Change in International Tax

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Ruth Mason, *The 2021 Compromise*, 172 **Tax Notes Fed.** 569 (2021), available at SSRN.

Only a fraction of tax law professors teach the course usually called "international tax." For the rest of us teaching tax at a law school, the effort that technical competency in international tax requires is unsustainable, especially given the instability of that part of the law that most affects US multinational business. But every tax professor should understand at least a little bit about the ways that international tax law is changing. I recommend reading Ruth Mason's work, most recently *The 2021 Compromise*, as a great way to gain competency regarding this evolution.

Mason's goal in this piece is to contextualize recent developments in the OECD/G20's BEPS project against the backdrop of her extensive prior work on the subject (see especially The Transformation of International Tax), and to put into perspective the changes currently underway in the international tax space. On July 1, 2021, 130 countries reached agreement in principle to Pillars 1 and 2 of the G20/OECD Base Erosion and Profits Shifting (BEPS) project. Pillar 1 concerns the allocation of taxing authority after the emergence of the digital economy and Pillar 2 is a proposal for a global minimum tax. This two-Pillar OECD project represents a second phase of the G20/OECD work on BEPS.

Mason is particularly anxious to point out that the ultimate impact of the developments under the first phase of the BEPS project should not be underestimated. Other scholars have complained that this first phase of negotiations fell far short of the policy changes that must be embraced to achieve anything like a fair and sensible system for the taxation of multinational enterprise, but Mason's view is that, however short the project's pre-2020 stages may have fallen, that activity has set the stage for Pillars 1 and 2, and it is unlikely that international tax will ever be the same. Everything is now open to change — from the processes and participants in the making of international tax policy, to the content of the consensus that will emerge for the allocation of tax shares, to the multilateral tools that are likely to become available to implement that allocation.

Mason's article provides a high-level summary of the technicalities of the Pillar 1 and Pillar 2 proposals in second phase of BEPS project. Pillar One of that project aims at reallocating taxing rights to source or market countries; and Pillar Two aims at establishing a minimum tax that would provide some self-regulation of tax competition. The fact that the outline of this second phase has been revealed (and appears to have been taken seriously enough that implementing steps may take place as early as the first quarter of 2022) makes Mason's analysis in prior work of the forces that led to the first phase, and the significance of that phase, all the more important.

Mason's article starts with the relatively familiar institutional development of the international tax regime that dominated in the twentieth century. The "1920s compromise" reflected the role of the US as an exporter of capital with the dominant goal of avoiding double taxation of its enterprises and with the arm's length standard as the primary weapon against tax avoidance. Then, this old regime became destabilized. As Mason's prior work explains, this destabilization was in part the result of the changing nature of economic global enterprise (especially the changes in the nature of cross-border economic activity that rendered useless the concept of permanent establishment). But it was also the result of other smaller fissures in the traditional system (especially the tax arbitrage made possible by the US check-the-box rules and other innovations that we non-international specialists may too often look at only from the domestic point of view). These fissures were exploited in ways that no one institution had the power or even the incentive to block.

In Mason's account, the situation changed with the 2008 financial crisis and increased publicity surrounding the

failures of the old regime. Politicians around the world felt increased pressure to look harder at the problems of international tax. The result was a shift in the identity of the participants in international tax policy, including EU institutions and a more energized G20. With that shift in participants came the possibility of cooperation that in turn led to the emerging norm of full taxation, developed in the first and second phases of the BEPS project. This norm, although not yet fully specified (and in the earliest implementation likely to reach only the very largest taxpayers), will displace the old emphasis on minimizing double taxation. This expansion of cooperative participants also makes possible agreement rejecting unilateral actions (including digital taxes) and embracing multi-lateral enforcement mechanisms. Among these mechanisms are more transparent reporting and what Mason calls “fail-safe” devices that reduce the incentive for jurisdictions to cede their right to tax by providing a contingent right to tax in others.

In sum, Mason’s new article, paired with her prior work on the subject, will be valuable to those of us teaching tax in law schools who have a vague sense of the way the old regime was supposed to work, but have not paid much attention either to the ways in which the old regime has failed on its own terms, or to the ways in which it falls short of the needs of an increasingly globalized economy. Those who read Mason’s work to understand the political economy behind the introduction of these changes will find the effort well spent.

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