. No simple formula could do this as the profit of each individual entity is intrinsically linked to existing transfer pricing rules.

Our proposal extends the thinking about the new unit rent: it proposes a new rent for the expansion of the business of an MNE in the common areas, using the size of its revenues and its profitability as proxies for the space and infrastructure it uses. Furthermore, instead of charging such rent using the CIT regime, our proposal creates a new system for the computation and payment of such rent.

Repurposing Pillar One towards an incremental global tax on MNEs for the common goal of fighting global crisis serves two critical purposes. The first one is to prevent a possible deadlock in the negotiation of the practical details and political negotiation of the Blueprint. The second is to commit the tax to such common purpose that it can provide a win, win, win outcome for governments, MNEs and the planet.

2.2. A common purpose dwarfing technical differences

There is nothing like a crisis to focus the mind and spur innovative solutions. The global community has already focused the collective mind on sustainable development through the 17 UN Sustainable Development Goals (SDGs)(2015)and climate change through the Paris Agreement (2015). Meanwhile, national governments all need tax revenue to fight the global crisis but have acted in more or less isolation or in competition with other countries in tax policy concerning MNEs. MNEs have benefited from digitalization and globalization and are in a position to contribute to the global fight, but no legal mechanism exists to facilitate that contribution. The G20/OECD Inclusive Framework on BEPS began the process of shifting towards a more collaborative approach to taxing MNEs through the Blueprint. The next logical extension is for the collective of governments working together to include MNEs in fighting the global crisis through a global tax mechanism.

Instilling a common purpose into the tax debates should help guide the selection of simpler technical design options towards achieving the common purpose. The end justifies the means in this time of crisis, within reasonable parameters, of course. There is a broad agreement that the current Blueprint needs to be significantly simplified to become manageable, as the current burden of compliance would likely exceed any potential gain. Simplification remains important with the US proposal as it would require a flexible approach to sourcing rules as a result of covering a wider range of activities.[23]

Having a common purpose should make it easier to find common ground at a technical level. For example, the sourcing rules need not be perfect in pinpointing the location of sales in each and every situation or business model when such information is not readily accessible; a reasonable approximation by the MNE might be just fine as long as there is sufficient degree of certainty and accuracy. Also, uniting around a common goal and the use of the tax revenue to achieve it would help bridge the divergence over difficult design issues, such as the degree of precision regarding the computation of the allocable profit and allocation key, the determination of who should give a credit for the tax levied by other countries or who should control the tax administration and certainty process. In other words, linking the taxation of MNEs to the common purpose should liberate us from the technical quagmire of complex design options and enable us to accept compromising on accuracy for greater simplicity. Indeed, what will matter most is not so much who gets to tax what, but rather how countries will use the new tax revenue to finance the common objective. To take our earlier analogy of unit rent, what is important is that the additional rent goes to repairing and maintaining the common areas and the building's infrastructure.

Repurposing Pillar One into an incremental global tax would likely reduce the level of political sensitivities for technical tax experts, especially sensitivities associated with uncertainty about potentially winning or losing tax revenue as a result of reallocation of taxing rights and relief for double taxation. Given the small amount of tax revenue potentially reallocated through the Blueprint,[24] it would be an historical mistake to see Pillar One collapse for the potential loss of small amounts of revenue of a small number of countries in the face of the global fight for sustainability. For low-capacity countries whose economic resources are dwarfed by those of large MNEs, collaborating with other governments in introducing a global tax might be the only feasible means to tax a small portion of MNEs' group profit.

2.3. A triple win approach

Conceptualizing the taxation of MNEs' global profit from the perspective of financing the achievement of global objectives would be a win, win and win proposition.

The first win would go to governments. This conceptualization would help justify the introduction of an incremental tax on MNEs. As a new tax, it would generate new revenue as opposed to moving tax revenues from one country (such as investment-hub jurisdictions or headquarter jurisdictions) to another (market jurisdictions). It would help mitigate the concerns about relieving double taxation, which were attempted by the ambitious rules in the Blueprint. As explained in section 4., our proposal is to separate this tax from the existing corporate tax system and not to provide a credit against other corporate income taxes, at least not until the MNEs' effective normal CIT rate exceeds a certain rate. Therefore, all governments will be winners. They would have a revenue stream, which may be modest at the inception, to meet their sustainable development goals.

MNEs would also be winners, at least from the public perspective. They benefit from the public infrastructure (physical, legal and digital) and market conditions (including enabling customers and users to generate data) that correlate to sustainable development. Paying taxes will help the financing of sustainable development, which will equally benefit MNEs and ensure they will have consumer markets in the future. It also provides a legal mechanism for MNEs and their representatives to contribute to the common cause without running afoul with corporate governance rules. In a way, while MNEs can continue to operate in a legalistic world of taxation that permits aggressive tax planning, which is considered by some to be incompatible with the MNEs' social responsibility,[25] an incremental tax provides a legal framework for them to meet the growing demand for acting like responsible citizens of this world and partners in the global fight.

23. US Proposal, *supra* n. 12.
24. OECD, *Tax Challenges Arising from Digitalisation – Economic Impact Assessment,* at para. 154 (OECD 2020).
25. *See*, for example, R.S. Avi-Yonah, *Corporate Taxation and Corporate Social Responsibility*, 11 NYU J. of Law & Business 1 (2014), pp. 1-28; H. Gribnau, *Corporate Social Responsibility and Tax Planning: Not by Rules Alone*, 24 Social & Legal Studies 2 (2015) pp. 225–250; H. Gribnau & A-G. Jallai, *Good Tax Governance: A Matter of Moral Responsibility and Transparency*, Nordic Tax Journal 1 (2017) pp. 70-88.

The biggest winner might be our planet, our economies and our societies. By taking a small step in treating MNEs as global citizens and taxpayers,[26]our proposal may help unite the interests of governments and MNEs and unshackle some technical constraints that prevent countries from reaching a consensus. If so, a global tax instrument would be created to help finance sustainability and protection of the environment. To paraphrase Neil Armstrong,[27]the proposed tax is one small step for MNEs and countries, but a giant leap towards a more sustainable future.

3. State of Play

3.1. Pivoting towards consensus

The proposal pivots the search for a consensus on Pillar One towards a common goal and offers a technical solution that provides the simplicity and certainty of a DST-like delivery mechanism as well as a potentially more effective and elegant regime of CIT for MNEs. And yet, it is based on the foundational doctrine of economic allegiance as well as the momentum on recent international tax reforms and corporate social responsibility.

3.2. Broad consensus on principles

The Blueprint is concerned with the taxation of MNEs' income, and thus forms part of the CIT system. Why tax corporate income in the first place since taxes are borne by and ultimately benefit people? If corporate income could be allocated to the owners of the corporation annually for income tax purposes, there would be no need for taxing corporations. In reality, however, for pragmatic reasons, it is administratively easier and politically more acceptable to tax corporations, especially foreign-owned corporations.[28]Corporate tax revenue is generally more important in developing countries than in developed countries.[29]It can be said, therefore, there is a general consensus on the relevance of corporate taxation.

A country's entitlement to tax an MNE can be explained by the doctrine of economic allegiance framed by the Four Economists in their report to the League of Nations in 1923.[30]According to this doctrine, a person's total tax liability is owed to "all those governments to whom the individual owes economic allegiance" or, in other words, to each of those governments "which render him service".[31]Governments provide services to taxpayers in connection to the production of wealth, possession of wealth and disposition of wealth. In the case of production of wealth, multiple stages are involved, which is illustrated by the following example:

> The oranges upon the trees in California are not acquired wealth until they are picked, and not even at that stage until they are packed, and not even at that stage until they are transported to the place where demand exists and until they are put where the consumer can use them.[32]
>
> The origin of the wealth therefore may have to be considered in the light of the original physical appearance of the wealth, its subsequent physical adaptations, its transport, its direction and its sale.[33]

The degree of economic allegiance is difficult to quantify in each and every situation. Practical compromises or arbitrary assignment were adopted in the initial model tax conventions developed by the technical experts of the League of Nations.[34]These model conventions form the basis of a vast network of tax treaties, approaching 4,000 in total. A country's entitlement to tax is tied to the residence of a corporation or the source of the corporate income (i.e. the residence/source paradigm). Presumably, a country provides service to a corporation as a host of the head office or income-earning activity

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26. As mentioned in, *infra,* notes 53 and 54, the values of shareholders of MNEs need to be aligned with the common purpose as well. These shareholders may demand transparency and accountability from the management of MNEs on their international tax behaviours.
27. *See* J.R. Hansen, *First Man: The Life of Neil A. Armstrong* (Simon & Schuster, 2005), at p. 493.
28. *See* R.M. Bird, *Why Tax Corporations?* A working paper prepared for the Technical Committee on Business Taxation, Canada, 1996, available at https://www.ecn.ulaval.ca/~sgor/cit/bird_FinanceCanadaWP_1996/whytaxcorps.pdf (accessed 11 May 2021). Also, because capital income is generally undertaxed under the personal income tax system, taxing corporate income is "integral to taxing income (including excess returns), and taxing capital is an important part of the larger income tax system": *see* K.A. Clausing, *Taxing Multinational Companies in the 21st Century* in J. Shambaugh and R. Nunn, eds. Tackling the Tax Code: Efficient and Equitable Ways to Raise Revenue (Washington DC: Hamilton Project, 2020), at p. 241.
29. *See* , for example, M.C. Durst, *Taxing Multinational Business in Lower-Income Countries: Economics, Politics and Social Responsibility* (ICTD, 2019), available at https://www.ictd.ac/publication/taxing-multinational-business-lower-income-countries-economics-politics-social-responsibility/ (accessed 11 May 2021).
30. Professors Bruins, Einaudi, Seligman & Sir Josiah Stamp, *Report on Double Taxation* , submitted to the Economic and Financial Commission of the League of Nations, Document E.F.S.73.F.19, 5 April 1923 (hereinafter the "1923 Report"), available at https://www.taxtreatieshistory.org/
31. Id., at p. 20.
32. Id., at p.23.
33. Id., at p.24.
34. S. Jogarajan , *Double Taxation and the League of Nations* (Cambridge University Press, 2018). For the influence of these earlier model conventions today, *see* *OECD Model Tax Convention on Income and on Capital* (21 Nov. 2017), Treaties & Models IBFD, and *UN Model Double Taxation Convention between Developed and Developing Countries* (1 Jan. 2011), Treaties & Models IBFD.

through maintaining the necessary legal and business environment, including a market. Going back to our earlier analogy of unit rent, a country charges rent from a corporation for the hosting service.

A market country's taxing right is embedded, but not explicitly stated, in the OECD Model or the UN Model. In the case of tangible goods, until the rise of digitalization, a corporation typically penetrates a market through setting a local subsidiary or permanent establishment (PE), and Article 7 recognizes the host of the market to tax the profit attributable to the subsidiary or PE. In the case of oranges from California, for example, if the oranges are sold by a US corporation in Canada through a Canadian subsidiary or PE, Canada has the right to tax the subsidiary's income or the US corporation's profit attributable to the Canadian PE.[35]Nowadays, the US corporation can sell oranges without a Canadian subsidiary or PE. Even though Canada does not provide service directly to the US corporation in terms of workforce and physical infrastructure, it does so indirectly because oranges still need to be packed and made available to the final customer. Canada's capacity to create and maintain a market for the oranges remains unchanged. The fact that the technical definition of PE may need to be modernized for the digital age does not mean Canada's entitlement to tax the sales profit is new.

In fact, a common theme between the Blueprint, article 12B and DSTs is to reaffirm a market jurisdiction's entitlement to tax based on the doctrine of economic allegiance.[36]Article 12B permits the market country to levy a withholding tax on income from automated digital services. Over 10 jurisdictions have adopted a DST[37]and about the same number of jurisdictions have announced the adoption of a DST,[38]and so did the European Union and the African Tax Administration Forum (ATAF). Moreover, 15 other jurisdictions[39]have also made public statements to that effect.

The United States, which is the largest market and home-base of most of the largest MNEs, also recognized market jurisdictions' right to tax based on sales. Its recent proposal[40]seeks to refine the means of identifying the "renters" and the "scope of use" by reducing the number of MNEs covered under the Blueprint using objective, quantitative criteria based on a high turnover threshold (USD 20 billion) and a profit margin (not yet specified). It does not challenge the right of market jurisdictions to tax market-based profit. The US proposal prefers to see definitive commitments from participating jurisdictions to withdraw their unilateral measures, such as DSTs when they participate in the multilateral approach proposed by the Blueprint in order to, among others, prevent excessive, overlapping charges on MNEs.

At this moment, one can say that there is political consensus on the doctrine of economic allegiance that is embedded in the existing tax treaties and on the right of market jurisdictions to tax market-based profit.

3.3. Areas of technical consensus under Pillar One

Since the launch of the G20/OECD BEPS Project in 2013, there has been universal agreement among governments and MNEs on the necessity of tax reform and the importance of undertaking the reforms at an international level.

There is an impressive consensus among governments, businesses and academics on a key aspect of reforming the international tax system: the time has come to view large MNEs operating globally as cohesive units, not as aggregated units of separate entities. The Blueprint does not raise this as an issue, but rather as a starting point. This is one of the most important aspects of the international tax reform: taxation is finally catching up with the economic and social reality of MNEs.

Other key areas of consensus are also emerging, including:

- An inclusive process and political consensus are critical preconditions for building consensus on the technical reform measures.
- Targeting the largest and most profitable MNEs.
- Reconceptualization of the taxation of MNEs and their "residual" profit as one economic and taxable unit. An MNE's profit includes routine profit and residual profit and a portion of the residual profit is attributable to a market jurisdiction in the absence of physical presence or nexus in the traditional sense (i.e. market-based profit).
- Using a simple and formulaic approach to compute the market-based profit.

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35. This is governed by the Canadian Income Tax Act, RSC 1985, c1 (5th supp.), paragraph 2(3)(b) and article 7 of the *Convention between Canada and the United States of America with Respect to Taxes on Income and on Capital* (as amended through 2007), Treaties & Models IBFD.
36. Collier, Devereux & Vella, *supra* n. 6 .
37. Austria, France, Hungary, India, Italy, Kenya, Sierra Leone, Spain, Tunisia, Turkey and the United Kingdom.
38. Belgium, Brazil, Canada, Czech Republic, Israel, Latvia and New Zealand.
39. Australia, Cambodia, Chile, Denmark, Egypt, Ivory Coast, Japan, Korea (Rep.), Netherlands, Norway, Poland, Russia, Slovak Republic, Slovenia and South Africa.
40. US Proposal, *supra* n. 12 .

- The determination of market-based profit should be based on consolidated financial income as opposed to the aggregate of tax income determined under the national laws of each relevant jurisdiction.
- Using proxies in allocating the countries' share of the market-based profit. The jurisdiction-by-jurisdiction allocation of such profit is based on a formula as opposed to the current transfer pricing methods. As such, the amount of profit allocated to each jurisdiction is notionally correlated to the benefit derived by an MNE from that jurisdiction.
- The allocation key should be the sales in jurisdictions (as modified to include revenue associated with user participation for digital services).
- Creating a multilateral process for preventing and resolving tax disputes in order to ensure tax certainty for MNEs and the tax authorities.
- Creating an effective multilateral agreement to remove tax treaty barriers and implement the above measures in a coordinated manner.

As well, a general desire for a simpler and workable solution has emerged from the public comments[41] on the Blueprint and the adoption of DSTs and article 12B of the UN Model Convention. The burden of compliance and administration cost should never exceed the revenue gain to be obtained.

3.4. Emerging common areas of interests of governments

Given the diversity of national interests affected and inherent challenges in forging global consensus in the absence of a global government, it is not surprising that there remains significant disagreement about the best means of taxing market-based profit by each market country (this can be understood as "new unit rent" in our analogy – *see* section 2.1.). There has been little, if any, discussion about governments working together to charge a "common rent" on MNEs for the common expenditures required to maintain the "common area" and the building infrastructure described in the analogy.

Are there signs to suggest that governments are recognizing the link between taxation of MNEs and sustainability and common issues facing the globe? Arguably yes. For example, the US Treasury Secretary Janet Yellen's letter to the G20[42] gives a second wind to multilateral collaboration and provides members of the Inclusive Framework with an opportunity to bridge the gaps between their positions. It states that the new Biden-Harris Administration is committed to the Paris Agreement, to fairness in the international tax system, and to putting the needs of developing countries on the international agenda. The Chinese President, Xi Jinping, said that "China will always be a builder of global peace, a contributor to global development and a defender of international order."[43] The Chinese State Taxation Administration announced that China and the OECD "will jointly participate in the global tax governance for the digital economy".[44]

At a technical design level, there will be a need to balance accuracy and certainty under the Blueprint proposal. The 230-page Blueprint is an example of favouring detailed calibration of rules for certainty. Commentaries from the MNEs on the Blueprint highlight the need for simpler rules and giving MNEs more latitude in using best efforts.[45] Some MNEs advocate using methods that are not accurate but much simpler to ensure tax certainty.[46] A simpler formulary allocation method can be a bridge between Pillar One and existing DSTs.

Multilateral cooperation among tax administrations has increased rapidly over the past decade or so in the areas of, among others, information exchange, including country-by-country reporting, resolution of tax disputes under the mutual agreement procedure, and implementation of minimum standards adopted by the BEPS Project in 2015.[47] The adoption of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS (MLI)[48] signalled a shift towards multilateralism, even though this instrument was designed to facilitate speedy amendment of existing bilateral tax treaties.

41. *Supra* n. 11 .
42. *See* " *Letter from Treasury Secretary Janet L. Yellen to G20 Colleagues* ", 25 Feb. 2021, available at https://home.treasury.gov/news/press-releases/jy0034 (accessed 2 May 2021).
43. Xi, Jinping, "Together, Let Us Fight COVID-19 and Create a Better Future", remarks at the 15th G20 Leaders' Summit, 21 Nov. 2020, available at https://www.chinadaily.com.cn/a/202011/22/WS5fb99cc7a31024ad0ba959d1.html (accessed 28 Apr. 2021).
44. "China, OECD to Boost Cooperation on Taxation", available at http://www.chinatax.gov.cn/eng/c101269/c5161420/content.html (accessed 28 Apr. 2021).
45. Public Comments, *supra* n. 11 .
46. *See* Johnson & Johnson Comments on OECD Tax Challenges Arising from Digitalisation – Report on the Pillar One Blueprint, *supra* n. 11 and also *https://events.taxanalysts.org/tawebinar03172021/949222* (accessed 4 May 2021).
47. *See* , for example, OECD, "International Tax Co-operation: Key Indicators and Outcomes", available at https://www.oecd.org/tax/international-tax-co-operation-map.htm (accessed 4 May 2021).
48. For signatories and parties, *see* https://www.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.htm (accessed 4 May 2021).

3.5. Corporate social responsibility and commitment to sustainability

There has been a growing momentum in incorporating corporate social responsibility in management and investment. Sustainability in the sense of "meeting our present needs without compromising the ability of future generations to meet their own needs"[49]has become increasingly recognized as a key global issue. The three dimensions of sustainability, i.e. environmental protection, social development and economic development are interconnected. The UN 17 Sustainable Development Goals (SDGs) "recognize that ending poverty and other deprivations must go hand-in-hand with strategies that improve health and education, reduce inequality, and spur economic growth – all while tackling climate change and working to preserve our oceans and forests".[50]

Many business leaders not only share concerns for sustainability but are also increasingly vocal in demanding reform and taking concrete initiatives to address a range of environmental and social causes.[51]This is important as the world's 100 largest MNEs are bigger than many of the world's national governments and are in a position to make positive contributions.[52]Business leaders have participated in developing the ISO 26000 which provides guidance on "how businesses and organizations can operate in an ethical and transparent way that contributes to sustainable development while taking into account the expectations of stakeholders, applicable laws and international norms of behaviour".[53]The OECD Trust in Business Initiative, the OECD Business for Inclusive Growth and the UN Global Investors for Sustainable Development Alliance are initiatives that aspire to create corporate responsibility worldwide. As Oliver Bäte, CEO of Allianz B and co-chair of the Global Investors for Sustainable Development Alliance, said: "As responsible companies, we can create long-term value by embedding sustainability into our core business. […] Investing in the stable development of societies across the globe is not only the right thing to do, it also includes economic opportunities. We are convinced that investments in emerging markets can foster sustainable growth without losing sight of our customers' interests".[54]

The corporate commitment to sustainable development and environmental protection is likely to continue as a new generation of executives are pushing for more concrete reforms of the economic regulatory infrastructure, especially on the environmental front. A similar trend is evident among investors, who are increasingly putting their money where their values are, while brokerage firms and mutual fund companies have begun to offer exchange-traded funds and other financial products that follow environmental, social and governance (ESG) investment criteria.[55]

While showing increasing commitment to social responsibility, MNEs are also known for taking advantage of mismatches between national tax laws and/or legislative deficiencies in national tax laws to minimize their taxes when tax revenue is the blood line for governments. As such, the sphere of tax minimization and the sphere of social responsibility are disconnected. There have been suggestions about using carbon taxes to lever the contribution of businesses to the achievement of the goals of the Paris Agreement on climate.[56]Repurposing the Blueprint into an incremental global tax would further connect the two spheres.

4. The Proposed Tax for Sustainability: Overview

4.1. Evolution from the Pillar One Blueprint

The proposed tax is an evolved version of the Blueprint with the modifications suggested by the United States. It will have rules that are similar to (but simpler than) those in the Blueprint in the following respects:

- In-scope taxpayers will be the largest and most profitable MNEs.
- The tax base will be the country's share of the market-based profit of an MNE determined based on consolidated financial income and formulaic allocation. In other words, it would also allocate a portion (say, 20 per cent) of the deemed residual

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49. Brundtland Commission, *Our Common Future* (UN through the Oxford University Press, 1987).
50. *Supra* n. 3 .
51. *See* , for example, S.K. Park & G. Berger-Walliser, *A Firm-Driven Approach to Global Governance and Sustainability* , (2015) 52 Am. Bus. L.J. 255; T.J. Radin, *Stakeholders and Sustainability: An Argument for Responsible Corporate Decision-Making* , (2007) 31 Wm. & Mary Envtl. L. & Pol'y Rev. 363; J. McGregor, *"'Climate change is real': CEOs share their disappointment over Trump's Paris accord exit* ", The Washington Post, 1 June 2017, available at https://www.washingtonpost.com/news/on-leadership/wp/2017/06/01/ceos-make-final-pleas-to-trump-to-stay-in-paris-climate-agreement/ (accessed 2 May 2021).
52. R.L. Nolan, *Big History, Global Corporations, Virtual Capitalism* , Harvard Business School, Working Paper 16-116, 2016, at p. 3.
53. International Organisation for Standardization, ISO 26000 Social Responsibility, available at https://www.iso.org/iso-26000-social-responsibility.html (accessed 4 May 2021).
54. UN Press Release, 16 October 2019 , "30 Business Titans Join UN Push to Scale Up Private Sector Investment for Sustainable Development".
55. R.G. Eccles & S. Klimenko, *The Investor Revolution* , Harv. Bus. Rev. (May-June 2019), available at https://hbr.org /2019/05/the-investor-revolution (accessed 2 May 2021).
56. OECD (2021), *Effective Carbon Rates 2021: Pricing Carbon Emissions through Taxes and Emissions Trading* , OECD Publishing, Paris, available at https://doi.org/10.1787/0e8e24f5-en (accessed 2 May 2021).

profit of an MNE group (say, above a profit margin of 10 per cent) to market countries using sales revenue sourced in the country as the method to allocate the market-based profit between them (including sales revenue generated by the interaction with users for digital models).

- The sourcing rules for determining the amount of sales revenue attributable to a specific market jurisdiction will be similar but simplified.
- The tax certainty process will seek to minimize tax disputes and effectively resolve tax disputes that would occasionally arise.
- Implementation will also be through a multilateral tax convention.

However, the proposed tax will differ from the Blueprint in three main aspects: (i) its purpose; (ii) the elimination of double taxation; and (iii) all of the simplifications these first two features can bring to the taxation model.

4.2. Repurposing Pillar One

By going beyond the mere reallocation of taxing rights under the Blueprint, our proposal means a new incremental and standalone tax on the market-based profit of MNEs. As such, if adopted, it will be the world's first global tax on MNEs. Like DSTs, such standalone tax requires minimal interaction with the existing CIT and international tax rules, such as transfer pricing rules under the arm's length principle. This feature of the proposed tax will greatly simplify the Blueprint proposal and will render it more administrable.

As will be explained, the proposed tax has some DST features and can be applied similarly, at least in the initial phrase of the implementation. Instead of removing unilateral DSTs with a reallocated tax base of CIT, which is the function of the Blueprint, our proposal will replace the DSTs with another tax, but based on the net profit and not just targeted at digital companies. This is to recognize the entitlement of market jurisdictions to tax market-based profit of MNEs.

In addition to recognizing each market jurisdiction's right to tax market-based profit, the proposed tax represents the exercise of taxing rights by all market jurisdictions as a collective in order to finance expenditures on fighting a common crisis (*see* section 2.1.). This dimension is absent in the Blueprint, but arguably implied or expected by political leaders and G20 Finance Ministers.

4.3. Hybrid nature

To ensure simplicity and workability, the proposed tax has two delivery options: a DST-like option (a tax on gross sales at a rate which is a proxy for CIT rate) and a CIT-like option (CIT rate on net profit). Each option has certain advantages and disadvantages but shares the same economic effect, approximately, because of the inter-changeability feature.

4.3.1. Inter-changeable DST and CIT design options

The inter-changeability of CIT and DST is a key feature of the proposed tax.[57] For those attached to the simple formulation of a DST, the Tax for Sustainability could be implemented through designing the tax rate by replicating the effect of a CIT based on the profitability of the MNE, and applying such rate to the sales allocated to a specific country.[58] Therefore, the amount of tax in a market country would be the same under either option as long as the CIT rate applicable to the profit allocated to that country could be transposed or converted into a rate of tax applicable directly on the sales in that country (i.e. like a DST).

In other words, and as shown in the following examples, whether the allocated market-based profit is taxable at the CIT rate or at a DST-like rate applicable to the sales that is used in the allocation formula for determining the amount of allocated market-based profit, the market country would obtain approximately the same amount of tax revenue and the MNE's burden of tax would be approximately the same.

The formula for a CIT-like option is:

$$T = w*[x*(SA/S)]$$

meaning:

Tax for sustainability = CIT rate * [market-based profit * (market sales / global sales)]

For example, Mega Inc. is an in-scope MNE with global sales revenue of 22.2 billion (" *S* ") and a global profit before tax (PBT) of 10 billion, resulting in a profit margin of 45 per cent (" *m* "). Mega Inc's deemed residual profit " *r* " is the profit above 10 per

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57. Such inter-changeability is also discussed in Collier, Devereux & Vella, *supra* n. 6 .
58. Id.

cent (i.e. 35 per cent). The deemed residual profit (" *r* ") therefore equals S*35%, and the market-based profit " *x* " would be deemed to be 20 per cent of *r* . If the MNE has 1 billion of sales revenue allocated to Country A (" *SA* ") and the CIT rate in Country A is 21 per cent (" *w* "), the tax for sustainability (" *T* ") payable to Country A will be 14.7 million:

T = 21%*[1.55B*(1B/22.2B)]

Example

Financials of Mega Inc.		
Global sales	*S*	USD 22,222,222,222
PBT	*PBT*	USD 10,000,000,000
Profit margin	*m*	45%
Policy Parameters		
Deemed routine profit margin	*a*	10%
Market-based profit share	*b*	20%
Consolidated		
Deemed residual profit margin = m – a	*n*	35%
Deemed residual profit = S * n	*r*	USD 7,777,777,778
Market-based profit = b * r	*x*	USD 1,555,555,556
Result in Country A		
Sales in Country A	*SA*	USD 1,000,000,000
Country A's share of market-based profit = x * (SA/S)	*c*	USD 70,000,000
CIT Rate in Country A	*w*	21%
Tax in Country A = c * w	*T*	USD 14,700,000

The conversion formula for a DST-like delivery option in the foregoing example would be as follows:

T = SA * (w*b*n)

meaning:

T = sales in Country A * (CIT rate * market-based profit share * deemed residual profit margin)

T = 1B * (21%*20%*35%)

or

T = sales * 1.47%

Example

Financials of Mega Inc.		
Global sales	*S*	USD 22,222,222,222
PBT	*PBT*	USD 10,000,000,000
Profit margin	*m*	45%
Policy Parameters		
Deemed routine profit margin	*a*	10%
Deemed market-based profit share	*b*	20%
Consolidated		
Deemed residual profit margin = m - a	*n*	35%

Result in Country A		
CIT Rate in Country A	*w*	21%
Sales in Country A	*SA*	USD 1,000,000,000
Tax Rate = n * b * w	*d*	1.47%
Tax in Country A = SA * d	*T*	USD 14,700,000

The DST-like delivery option replicates the mechanism of DSTs to achieve the net taxation of MNE profits.[59]As explained in Annex A, the rate of tax ("d") will vary depending on the profit margin of the MNE or the CIT rate in the particular country.

4.3.2. Advantages of DST-like delivery mechanism

Although the economic effect is similar, a DST-like approach would be simpler to implement, especially for countries that do not want to invest much administrative resources to achieve perfect integration between the proposed tax and CIT. Using a DST-like delivery may also allow further simplifications and advance certainty, such as using the average CIT rate in participating countries for variable " *w* " (CIT rate), using the MNE average profit margin of previous years for variable " *n* " (deemed residual profit margin) or, for low-income countries,[60]using a fixed number for "d" (tax rate on sales) based on the higher scale of Annex A (e.g. 2 per cent).

A further simplification would be to use a bracket system using the average rates per bracket in the Annex A table:

Brackets	Average profit margin of the MNE group above the threshold of 10% for the previous years (%)	Tax rate for the year (%)
1	0.1 to 10	0.25
2	10 to 20	0.5
3	20 to 30	1
4	30 to 40	1.5
5	above 40	2

Some relief mechanism could be developed to avoid a cliff effect when the MNE changes bracket (for example, the year an MNE moves from the second bracket to the third, the rate that increases by 0.5 per cent could increase only by half, i.e. it would increase by 0.25 per cent to a rate of 0.75 per cent instead of immediately go to a rate of 1 per cent).

The CIT-like option would, however, allow a participating jurisdiction to credit the tax (or exempt the allocable profit) to relieve economic double taxation if it chooses to. It would also provide the basis for the possible evolution of the new tax into a comprehensive regime of taxing MNEs on a global formulary apportionment basis.

Even if the proposed tax is, like a DST, independent from CIT and therefore not requiring a relief from double taxation, where the effective tax burden of the combined proposed tax and CIT exceeds a certain rate (say, 25 or 30 per cent) in both a jurisdiction and globally, a credit for the proposed tax should be considered in that country.

4.4. A humble beginning

With the hybrid features, the proposed tax can be implemented with more simplicity while laying the foundation for a long-term CIT system of taxing MNEs. It allows simpler and more flexible policy designs and administration features, especially for low-income countries. The proposal also preserves the fiscal sovereignty of the market country as it retains the power to implement and administer the new tax with greater autonomy. Meanwhile, it would be a legal mechanism for in-scope MNEs to make a net contribution to the common cause (i.e. not just simply to reallocate profits).

Furthermore, while the DST design option makes it easier for implementation at the beginning, the CIT option can be the basis for a future tax system for MNEs. In other words, by making it easy to take a small step first – replicating the mechanism of a DST on a multilateral level – the proposed tax, which might be analogized to an infant, can mature into a full-fledged global tax on MNEs. If ever one day the conditions are ripe for taxing MNEs' income on a formulary apportionment basis, the proposed

59. In such a case, like many DSTs, the MNE group will have to file a return for the tax, based on the sales of the previous year. The MNE will still need to compute its consolidated profit, its profit margin and other key elements to determine the tax rate. However, for low-income countries with limited resources, the tax rate could be fixed at the maximum in order to simplify the administration and compliance.
60. "Low-income countries" can be based on the classification by the World Bank Group Income Classifications of 2020, ***see*** https://datahelpdesk.worldbank.org/knowledgebase/articles/906519-world-bank-country-and-lending-groups (accessed 11 May 2021).

tax can be transformed into a general MNE tax regime. In that case, the adherence of countries to a global allocation would resolve issues of double taxation with other CIT systems.

But at this juncture, our goal is to create a global tax instrument with potential for long-term stability and growth while immediately giving countries a revenue stream to address the global crisis identified in the Paris Agreement and meet the UN sustainable development goals. To make it simple, as explained in section 5.6. , elimination of double taxation will be achieved through a deduction of the Tax for Sustainability from income as any other expense. Crediting the new tax against the CIT will be the exception.

4.5. Accountability and transparency

As mentioned earlier, the object of this proposed tax is to provide governments with additional financial assistance from the largest and most profitable MNEs to achieve the common goal and ensure the prosperity of future markets and, with it, the prosperity of those MNEs. It is a new partnership in this global age.

It would therefore be crucial for governments to use the new tax revenue to invest in sustainable development or, to use our earlier analogy of a condominium building (*see* section 2.1.), to attend to the building infrastructure in need of urgent repairs. This should not be difficult as the SDGs cover large parts of any nation's budget. Also, governments are already forced to spend a large part of their revenues to compensate for the effect of climate change. Accountability by governments for public expenditure on SDGs and climate actions would thus be the counterbalance for levying the Tax for Sustainability on MNEs.

To highlight the common goal of the proposed tax, the goal could be stated in the preamble of the Multilateral Convention on Tax for Sustainability (Convention). The Convention can have a provision to set out how governments might report their expensing of the tax. Governments could even be encouraged to pool the tax revenues to finance global projects, such as cleaning the ocean.[61]

MNEs that pay the Tax for Sustainability would be able to publicly state that they pay the tax, thereby contributing to the goal of sustainability, and disclose the tax payment in their financial statements. Without interfering with their sovereignty, countries could even involve in-scope MNEs to partnership with them on the delivery of specific projects on climate change and sustainable development.[62]

4.6. Guiding principles

The proposed Tax for Sustainability aims to be fair, simple and respectful of fiscal sovereignty. It is meant to be a sustainable tax instrument for promoting sustainable development.

4.6.1. Fairness

There is little consensus on the meaning of fairness in international taxation.[63]Like beauty, fairness lies in the eyes of the beholder. Perspective matters.[64]

From the perspective of nation states seeking to tax MNEs, our proposal is fair as it is consistent with the doctrine of economic allegiance. Using the language of the 1923 Report, market jurisdictions provide service to MNEs through maintaining a market for the goods and services of MNEs and are thus entitled to tax a portion of the MNEs' market-based (not the total) profit. Existing international tax rules often fail to enable market countries to actually exercise their taxing rights. Addressing this unfair outcome for market jurisdictions was the main reason the Pillar One Blueprint was developed by the Inclusive Framework. In other words, the governments of market jurisdictions have not been able to collect rent (CIT) from MNEs for hosting the market for them. In our earlier analogy to the condominium building (*see section* 2.1.), the unit rent has not been collected by each unit owner.

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61. We thank Richard Collier for suggesting this idea to us. The object of the new tax is to finance sustainable development and, although governments need funding now to recover from the COVID-19 crisis and redouble their efforts to meet the 2025 Paris Agreement on climate objective, and the 2030 SDGs, it will be incumbent on participating countries to develop a coherent system to account for their spending for sustainable goals, inspired by the values of the MNEs contributing.
62. As stated in section 3.5. , many business/government partnerships have emerged in recent years. The OECD Trust in Business Initiative, the OECD Business for Inclusive Growth and the UN Global Investors for Sustainable Development Alliance are initiatives that aspire to create corporate responsibility worldwide.
63. *See* , for example, M. Devereux et al., *Taxing Profit in a Global Economy* (Oxford University Press, 2020) (hereinafter the "Devereux et al."); R. Krever and F. Vaillancourt, *The Allocation of Multinational Business Income: Reassessing the Formulary Apportionment Option* (Wolters Kluwer, 2020); and J. Li, *Global Profit Split – An Evolutionary Approach to International Income Allocation,* Canadian Tax J., Volume 50, Number 3 (2002), pp. 823-833.
64. J.S. Wilkie, *Perspective Matters: One Country's "Offshore" Is Other Countries' "Onshore"* , Tax at Osgoode Hall Law School, 18 April 2021, available at https://tax.osgoode.yorku.ca/2021/04/perspective-matters-one-countrys-offshore-is-other-countries-onshore/ (accessed 2 May 2021).

Furthermore, in order to address the issue of inter-nation inequalities in fiscal capacity, our proposal could have a redistributive mechanism built in so that low-income countries could tax their share of the global profit at a higher rate.[65]Such mechanism is unprecedented and feasible only through a multilateral tax instrument such as our proposed tax. It would assist developing countries in meeting their sustainable development goals.

As a new dimension of fairness in the age of global crisis, it would be fair for all market jurisdictions acting together to tax MNEs for the expenditures on financing the connectivity of national markets as well as sustainable development. Again, using our analogy of the condominium building, the collective of unit owners has the legitimate right to add a portion of the common expenses to the unit rent.

From the in-scope MNEs' perspective, paying the Tax for Sustainability is as fair as paying rent. Market-based profit is derived from taking advantage of the market that is maintained by governments through investing in the legal, physical, digital and other infrastructures. Limiting the Tax for Sustainability to the largest and most profitable MNEs may appear to be unfair as smaller and less profitable MNEs are outside the scope. The main justification is the necessary compromise between perfection and efficacy and workability. The future evolution of the Tax for Sustainability into a comprehensive system of taxing MNEs could revisit its scope.

From the perspective of the general public, our proposal would meet a common-sense notion of fairness by addressing the concerns that MNEs do not pay their fair share of tax.[66]In addition to functioning as a replacement of DSTs, our proposal would help address the global crisis that would benefit all countries, especially those that are inadequately equipped on their own to manage such a crisis.

4.6.2. Simplicity and stability

Simplicity is an important, and yet often difficult to achieve, objective of tax design owing to the need to balance various competing goals. To achieve simplicity, our proposal relies on readily available information, such as consolidated financial statements, adopts clear and objective sourcing rules, and removes the complexity associated with tangling with existing transfer pricing rules.

Our proposal has the potential for being more stable than a complex reallocation of MNE residual profits. Many commentators have regarded the current design of Pillar One as too complex: "In limiting amount A to its calculations of residual profits by lines of business, the OECD has produced a convoluted and controversial structure that in the absence of universal agreement on the application of its segmentation decisions – which certainly will not happen – guarantees the kinds of uncertainties, complexities, and controversies that the OECD insists it wants to avoid".[67]

Our proposal intends to lessen the need for the accuracy that some of the most complex design features of the Blueprint intend to bring (such as segmentation, identification of residual profit owner, implementation and establishment of a fine-tuned supra-national administration and dispute prevention/resolution system).

4.6.3. Preserving fiscal diversity

By elevating the proposed tax out of the existing CIT system and requiring minimal changes to domestic law, our proposal respects the diversity of national fiscal policies. This reflects the reality that it is the nation states that are accountable to the people and responsible for financing public expenditures, including those on sustainable development. Each nation sets its own fiscal policies, including corporate tax policies, to best meet its needs and to reflect the collective aspirations. Our proposal seeks to preserve such diversity while creating a global tax structure for addressing global challenges.

5. The Proposed Tax for Sustainability: Technical System Design

5.1. Design issues and objectives

The proposed tax is a standalone system, which will operate in parallel with the CIT system. It is thus different from the Pillar One in the Blueprint, which is part of the CIT system and cannot be enforced on its own.

Like all taxes, the following essential elements of the Tax for Sustainability must be defined in a way that they constitute a system: (i) Who are taxable? (ii) What is taxable? (iii) How much tax is payable? (iv) How is the tax paid or collected? (v) How to resolve tax disputes? As mentioned in section 4.1. , the design of (i), (ii) and (v) will be largely informed by the Blueprint as

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65. P.B. Musgrave & R.A. Musgrave, *Inter-Nation Equity* , in *Modern Fiscal Issues* pp. 63-85 (R.M. Bird & J.G. Head eds., U. Toronto Press, 1972); Devereux et al., *supra* n. 63 , at heading 2.1.
66. *See* Y. Ran Kim, *Digital Services Tax: A Cross-Border Variation of the Consumption Tax Debate, (2019) Vol.72:1:131* Alabama L. Rev. 131-85; and W. Cui, *The Digital Services Tax on the Verge of Implementation* , (2019) 67:4 Canadian Tax J. 1135 – 52.
67. Graetz, *supra* n. 11 , at p. 206.

modified by the US proposal, and the design of (iii) and (iv) will be informed by DSTs' simple design and recent developments in international tax cooperation.

The technical design seeks to strike a proper balance between perfection on paper and performance on the ground. The goal is not to let perfection be the enemy of progress. A second-based solution may be the best solution in this moment of international crisis. Complex rules to achieve more perfect technical design may be sacrificed for simpler options as long as they are consistent with the guiding principles. The ultimate goal is to develop a reasonable workable solution sooner rather than later.

The existing international tax system has ample examples of second-best choices because, as recognized in the 1923 Report, it "may well be that the precise amount of profit to be allocated to particular countries is never finally determinable".[68]

5.2. In-scope taxpayers

Following the direction of the Blueprint and the recent US approach, the proposed tax would apply to in-scope MNEs based on revenue and profitability thresholds and each MNE group will be treated as a taxable unit. The revenue threshold can be set high enough to capture only the largest and most profitable MNEs.[69]

MNEs in all industries and sectors that derive market-based profit are potentially in-scope. The type of ownership (e.g. by the government or tax-exempt entities) should not affect scoping.

The MNEs that are currently carved out from the scope in the Blueprint should be included in the proposed tax for simplicity, fairness and certainty purposes. Financial institutions meeting the revenue and profitability thresholds should be in-scope so their market-based profit is taxable under the proposed tax. Financial institutions are already exploring different avenues to contribute to the Paris Agreement on Climate and the SDGs; this will be their concrete contribution.[70]

MNEs engaged in the extractive activities should also be considered, acknowledging, however, that the existing taxation of their profit from the exploitation of finite natural resources belonging to a country may need special considerations.[71] But, if these MNEs' profit margin is high, they should also contribute to the Paris Agreement and the SDGs.

A challenge associated with including these sectors in the scope is to devise sensible sourcing rules for sales revenue. As explained in section 5.4. , a formulaic approach could be used. What is more important is that all large and profitable MNEs contribute to the common cause, and not so much who exactly they pay it too as long as the tax revenue goes to that common cause.

5.3. Tax base: Market-based profit

Building on the impressive work of the Blueprint, an MNE's market-based profit is a portion (say, 20 per cent) of the residual profit, and the residual profit would be the profit margin that exceeds a certain threshold for routine profit (say, 10 per cent). The measure of profit will be an adjusted profit before tax ("PBT") derived from the consolidated financial accounts of in-scope MNE groups. The starting point would be defining acceptable financial accounting standards, which would be those that produce equivalent and comparable outcomes to IFRS, based on the work of the International Accounting Standards Board (IASB) and securities regulators. As suggested in the Blueprint, the PBT is a comprehensive figure containing all income and expenses of an MNE, taking into account all the real costs of doing business.[72] Moreover, the PBT is unaffected by the classification of specific items in different sections of the Profit or Loss Statement and it approximates the measure of profit on which CIT is normally levied. The Blueprint also considers that a limited number of book-to-tax adjustments will apply to determine the relevant measure of PBT and seeks alignment of the tax base with the corporate tax base of Inclusive Framework members. Such adjustments are unnecessary under the Tax for Sustainability because the Tax for Sustainability is a separate tax regime from the CIT.

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68. *See* 1923 Report, *supra* n. 30 , at p. 26.
69. An economic analysis by the OECD concluded that the tax sensitivity of a firm in an MNE group with a high profitability rate (above 10%) is nearly half the sensitivity of a firm in an MNE group with a low profitability rate (between 0% and 10%). *See* V. Millot et al. (2020), " *Corporate taxation and investment of multinational firms: Evidence from firm-level data* ", OECD Taxation Working Papers, No. 51, OECD Publishing, Paris, available at https://doi.org/10.1787/9c6f9f2e-en (accessed 11 May 2021).
70. Financial institutions are already participating in different actions to support the Paris Agreement and UN SDGs. The G20 Communiqué, *supra* n. 5 , states: "We welcome the establishment of the Sustainable Finance Study Group, which we are upgrading to a working group, and we look forward to its work, for 2021, on developing, in a collaborative manner, an initial evidence-based and climate-focused G20 sustainable finance roadmap, improving sustainability reporting, identifying sustainable investments, and aligning International Financial Institutions' efforts with the Paris Agreement." It would therefore be logical for FIs to also contribute directly to the financing of sustainable development (unless their effective tax rate is already higher than the average CIT rate of participation countries).
71. Typically, countries will use several instruments to optimize their return on the exploitation of finite natural resources – for example, production-sharing contracts, up-front bonus payments, ongoing royalties, as well as corporate income taxes (possibly in a ring-fenced regime with a higher rate).
72. Pillar One Blueprint Report, *supra* n. 7 , at sec. 5.2. Stakeholders generally agreed with the Blueprint approach to using consolidated financial accounts as the starting point, but criticized extensively the segmentation framework.

Business line segmentation in the Blueprint was needed to ensure that conglomerates first fall within the scope and then are taxed on a level playing field with their competitors. It generated significant criticism for its complexity and uncertainty. Like the US proposal, the proposed Tax for Sustainability would have less need for segmentation because of the comprehensive scope. Under a comprehensive approach to scoping, conglomerates amongst the largest MNEs should be included in the scope even if the blending of their different business lines results in a profit margin below 10 per cent, as long as one of their segments is large and profitable. Using the simplification of the DST-like delivery mechanism and the brackets system described in section 4.3.1. , the minimum rate for the Tax for Sustainability could be, in such a case, a minimum of 0.25 per cent on the market sales. Even if the tax is set at its lowest on the scale because highly profitable segments are blended with less profitable ones, the tax would apply to a broader tax base.

5.4. Attribution of market-based profit and sourcing rules

Like the Blueprint, the proposed tax will determine the amount of market-based profit attributable to each market jurisdiction based on a formula, using sales as the sole allocation key. The connection with a particular market will be the sales revenue attributed to it. In order to keep the new tax administrable, a nexus is needed so that a minimum level of revenue associated with the market jurisdiction would be required in a particular year. This level would be kept reasonably low in order to allow small market countries to participate in the proposed tax regime.

Allocating the revenue from the sales of services or goods, or revenues derived from users or user data, to a country is key to the proposed tax regime. To keep the sourcing rules as simple and predictable as possible, it is important to rely on data already available to in-scope MNEs and that can produce a result that correlates with the expected final use of the good or service. In difficult cases, or to verify the correlation, objective macro data as proxies could be used (*see* further in this section). Also, and as explained in section 5.7. , MNEs should be able to obtain a pre-approved method of sourcing to prevent disputes and obtain early certainty.

In general, because of the comprehensive scope, the proposed tax would require sourcing rules for revenues in a variety of industries and transactions that are not covered by the Blueprint. The sourcing rules would vary according to the nature of the revenue. As a general principle, however, the revenue should be sourced where a good or service is ultimately used or consumed (including business consumers) or, in the case of revenue associated with users, where the users are. The application of the revenue sourcing principle would be adapted to different scenarios. For example:

- revenues derived from the sale of tangible goods could generally be sourced where the place of final use of the good is (the place of final delivery could be used as reasonable approximation);
- services could generally be sourced where the services are used;
- online advertising could (as recently proposed in the Canadian Budget for a DST)[73]generally be sourced based on the location of the user who views, listens to, clicks on or otherwise consumes the advertisement;[74]
- fee revenue of social media interfaces could be sourced at the locations of the interface users on a formulaic basis[75](based on the number of active users of the interface in a country);
- the sale of user data could be sourced where the users to whom the data relates are; and
- the licensing or other exploitation of intangible property could be sourced where the intangible property is used.

Nevertheless, difficult cases will exist. For example, it would be particularly challenging to locate the place of final use of components (such as computer chips) and business-to-business (B2B) services (such as cloud computing services). The sourcing of revenues for financial institutions in scope may also be difficult.

It may be considered to have a general requirement that in exceptional cases MNEs may use “best efforts” in choosing a sourcing rule that would be most appropriate under its business model and the data that most accurately determine the location of the revenue based on the above principles.

Where sourcing the revenues becomes too difficult, the sourcing rules should provide for general proxies, such as using consumer market data.[76]Since in-scope MNEs are the largest and most profitable firms, their products and services are

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73. Annex 7 - Consultations on Other Tax Measures: Supplementary Information - Canada.ca (budget.gc.ca) Canada, Budget 2021.
74. Needless to say, it is important to keep in mind data protection laws and/or privacy laws and avoid any erosion of the right to privacy and other constitutional norms.
75. Canada, Budget 2021, *supra* n. 73 .
76. Data like the *Actual final consumption of households* (United Nations System of National Accounts (SNA), 2008, 9.116.) may be an indicator of the size of a consumer market. The actual final consumption of households covers goods and services which are effectively available for individual consumption by households, regardless of whether the ultimate bearer of the expense is government, Non-profit institutions serving households (NPISH) or households

available across the globe, and their revenues in countries will most likely correlate significantly with the countries' respective consumer market size. It may be apparent to tax administrations when the revenue allocation to countries is at odds with the countries' respective consumer market size (which could be used as an audit risk factor).

The application of these sourcing rules will be supported by a variety of other features, including anti-avoidance provisions, standardized reporting obligations for taxpayers, and an early tax certainty process confirming the methodology proposed by the MNE and valid for a number of years, and a dispute resolution mechanism for situations where two or more countries claim a single stream of revenue to have a source in their countries.

5.5. Tax rates

As discussed in section 4.3.1. , the basic rate of the proposed Tax for Sustainability is the CIT rate. However, such rate can be converted into a DST-like rate and apply to gross sales for simplicity.

Assuming the CIT rate is 21 per cent, a replicated DST rate would be approximately 1.5 per cent for an MNE with a deemed residual profit margin of 36 per cent (*see* Annex A). For greater simplicity, a bracket system can be considered (*see* section 4.3.2.).

5.6. Elimination of economic double taxation

In-scope MNEs will likely be subject to both the proposed tax and CIT on market-based profit. There will thus be economic double taxation at the corporate level,[77] but not, technically speaking, juridical double taxation because the proposed tax is separate from the existing CIT system. The degree of economic double taxation depends on whether the market-based profit is fully taxed under the CIT system and the CIT rate of the country that is a headquarters jurisdiction or a host country of a constituting entity of the MNE group. Hypothetically, if the market-based profit is "stateless" for CIT purposes, there would be no economic double taxation.[78]

The hybrid nature of the proposed tax would enable countries to recognize the tax as if it were a DST payment and allow it to be deducted in computing income for CIT purposes. The proposed tax would not be expected to be eligible for a tax credit against the CITs of entities within the group. But it will be deductible in computing taxable income for the entities earning the sales revenue. This is to ensure simplicity and certainty, as well as providing a new revenue stream to governments. It could also be possible to allocate the group tax for deduction purposes using a simple formulaic approach such as the ratio of inclusion of sales revenue by entities of the MNE group.

According to the MNEs' commentaries on the Blueprint, double tax relief rules are a main cause of complexity. A country could always opt for crediting the proposed tax against the CIT otherwise payable by MNEs' entities in that country. After all, the tax base of the proposed tax is, presumably, included in the tax base of the CIT. It can be imagined that countries with a high CIT rate and mature or sophisticated existing CIT systems may choose the credit method.

Even in a country that opts for the DST-like option, in exceptional cases, the proposed Tax for Sustainability can be credited against the CIT if, for example, the level of economic double taxation is significant (e.g. the combined CIT and the proposed tax cause the effective tax rate of an in-scope MNE to exceed a threshold of 25 or 30 per cent globally and in a country).

5.7. Administration and tax certainty process

The proposed tax will follow the general thinking of the Blueprint about creating a centralized process for compliance and administration and a multilateral mechanism for tax certainty. However, such process and mechanism would be simplified.

The Blueprint contemplates a comprehensive tax administration system and tax certainty process. In summary, under a centralized administration system as contemplated under the Blueprint, the MNE group would first identify a coordinating entity to coordinate and file a single return. The coordinating entity will file the self-assessment return and documentation package with a lead tax administration (likely the country where the "ultimate" parent entity resides). The lead tax administration will validate whether the return is complete and exchange the return and the documentation package with all affected tax authorities.

The coordinating entity may make a voluntary request for certainty and the lead tax administration will have the option to undertake an initial review with a view to filtering out lower risk MNE groups. The self-assessment will be reviewed by a review panel, a process that may require additional information to be provided by the MNE. If the review panel cannot agree with the

themselves. Actual final consumption of government and NPISHs is equal to consumption expenditure less social transfers in kind, or, in other words, collective consumption. The difficultly in using macroeconomic data may be one of timing.

77. It is beyond the scope of this article to consider economic double taxation at the level of individual shareholders.

78. President Biden's Remarks, *supra* n. 2 , mentioned that recent studies show that 55 of the nation's biggest corporations paid zero federal tax in 2020 while making more than USD 40 billion in profit.

self-assessment, or if any affected tax administration does not accept the decision of the review panel, or if the MNE does not accept revisions proposed by the review panel, the disputed points may be referred to a determination panel.

The implementation of this process in a way that would be binding on tax administration would mean a delegation of tax administrative power to a supra-national body (such as a conference of the parties of the multilateral convention). Having a perfect coordination and tax certainty on all of the elements of Pillar One (scope, tax base, revenue sourcing, nexus, elimination of double taxation) would also be resource intensive as noted by several stakeholders during the public consultation.

Under the proposal of this article, the tax administration and certainty process would be simplified greatly through: (i) simpler scoping, segmentation and sourcing rules; (ii) eliminating the obligation for countries to agree on who amongst them should give relief; and (iii) including a process to pre-approve the MNEs' choice of methodology on the computation of the tax base and the sourcing rules. The number of disputes may be kept low if MNEs are discouraged from "gaming" the system in light of the noble, common goal and potential reputational harm. Also, keeping the process as light as possible would ensure the participation of all countries, including developing countries with limited resources.

For the first time in history countries would come together to tax an MNE group as a whole (and not only separate entities). This group taxation necessarily involves a high level of coordination amongst them and with the MNEs in scope.[79] To ensure an effective coordination, countries will need to agree on the broad parameters of this new taxing right (*see* section 5.8.). They should also cooperate in designing a standardized tax return to facilitate the compliance for both the MNEs and the tax administration. Also, as mentioned above, the MNEs in scope should be given access to an early tax certainty process to ensure countries are in agreement with the methodology they choose to determine key aspects of the new tax such as the scope, tax base determination and revenue sourcing. Countries should agree to be bound for a few years by this "multilateral ruling process" on the methodology, which would minimize greatly areas of potential dispute. If, despite all of this, tax disputes occur, there should be a streamlined, timely and effective binding dispute resolution mechanism available for the MNEs.

5.8. Multilateral Convention on Tax for Sustainability

5.8.1. Importance and effect

As the world's first global tax on MNEs, the proposed tax can only be implemented through a multilateral tax convention (the Tax for Sustainability Convention) that is adopted into domestic law but largely self-enforcing. Domestication of the convention should be simpler than that contemplated by the Blueprint as minimal changes to domestic law would be required for the convention to take effect.

This multilateral convention will prevail over any domestic law or bilateral tax treaties. It is important because the proposed tax, which would be based on consolidated group profit and a formulary allocation method, would be considered inconsistent with the existing rules on permanent establishment, profit attribution and transfer pricing. The convention would provide certainty by circumscribing the application of such rules to the extent of market-based profit covered by the proposed Tax for Sustainability.

Even if no tax treaty exists between a pair of participating countries, the multilateral convention would be important as taxing MNEs' group profit by multiple countries will require an unprecedented amount of coordination between participating countries.

While a specific country may, at least in theory, implement the proposed tax solely in its domestic legislation (and assuming that the connection between the taxpayer and the country would be sufficient under international public law), it would encounter significant difficulties in enforcing, administering, and collecting such tax. Such difficulties would be mitigated through an international public law instrument such as the multilateral convention.

5.8.2. Title and preamble

The title and preamble of the Tax for Sustainability Convention should state the purpose and object of the tax, including raising revenues to achieve the goals of Paris Accord and the SDGs (and beyond the deadlines set in these accords). Although there is an uncertainty surrounding the role and value of preambles, they are important to interpreting the convention.[80] Article 31 of the Vienna Convention on the Law of Treaties (VCLT) states that "a treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose".[81] To remove any uncertainty associated with preambles, the purpose of the convention could be stated in a standalone provision.

79. Useful insights can be obtained from the experience of the ICAP Project for designing ways of international coordination. See M.H. Martini & R. (Ronald) Russo, *The International Compliance Assurance Programme: Review of the Full Programme* , 75 Bull. Intl. Taxn. 4 (2021), Journal Articles & Opinion Pieces IBFD.

80. M.H. Hulme, *Preambles in Treaty Interpretation* , University of Pennsylvania Law Review, available at https://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=9527&context=penn_law_review (accessed 4 May 2021).

81. Art. 31, *Vienna Convention on the Law of Treaties* , 1969, Done at Vienna on 23 May 1969. Entered into force on 27 January 1980. United Nations, Treaty Series, vol. 1155, p. 331.

5.8.3. Structure and content

To ensure consistency and certainty in the implementation, interpretation, and administration of the proposed tax, the convention should contain provisions that enable the operation of the tax, that is, basic charging rules, administrative rules and tax certainty rules mentioned above.

The convention should contain the appropriate degree of detail to ensure its coordination and that its exercise would be circumscribed by multilaterally agreed treaty provisions. But it would also need to be drafted in terms that will be sufficiently broad as to provide flexibility in its interpretation and allow the convention to evolve over time and adapt to new business models. Accompanying commentary and other guidance would help ensuring a consistent and coherent application of the new taxing right and providing tax certainty.

It would be essential to agree on the key parameters for the exercise of this new taxing right (such as entities subject to the new tax, the tax base, sourcing rules, coordination, etc). But there could be a certain discretion for a country to set the tax rate and choose between the DST-like or CIT-like delivery mechanism, as long as it exercises its taxing right within the agreed limits.

5.8.4. Relationship with bilateral tax treaties and domestic law

As bilateral tax treaties will remain in force, the multilateral convention will coexist with them. Contrary to the BEPS Multilateral Instrument, the Multilateral Convention to implement the Tax for Sustainability would generally not modify existing provisions of bilateral tax treaties. Instead, it would supersede and prevail over them for the application of the Tax for Sustainability to in-scope MNEs. Future tax treaties will also need to have a coordination clause to avoid inadvertently reintroducing obstacles to the application of the Tax for Sustainability.

In addition to removing the tax treaty obstacles, the Multilateral Convention would also need to circumscribe the exercise of the right to tax MNE profits in other means similar to the proposed tax. It would also require that a participating country amend its domestic law by deducting the tax in computing taxable income for the CIT.

5.9. Withdrawal of DSTs

With a new Tax for Sustainability, countries should withdraw their DSTs. The rate of the proposed tax would be lower than the rate of the DST in many countries, but this does not mean less tax revenue. The reason is that the DST's tax base is much narrower and does not apply generally to corporate giants like cloud computing or pharmaceutical companies. Because the tax base of the proposed tax is comprehensive, the tax base would be much broader and capable of generating the same amount of tax revenue with a lower tax rate. But perhaps more importantly, the proposed tax would not lead to uncertainties in its application owing to the risks of triggering trade war with the United States or violating existing bilateral tax treaties.

Annex A illustrates the impact a new tax based on the Pillar One formula would have if converted into a "net tax rate" (i.e. a 20 per cent market share of an MNE profit above 10 per cent at a CIT rate of 21 per cent) applicable directly on the sales revenue in a country. It helps comparing the effect of such a new tax and DSTs that apply a rate of approximately 3 per cent on the revenues from digital services only (which excludes B2B cloud computing services and other profitable businesses like pharmaceutical and financial services).

6. A Generational Moment[82]

6.1. Time to act

"We remain committed to reaching a global and consensus-based solution building on the solid basis of the Reports on the Blueprints for Pillar One and Pillar Two, by mid-2021", said the G20 Finance Ministers.[83]

The Inclusive Framework was "urged" to address "the remaining outstanding issues with a view to achieving an agreement by the set deadline."[84]It appears that a window of opportunity exists to bring about an historical change in the taxation of large MNEs.

If history is of any inspiration or prediction of what is to come, the present moment seems like a golden opportunity. Global challenges in the past have led to international consensus. For example, the agreement to create the League of Nations after World War I (WWI) led to the model conventions, which laid the foundation of today's tax treaties.[85]The Bretton Woods

82. US Proposal, *supra* n. 12 .
83. Collier, Devereux & Vella, *supra* n. 6 .
84. Id.
85. Jogarajan , *supra* n. 34 .

consensus[86] reached after World War II (WWII) led to the creation of the liberalization of trade and increased cross-border investment, which led to the proliferation of bilateral tax treaties, embodying the international tax consensus. The looming global social, economic and environmental crisis led to the UN SDGs and Paris Agreement. The Blueprint - developed as part of the BEPS Project, which was triggered by the 2008-09 global financial crisis - has the potential of becoming a global tax instrument to facilitate the implementation of UN SDGs and the Paris Agreement.

Another dimension of history is equally inspiring, albeit for different reasons – unilateralism is the beginning or trigger of multilateralism.[87] The multilateral process under the auspices of the League of Nations to prevent double taxation became necessary because countries unilaterally introduced income taxes. The urgency of consensus after WWI arose because domestic tax charges increased manifold to fund the war effort, which exacerbated the extent of double taxation. The model tax conventions developed by the League of Nations during the inter-war period were put into practice only after WWII decimated the budgets of European countries, and the United States and European countries wanted to do something about double taxation in the reconstruction under the Marshall Plan. Before WWII, countries such as the United States and Canada relied on domestic law to eliminate double taxation unilaterally.[88] The United Kingdom did not conclude any tax treaties until 1945, when it signed with the United States.[89] Similarly, Canada had its first treaty in 1942, also with the United States.[90]

The history of international taxation suggests that unilateral actions are a typical precondition for creating circumstances that stimulate conditions in which global consensus may be built. The recent rise of unilateral DSTs at a time when global consensus remains illusive is similar to patterns that could be observed in the inter-war period. The global community should be encouraged to treat the unilateral DSTs as a jumping board towards a global mechanism that is capable of addressing the underlying needs of countries. In other words, the rising unilateralism is a natural phenomenon to the crisis and a cry for reform. Our proposed Tax for Sustainability responds to such a cry by providing countries with a workable multilateral solution that is infused with the common values of sustainability.

Our proposed repurposing of the Blueprint is a workable solution. It aims to simplify the Blueprint by elevating it out of the existing complex system. It also strives to increase the chance of the Blueprint becoming a stable instrument for the future. As a global tax instrument, the repurposed Blueprint would recognize the global nature of MNEs and the corresponding social and fiscal responsibility. Digitalization and globalization present unprecedent opportunities for MNEs to earn profit from exploiting global markets and customer/user created “free” data. Although functioning as global firms, the current international tax system engages with them on a nation-to-nation or bilateral basis and regards each member of the corporate family as separate or as an orphan. In the face of growing global crisis and with the momentum built by the BEPS Project, there is likely no better time to legally require these global firms to contribute to the common cause of sustainability or, to use our earlier analogy of rent, to contribute to the effort in maintaining the common areas and building infrastructure so that our world does not collapse on us.[91]

6.2. Think big

At this juncture, it is important to think big. The problem facing the global community is big. The number of countries participating in the UN SDG agenda and Paris Agreement is big. The amount of tax revenue required to finance spending on sustainable development and climate change is big. The size of MNEs and their economic might are big. The challenge in simplifying the Pillar One as currently conceived is big. Repurposing the taxation of MNEs is the big idea.

The proposed tax has the promise of bridging the concerns of various key stakeholders about the Blueprint, article 12B and DSTs. Countries with DSTs want to raise revenue and achieve fairness, while the United States want to be free from discriminatory taxation of US-based MNEs and MNEs want tax certainty and predictability. The proposed tax replaces the DSTs at national level with a global regime and on a broader basis. Even though over half of the in-scope MNEs may still be based in the US, MNEs based in other jurisdictions would also be subject to the tax.

The proposed tax is transitional in the following respects. It is built on the areas of consensus about the Blueprint but takes the Blueprint proposal to the next level – a separate tax on MNEs as opposed to mere tax base allocation. It draws on insights

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86. D. Rodrik, *The Globalization Paradox* (W.W. Norton and Company, 2011), at pp. 67-88.
87. We thank Johann Hattingh for bringing this point to our attention.
88. For more information, ***see*** M.J. Graetz and M.M. O’Hear, *The “Original Intent” of U.S. International Taxation* , (1997) Duke L. J. (vol. 46) 1021-1108; and C. Campbell and R. Raizenne, *The 1917 Income War Tax Act: Origins and Enactment* in J. Li, J.S. Wilkie & L. Chapman, eds., *Income Tax at 100 Years: Essays and Reflections on the Income War Tax Act* (Canadian Tax Foundation, 2017), at pp. 250-252.
89. J.F.A. Jones, *The History of the United Kingdom’s First Comprehensive Double Taxation Agreement* in John Tiley, ed., *Studies in the History of Tax Law* , vol. 3 (Hart Publishing, 2009), at Part 3.
90. B.J. Arnold & J. Sasseville, *A Historical Perspective on Canada’s Tax Treaties* in Li, Wilkie & Chapman, *supra* n. 84 , at pp. 112-113.
91. K. Davis-Nozemack & K. Kisska-Schulze, *Applying Sustainability to Tax* , (2020) 23 Florida Tax Rev. 2, at p. 506: “For too long, tax policy literature has skirted meaningful normative analysis. It avoids contemplating challenging normative questions and interrogating underlying assumptions. The world faces the simultaneously marvelous and pernicious effects of industrialization and rapid economic expansion, but current analytical approaches to tax have not adequately considered the role that tax plays in contributing to and can play in ameliorating the national and global crises wrought by industrialization.” *[footnote omitted]*

from the DSTs and seeks to achieve the policy goals of DSTs through a multilateral instrument with the benefit of simplicity and efficiency for both MNEs and national tax authorities. In order to circumvent the complexity caused by interactions with existing rules, especially with respect to double taxation elimination, the proposed tax would adopt simpler proxies and reduce the need for double taxation relief. As an evolved Blueprint proposal, the proposed tax could operate in parallel with Pillar Two in that a global minimum tax rate could be used to set the tax rate for the proposed tax. Its scope would be limited to the market-based profit of the most profitable MNEs.

6.3. Think simple

For members of Inclusive Framework to accept the Blueprint proposal, it needs to be simple, certain and, perhaps most importantly, serve their needs. Our proposal is simpler and more certain through reducing the need for line-drawing and more reliance on objective data or proxies. By removing the barriers of bilateral treaties on taxing MNEs on a group and formulaic basis, the proposal offers more stability as well as simplicity. Concerns with tax sovereignty are addressed through limiting the new regime to market-based profit of in-scope MNEs and giving countries the option to set their tax rates and choose whether to credit the new tax against the CIT.

The simpler method for computing tax that mimics a DST should serve the needs of developing countries. A built-in feature for potentially doubling the tax payable to low-income countries could even be conceived through designing the tax rate, which would give additional assistance to those countries.

Simplicity is important with a new tax instrument. We are reminded of the Canadian Income War Tax Act (1917) that had only four pages but contained the necessary features to grow to meet the needs of the society.[92]Our proposed repurposed Blueprint proposal has the potential of becoming a basic regime of taxing MNEs, with the necessary modifications of the formula to cover not only market-based profit but also other types of residual profit or profit in general. Such directional change has already occurred through the BEPS Project, which signals the beginning of a new regime that regards MNEs as unitary entities. Thinking of the Blueprint in this fashion may help liberate thinking about opting for simpler and less intricate technical design options. Given the amount of revenue at stake and the importance of generating global consensus, it would be wise to keep the Blueprint as simple as possible.

7. Conclusions

Our proposed Tax for Sustainability may appear to be idealistic and aspirational. However, it is more realistic in the sense that this is what the world needs right now and what politicians, G20, developed and developing countries and many business leaders are asking for in different ways: financing sustainable development, promoting corporate responsibility, having a simple and fair taxation system. Efforts to simplify the Blueprint may have been constrained by its inseparability from the existing rules. We hope the proposed repurposing of the Blueprint can help facilitate the reaching of consensus.

Annex A

The table below illustrates the effect of a tax on the “residual” profit using sales as allocation key.

The table assumes that the profitability threshold (or the “routine” profit) is set at 10%, the portion of the excess profit (or the “residual” profit) is 20%, that the sales in a jurisdiction is the allocation key, and that the jurisdiction’s corporate tax rate is the OECD average of 21%.[93]

The tax rate as currently conceived will be lower than the nominal rate of existing DSTs. However, the number of large MNEs in scope will be more than digital giants (it would include pharmaceutical companies for examples) and would also include B2B cloud computing services which are not covered under the vast majority of DSTs. And so, on these aspects, the tax base for this tax is broader than DSTs.

Profit margin of the MNE group above the threshold of 10% (“Residual Profit Margin”) (%)	**Tax rate applicable on in-scope revenues in markets = Residual profit margin × market share of 20% × CIT of 21% (%)**	**Amount of tax on a revenue of 500 million (USD)**
0	0.00	0
1	0.04	210,000

92. Canada, *The Income Tax War Act* , 7-8 George V., CHAP.28, assented to 20 Sept. 1917.
93. The average combined (central and sub-central government) statutory tax rate for all 109 covered jurisdictions was 20.6% in 2020 according to the OECD report *Corporate Tax Statistics: Second Edition (2020)* , available at https://www.oecd.org/tax/tax-policy/corporate-tax-statistics-second-edition.pdf (accessed 2 May 2021).

Profit margin of the MNE group above the threshold of 10% ("Residual Profit Margin") (%)	Tax rate applicable on in-scope revenues in markets = Residual profit margin × market share of 20% × CIT of 21% (%)	Amount of tax on a revenue of 500 million (USD)
2	0.08	420,000
3	0.13	630,000
4	0.17	840,000
5	0.21	1,050,000
6	0.25	1,260,000
7	0.29	1,470,000
8	0.34	1,680,000
9	0.38	1,890,000
10	0.42	2,100,000
11	0.46	2,310,000
12	0.50	2,520,000
13	0.55	2,730,000
14	0.59	2,940,000
15	0.63	3,150,000
16	0.67	3,360,000
17	0.71	3,570,000
18	0.76	3,780,000
19	0.80	3,990,000
20	0.84	4,200,000
21	0.88	4,410,000
22	0.92	4,620,000
23	0.97	4,830,000
24	1.01	5,040,000
25	1.05	5,250,000
26	1.09	5,460,000
27	1.13	5,670,000
28	1.18	5,880,000
29	1.22	6,090,000
30	1.26	6,300,000
31	1.30	6,510,000
32	1.34	6,720,000
33	1.39	6,930,000
34	1.43	7,140,000
35	1.47	7,350,000
36	1.51	7,560,000
37	1.55	7,770,000
38	1.60	7,980,000
39	1.64	8,190,000
40	1.68	8,400,000
41	1.72	8,610,000
42	1.76	8,820,000
43	1.81	9,030,000
44	1.85	9,240,000
45	1.89	9,450,000
46	1.93	9,660,000

Profit margin of the MNE group above the threshold of 10% (“Residual Profit Margin”) (%)	**Tax rate applicable on in-scope revenues in markets = Residual profit margin × market share of 20% × CIT of 21% (%)**	**Amount of tax on a revenue of 500 million (USD)**
47	1.97	9,870,000
48	2.02	10,080,000
49	2.06	10,290,000
50	2.10	10,500,000