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Globalization and its Fallout: Ten Years of International Tax Tumult

I. Introduction

I'd like to thank the American College of Tax Counsel for inviting me to give this prestigious lecture this evening.

I attribute this invitation to the work I've done in writing a regular column for Tax Notes. Because being asked to give this lecture honors the publication as well myself, I want to take this opportunity to thank Tax Notes for providing me with a forum to express my thoughts and views on international tax developments on a regular basis over the past 10 years, and to recognize the importance of Tax Notes to this community. The existence of a forum like the one the publication provides is also a recognition of the unique characteristics of the tax professional community – including lawyers, accountants, and economists, government officials, tax policy wonks, and taxpayers -- who have nurtured this publication, whose subscriptions have kept it viable and allowed it to support the free expression of ideas. To all of you, thank you for reading me, and Tax Notes generally.

Given that this lecture coincides precisely with the 10-year anniversary of my writing for Tax Notes, I thought I'd take the opportunity to reflect on international tax developments over that time period. That has presented me with the valuable opportunity to go back and review a decade of bi-weekly columns. There's been a lot going on in international tax in the past decade, but 10 years of writing has focused on 3 main topics.

These include the OECD's base erosion and profit shifting project, known as BEPS;¹ the 2017 U.S. Tax reform, referred to as the Tax Cuts & Jobs Act, or TCJA;² and the OECD's current work on international tax reform, colloquially known as the 2-pillar project (formally, the OECD/G20 Inclusive Framework on

¹ See <https://www.oecd.org/tax/beps/>.

² Formally known as the Act to Provide for Reconciliation pursuant to Titles II and V of the Concurrent Resolution on the Budget for Fiscal Year 2018, Pub. Law No. 115-97, 115th Cong., 131 STAT. 2054 (Dec. 22, 2017).

BEPS' Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalization of the Economy).³

Other topics have recurred periodically along the way, including: EU state aid and the application of this doctrine to cross-border planning; the structure of international tax governance, mostly focused on developments at the UN, and divergences and differences between the UN work and the OECD's; developments in technology (including the impact of digital broadly, but also, more narrowly, developments in cryptocurrency and Artificial Intelligence; and most recently, the Supreme Court case of *Moore v. United States*,⁴ which has prompted a re-examination for many of the scope of the 16th amendment, the meaning of the terms "realization," and "income," and the use of the Supreme Court's agenda as a means of advancing a political agenda.

But the goal here is not simply to provide a recap of 10 years of tax developments. Looking for themes in the international tax policy debates of the past decade allows us to reflect on macro-economic and geo-political changes, and how the work of tax advisors is influenced by, and influences, these larger macro shifts. These broader geopolitical and economic developments include:

- Globalization, and the more recent retrenchment therefrom;
- The rise of China as an economic powerhouse, and the subsequent backlash;⁵
- The rise of Asia more generally and the BRICS large emerging economies;⁶
- The growth of global supply chains;⁷

³ See OECD, Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy (Oct. 8 2021) <https://www.oecd.org/tax/beps/statement-on-a-two-pillar-solution-to-address-the-tax-challenges-arising-from-the-digitalisation-of-the-economy-october-2021.htm> .

⁴ Docket No. 22-800 (docketed Feb. 23, 2023).

⁵ See Mindy Herzfeld, *Pillar 2, State Aid, and Industrial Policy*, 181 TAX NOTES FEDERAL 399 (OCT. 16, 2023). See generally, James Andrew Lewis, Supply Chain Sovereignty and Globalization (Oct. 19, 2022), <https://www.csis.org/analysis/supply-chain-sovereignty-and-globalization> (noting that "[s]upply chains are a focal point for tensions between the United States and China, and a central task for democracies is to reduce China's role in international supply chains," and that "[t]ensions over supply chains are also part of an increased desire for tech sovereignty.")

⁶ See Valentina Romei and John Reed, *The Asian Century is Set to Begin*, FT (Mar. 25, 2019); Edited by Vai Io Lo and Mary Hiscock, eds., *The Rise of the BRICS in the Global Political Economy: Changing Paradigms?* (Elgar Online 2014).

⁷ The OECD estimated in 2020 that 80 percent of world trade passed through global supply chains. Daniel Vaughan-Whitehead, *Behind the Rise of Global Supply Chains*, (Cambridge Scholars Publishing 2022) at 2 (noting that "In almost four decades, the dominant business model has completely changed," and describing how in the 1970s and 1980s the purpose of a multinational company was to set up subsidiaries in key strategic locations to be used for mass production and platforms for exporting all over the world, but since that time, companies' "strategy of

- The Global Financial Crisis, which in turn led to concerns about inequality;⁸
- The increasing importance of technology, and a growing divergence between the United States and Europe in this area; and
- The rise of private capital.⁹

Consideration of international tax developments over the last decade within the context of broader macro-economic and geo-political trends prompts several questions about how and where tax lawyers fit into the picture. To what extent did tax lawyers help facilitate globalization trends, including destructive ones such as the global financial crisis? Or is it more appropriate to characterize tax lawyers merely as reactors and responders to client demands, working within a blueprint and on a stage prescribed for them both by larger economic trends and by individual clients? To what extent should tax lawyers be consider accountable for the trends in cross-border tax planning that has prompted severe backlash resulting in multilateral coordination? Are tax lawyers, in providing advice to their clients, doing so driven by client demands, or do they have little flexibility in shaping, or whether they play a role in shaping those demands?

II. The Prequel

To set the stage of the international tax policy developments of 2014-2024 – the time span of my writing for Tax Notes International – we start by taking a few steps back, with a review of some of the transactions that shaped my experiences in private practice. These transactions form the backdrop to a tax profession that was – and is -- increasingly internationally focused; aspects of the way in which international tax was practiced at large professional services firms ultimately led to the OECD’s adoption of a major project to crack down on cross-border tax planning.

All Spins, All the Time

My first week of employment at Weil Gotshal & Manges in NYC in late 1996 -- my first job in the tax field out of law school -- happened to coincide with the

expansion rapidly changed: it is now based mainly on the use of external suppliers or contractors that produce for the company all necessary goods to be sold to consumers.”)

⁸ See, e.g., Mohamed A. El-Erian, *The Only Game in Town: Banks, Instability, and Avoiding the Next Collapse* (2016); Joseph Stiglitz, *Freefall: America, Free Markets, and the Sinking of the World Economy* (2010).

⁹ See Sirio Aramonte and Fernando Avalos, *The Rise of Private Markets*, BIS Quarterly Rev. (Dec. 2021).

release of the check-the-box regulations.¹⁰ Although the full extent of the regulations' impact in the international arena was not known at the time, these regulations helped facilitate cross-border planning by making it easier for taxpayers to select their preferred tax treatment without a lot of legal complexity, and by allowing them to benefit from the variations among different jurisdictions' tax rules. Planning that could produce but modest benefits in an era of limited cross-border activity became turbo-charged as the changes in tax rules coincided with the growth of new foreign markets for U.S. businesses and ever more complex supply chains.

The flip side of growth in global activity was the demise of some U.S. corporate giants. The first project I worked on at Weil was the spin-off of Westinghouse, which resulted in the separation of the industrial group from the more recently acquired media operations. In retrospect, the Westinghouse spin represented the decline of a U.S. industrial icon, and with it, the U.S. industrial conglomerate more broadly. At the time of the spin-off transaction, the name Westinghouse was practically synonymous with U.S. research and development and science prowess.¹¹ But the company began to morph in the 1990s, when it started to acquire TV and radio stations, and eventually purchased CBS in 1995 and Infinity Broadcasting in 1996. These acquisitions then prompted the spin-off of the remaining industrial businesses.

In a way, Westinghouse's story is also one of how large mature businesses have been combined and repackaged in the last several decades, in structures heavily influenced by tax considerations. In 2000, CBS merged with Viacom. Westinghouse's nuclear energy business, meanwhile, was purchased by British Nuclear Fuels in 1999; then by Toshiba in 2006. Private equity firm Brookfield Business Partners purchased Westinghouse Electric in 2018.

Another large transaction that occupied my time at Weil Gotshal involved the split-up of U.S. telecom US West. If the Westinghouse spin represented the upheaval among U.S. industrial companies, the US West split provides a window into the dramatic changes in the telecom industry at the turn of the last century.

US West was one of the 7 Regional Bell Operating Companies that resulted from the breakup of AT&T in 1983. The 1996 transaction involved the split-off of the

¹⁰ T.D. 8697, 61 FR 66584-66593 (Dec. 18, 1996).

¹¹ See <https://westinghouse.com/pages/about>.

telephone company from the media assets, (including cable, wireless and international businesses) known as MediaOne.¹²

What happened to these 2 companies? US West merged with Qwest in 2000. Qwest merged with CenturyLink in 2011.

In 1999, MediaOne was acquired by AT&T, which followed that acquisition with the purchase of Cablevision, and then split into 3 separate companies: long distance, wireless, and broadband (then purchased by Comcast).

This is all a lot of detail about 25 year-old transactions. But recounting them and tracking the subsequent history of the companies involved allows for reflection on the extent to which these tax-driven spin-offs – in their underlying rationale and in the specifics of their structures -- were motivated both by significant changes in the business landscape and tax law changes. The repeal of the *General Utilities* doctrine¹³ made it costly to wind-up an unwanted business and so by default tilted the deal landscape towards spin-offs for repackaging corporate assets. Enactment of section 355(e) in 1997¹⁴ -- which was prompted in part by the planned Westinghouse spin/merger transaction -- forced a restructuring of that transaction and a rethink of the US West deal as well.

As an indication of just how important spin-off transactions were to achieving the corporate and business objectives of large U.S. multinationals in the late 1990s, when I departed Weil Gotshal in 1998, I then spent the next few years working on a spin-off transaction at Ford Motor Company. Ford's decision to spin off its less-profitable Visteon parts division in 2000 followed on the heels of General Motors' decision to spin-off its parts division (Delphi), but both those transactions soured as the parts companies ended up in bankruptcy a few years later.

International M&A Grows Up

Working in Deloitte's U.S. tax group for the 10 years immediately prior to my joining Tax Analysts provided me with a keen window into the types of business imperatives that were motivating taxpayers to undertake cross-border tax planning, the U.S. tax rules that were enabling that planning, and the variation among countries' tax systems which gave taxpayers the opportunity to engage in tax arbitrage in a way that the global growth of professional firms also facilitated.

¹² See <https://www.telcomhistory.org/resources/online-exhibits/telephone-company-histories/us-west/>.

¹³ *General Utilities & Operating Co. v. Helvering*, 296 U.S. 200 (1935).

¹⁴ Taxpayer Relief Act of 1997, Pub. Law No. 105-34, 105th Cong., 111 Stat. 787, Sec. 1012(a).

Among the structural business trends to which I bore first-hand witness were the rise of private equity and private capital and the growth of principal structures, which often involved migration from high-tax and high-labor cost jurisdictions into lower-cost hubs, and the deployment of cash overseas.¹⁵ The tax rules that encouraged those business trends included the growing importance of check-the-box planning, the high tax costs of repatriating cash to the United States, the growing divergence between the corporate U.S. tax rate and rates in other countries, and other countries' increasing aggressiveness in attempting to attract U.S. investment. One of the biggest changes in the practice of tax over this 10-year period involved the growing importance of the transfer pricing practice – increasingly, the most important planning was less dependent on the technical parameters of the law, and more about the economics of the costs that could be justified for cross-border transfers of and returns on intellectual property.

The same time period coincided with increasing pressure on U.S. companies to invert overseas to take advantage of more advantageous tax regimes, and the congressional backlash that resulted, along with subsequent restrictive interpretations of that law by Treasury. This allowed for a glimpse into the way in which tax cultures and different risk profiles could influence corporate decision making, with some companies willing to move forward with an inversion transaction that could increase earnings per share, and others reluctant to do so if it meant undue publicity.

Working both as an advisor to public companies and on private equity deals provided a unique window into the different risk appetites of private as compared to public companies. While public companies' planning drew lots of attention – including from U.S. congressional committees¹⁶ and in other countries' Parliaments¹⁷ -- private companies had much greater leeway to take riskier positions without the concerns about public attention.

It turns out that the ten years I spent at Deloitte overlapped with a turbo-charged globalization. In tax structuring, this meant increasing integration of business lines across jurisdictions. But the globalization trend also impacted the advisory side of

¹⁵ Tax Increase Prevention and Reconciliation Act of 2005, Pub. Law No. 109-222, 109th Cong., 120 STAT. 345 Sec. 103(a)(2).

¹⁶ See S. Hrg. 113-90, OFFSHORE PROFIT SHIFTING AND THE U.S. TAX CODE—PART 2 (APPLE INC.), HEARING BEFORE THE PERMANENT SUBCOMMITTEE ON INVESTIGATIONS OF THE COMMITTEE ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS UNITED STATES SENATE, 113th Cong., 1st Sess., (May 21, 2013).

¹⁷ See David D. Stewart, U.K. Public Accounts Committee Grills HMRC Over Tax Gap, Avoidance, 2013 WTD 209-1 (Oct. 29, 2013).

the business, as the Big4 accounting firms grew ever more global with their coordinated advice.

All these experiences provided me a unique perspective from which to reflect on international tax policy developments as a contributing editor for Tax Notes International beginning in 2014.

III. Tax Notes International

As noted in the introduction, much of my writing for Tax Notes International has addressed the 3 big developments in international taxation of the past 10 years – BEPS, TCJA, and the OECD 2-pillar project. But before turning to those specific topics, it's worthwhile to note that the position created for a contributing editor at Tax Notes International itself reflected a recognition of the growing importance of international tax.

BEPS

My writing on BEPS has focused primarily on 2 big questions: What motivated it? And what did it accomplish?¹⁸

*Motivations*¹⁹

The official OECD line is that BEPS grew out of public ire over the global financial crisis, and the resulting cutbacks to public services driven by government austerity programs.²⁰ But – as I've previously argued -- it's misleading to draw a direct line from public discontent to a government focus on corporate tax avoidance.²¹ It's perhaps more accurate to say that a focus on corporate taxpayers proved useful for governments and activists that needed an easy explanation for why lower-income individuals bore the brunt of the financial crisis.²²

¹⁸ BEPS had its origins in a 2012 G20 Leaders meeting held in Los Cabos, Mexico. See G20 Leaders Declaration (Jun. 2012): "We reiterate the need to prevent base erosion and profit shifting and we will follow with attention the ongoing work of the OECD in this area." See <https://www.g20.org/en/about-the-g20/previous-summit?activeAccordion=73814cd9-ed16-4890-aca8-232da5793466%2C7da5c65a-e9d1-4d3f-8ba3-4991ac05c2c0>.

¹⁹ Much of my writing on this topic is found in the articles listed in the subsequent footnotes published in Tax Notes International, as well as my article *The Case Against BEPS: Lessons for Tax Coordination*, 21 Fl. Tax L. Rev. 3 (2017).

²⁰ See <https://www.oecd.org/tax/beps/about/>: "Following the financial crisis in 2008, the G20 countries put tax at the top of their agenda and have led the fight against tax evasion and avoidance."

²¹ Mindy Herzfeld, *Rocky Shoals Ahead for International Tax*, 96 Tax Notes Int'1 1057 (Dec. 23, 2019).

²² Mindy Herzfeld, *Rocky Shoals Ahead for International Tax*, 96 Tax Notes Int'1 1057 (Dec. 23, 2019).

More broadly, the larger backdrop to the BEPS project was the trend in globalization that also exacerbated the consequences of and reactions to inequality.²³

A third motivation for countries' increased focus on cross-border profit shifting was the rise of U.S. tech, and the concentration of tech dominance in the United States- along with the high profits generated by U.S. tech companies. These concerns have not subsided.²⁴

The BEPS project can also be explained through an institutional perspective on history.²⁵ The OECD would have become marginalized if it was limited to representing its 38 member countries in the international tax arena.²⁶ Taking on a project with buy-in from a larger group of countries -- at the behest of the G20 -- allowed the OECD's tax function to magnify its importance on a larger political stage.²⁷

Another possible prompt for the BEPS project is the integrationist agenda within the EU. That effort facilitated cross-border profit shifting within Europe, while EU treaty constraints prevented member countries from cracking down on intra-EU planning.²⁸ BEPS allowed the EU commission to use the OECD as a cover to advance an agenda that benefited integration.

All of these trends: globalization, growth of supply chains, and the rise in value of mobile intangible assets -- grossed-up the benefits of, and so facilitated the incentives and opportunities for, cross-border tax planning.

But other tax trends – driven by governments rather than taxpayers and advisors – also played a role. Intensifying tax competition among countries²⁹ led to an

²³ Mindy Herzfeld, *Rocky Shoals Ahead for International Tax*, 96 Tax Notes Int'l 1057 (Dec. 23, 2019).

²⁴ Mindy Herzfeld, *Rocky Shoals Ahead for International Tax*, 96 TAX NOTES INT'L 1057 (Dec. 23, 2019).

²⁵ On the importance of institutions in understanding historical trends generally, see Sven Steinmo, *Historical institutionalism*, in Donatella and Keating (eds) *Approaches and Methodologies in the Social Sciences*. (2008).

²⁶ See Library of Congress Research Guide

<https://guides.loc.gov/brics#:~:text=%22BRICS%22%20is%20the%20acronym%20denoting,Economics%20Paper%20No%3A%2066>), explaining how the term “BRIC” was originally coined in 2001 by the Goldman Sachs economist Jim O'Neill in a report, *Building Better Global Economic BRICs* (Global Economics Paper No: 66). The first BRIC annual summit took place in 2009.

²⁷ See Mindy Herzfeld, *BEPS 2.0: The OECD Takes on New Territory*, 81 Tax Notes Int'l 987 (Mar. 21, 2016).

²⁸ See Mindy Herzfeld, *The ECJ Takes on the OECD*, 73 Tax Notes Int'l 107 (Jan. 13, 2014).

²⁹ See Mindy Herzfeld, *Political Reality Catches Up With BEPS*, 73 Tax Notes Int'l 387 (Feb. 3, 2014) (describing how the prior two decades had seen “a significant percentage of OECD member countries ... put in place programs to attract and retain mobile income. The OECD project did not lead to the elimination of targeted tax regimes that attempt to attract mobile income...”).

increasing disparity between the U.S. rate and corporate tax rates in the rest of the world.³⁰ The lack of a U.S. participation exemption and the accounting treatment of deferred earnings meant that foreign tax planning was an ever-growing part of the U.S. advisor's playbook.³¹

What did it accomplish?

There's not a lot of data one can look to for answers as to what BEPS accomplished. Economic data do not paint a clear picture of the impacts from specific provisions, and it's always difficult to separate results specifically driven by tax changes from those prompted by other economic events. In the case of BEPS, piecing out the causes and effects is even more challenging because the project was multilateral, and it's hard to separate out changes prompted by BEPS reforms from those resulting from the 2017 U.S. tax law changes. Moreover, the data in 2020 and subsequent few years is muddied by COVID.

Corporate financial statement data shows no material increase in companies' effective tax rates post-BEPS, but this picture is complicated by the fact that TCJA – coming on the heels of BEPS changes -- reduced the U.S. rate by 14 points. Other types of changes are harder to capture in numbers but can be gathered through anecdotal evidence of behavioral modifications. Such anecdotal evidence suggests that the BEPS rules have prompted alterations in corporate behavior and to the tax planning strategies proposed by advisors. Although the number of tax professionals hasn't really decreased, it's possible that, rather than being focused on achieving very-low effective tax rates, corporations and their advisors are now spending more time engaged in compliance work and planning around double taxation.

Some specific BEPS reforms can be considered in isolation to try and measure the project's impact. Action 6 – a BEPS minimum standard -- mandates that all tax treaties include language stating that the treaty cannot be used to facilitate tax abuse.³² Article 29 of the OECD model now includes a principal purpose test (or, alternatively, the U.S. Limitation on Benefits article).³³ Although there is yet to be

³⁰ <https://taxfoundation.org/data/all/global/corporate-tax-rates-by-country-2023/>

³¹ See Jane Gravelle, *Reform of U.S. International Taxation: Alternatives*, CRS Rep. No. 7-5700 (Aug. 1, 2017).

³² OECD, Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, Action 6 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project (2015).

<http://dx.doi.org/10.1787/9789264241695-en> .

³³ That test states that:

“a benefit under this Convention shall not be granted in respect of an item of income or capital if it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining that benefit was one of the principal

any litigation around this principal purpose test, the vague language appears to be acting as a deterrent, at least prompting taxpayers to shy away from implementing structures the only purpose of which is to obtain treaty benefits.

Action 13 of BEPS mandates that countries adopt rules that require taxpayers to file a report providing information on profits, employment, and tax by jurisdiction (the country-by-country report). But there's little evidence to suggest that many tax administrations are utilizing these reports comprehensively. And the data – aggregated by jurisdiction – posted on the OECD website – highlights anomalies in the way the information is requested and the distortions in the way the information is produced.³⁴ But like the principal purpose test, the CbC report may have changed taxpayer behavior, pushing companies to restructure their operations to minimize risks associated with disclosure of facts that could flag discrepancies to tax authorities.

Other aspects of BEPS worth considering as part of an effort to measure the project's impact include the anti-hybrid rules (BEPS action 2)³⁵ and action 5, focused on harmful tax practices, which introduced substance requirements for patent boxes.³⁶ Here, too, it's difficult to come by quantitative data that permit definitive conclusions to be drawn about the project's effects. But anecdotally, there are suggestions that companies are less likely to use hybrid instruments than previously, and that they are putting more substance in jurisdictions in which they hold intellectual property. The DEMPE (Development, Enhancement, Maintenance, Protection and Exploitation) transfer pricing standard – which requires an alignment of the return on capital and risk with substantive activities taking place in a jurisdiction -- also has prompted behavioral changes.

Another potential impact of the BEPS project is its influence on U.S. tax reform. Although the need for the reform of U.S. international tax rules had been recognized for years before BEPS was a glimmer in Pascal Saint-Amans' eye, and

purposes of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of this Convention.”

OECD, *Model Tax Convention on Income and on Capital* Art. 29(9) (2017).

³⁴ https://stats.oecd.org/Index.aspx?DataSetCode=CBCR_TABLEI See Martin A. Sullivan, *Are Country-by-Country Reports Worthless?* 97 *Tax Notes Int'l* 140 (Jan. 13, 2020); Martin Sullivan, *Five Years of CbC Reporting Yields Disappointing Results*, 180 *Tax Notes Federal* 1207 (Aug. 21, 2023).

³⁵ OECD, *Neutralising the Effects of Hybrid Mismatch Arrangements, Action 2 - 2015 Final Report*, OECD/G20 Base Erosion and Profit Shifting Project (2015) <http://dx.doi.org/10.1787/9789264241138-en> .

³⁶ OECD, *Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance, Action 5 - 2015 Final Report*, OECD/G20 Base Erosion and Profit Shifting Project (2015) <http://dx.doi.org/10.1787/9789264241190-en> .

although members of Congress would be reluctant to describe U.S. law changes as a response to a multilateral project, they were also acutely aware of the changes to the international tax competitive landscape brought about by BEPS.

Against the tally of BEPS accomplishments one must weigh the list of things left undone. For one, BEPS didn't begin to address what was for many countries the primary motivator of the project, namely providing more taxing rights for market countries over tech profits generated mainly by U.S. headquartered companies.³⁷ Instead, the BEPS action 1 report simply laid out alternatives without providing any recommendations. Also missing from the list of BEPS successes was any recommendation for adoption of CFC (controlled foreign corporation) rules, which were summarized in BEPS action 3.³⁸ That report was limited to a comparison of different CFC regimes.

More broadly, the countries involved in the BEPS project declined to revisit the underlying principles of the international tax system in light of technological developments, globalization, and the increased economic strength of former colonies – all of which had prompted the tensions that gave rise to BEPS in the first place.³⁹

Ultimately, the failure of the BEPS project to address these systemic questions prompted some countries to take unilateral action shortly after its completion,⁴⁰ highlighting another disappointment of the project: its failure to resolve questions around the OECD's legitimacy in representing the interests of a broad spectrum of countries not limited to OECD members.⁴¹

Before discussing what is often referred to as BEPS 2.0, we'll take a detour to the United States to discuss the TCJA.

U.S. Reform: 2017 Tax Cuts & Jobs Act

³⁷ OECD, *Addressing the Tax Challenges of the Digital Economy, Action 1 - 2015 Final Report*, OECD/G20 Base Erosion and Profit Shifting Project (2015) <http://dx.doi.org/10.1787/9789264241046-en>.

³⁸ OECD, *Designing Effective Controlled Foreign Company Rules, Action 3 - 2015 Final Report*, OECD/G20 Base Erosion and Profit Shifting Project (2015) <http://dx.doi.org/10.1787/9789264241152-en>.

³⁹ Mindy Herzfeld, *Rocky Shoals Ahead for International Tax*, 96 Tax Notes Int'l 1057 (Dec. 23, 2019).

⁴⁰ Mindy Herzfeld, *The OECD Consults on a New Tax World Order*, 93 TAX NOTES INT'L 702 (FEB. 18, 2019)

⁴¹ "There are also larger — and more serious — concerns about the continued legitimacy of the process for developing international tax rules. Although the OECD managed to maintain a role as a global rule-setter with the BEPS project, unhappiness with some of the recommendations thrust the organization into phase 2 of a mission to develop rules for taxing the digital economy." Mindy Herzfeld, *Rocky Shoals Ahead for International Tax*, 96 Tax Notes Int'l 1057 (Dec. 23, 2019).

As with the BEPS project, birth tax and larger macro-economic and geo-political trends were factors in prompting Congress to enact major changes to the international tax rules in 2017. But far from being an automatic response to BEPS, the reforms introduced by TCJA were the culmination of over a decade of bipartisan policy proposals.⁴²

The drivers for major reform on the tax side include the growing discrepancy beginning in the 1990s between the corporate tax rates in the rest of the world and the U.S. corporate rate; the fact that the U.S. worldwide system imposed tax on dividends from foreign subsidiaries to U.S. corporate shareholders at the full 35 percent corporate rate, while the rest of the world had moved towards territorial taxation.⁴³ These trends led to a lockout effect of almost \$3 trillion of foreign earnings kept offshore prior to TCJA's enactment.⁴⁴

Then there were the incentives for foreign-to-foreign planning that maximized the benefits for U.S. companies to move their intellectual property offshore, which included the check-the box regulations⁴⁵ (along with enactment of section 954(c)(6)); and expansion of patent boxes and other special tax regimes adopted by countries throughout the world.⁴⁶

All of these developments led to the pernicious trend of U.S. companies inverting overseas, one that the Obama administration attempted to stop through regulations, but that Republicans repeatedly emphasized demonstrated the need for comprehensive reform.⁴⁷

On the political side, the spark for TCJA was provided both by President Trump's insistence on a very low corporate tax rate, the failure of the Republican campaign to repeal Obamacare – which intensified their need for a legislative win, and their

⁴² See Mindy Herzfeld, *Designing International Tax Reform: Lessons from TCJA*, 28 Int'l Tax & Publ. Fin. 1163 (2021); Herzfeld, *How to Think About How the US Congress Thinks About International Tax Reforms*, 5 Brit. Tax Rev. 504 (2022); Harry Grubert and Rosanne Altshuler, *Fixing the System: An Analysis of Alternative Proposals for the Reform of International Tax*, 66 Nat'l Tax J. 671 (2013).

⁴³ See The Tax Foundation, *The United Kingdom's Move to Territorial Taxation* (Nov. 14, 2012) at <https://taxfoundation.org/research/all/eu/united-kingdoms-move-territorial-taxation/>.

⁴⁴ Fadi Shaheen, *The GAAP Lock-Out Effect and the Investment Behavior of Multinational Firms*, 67 Tax L. Rev. 211 (2014); Jt. Comm. on Tax'n, *Background and Selected Policy Issues on International Tax Reform*, JCX-45-17 (Sept. 28, 2017).

⁴⁵ 1998 C.B. 334.

⁴⁶ See Cong. Rsch. Svc., *Patent Boxes: A Primer*, R44829 (updated May 1, 2017).

⁴⁷ See Republican Staff, Committee on Finance, United States Senate *Comprehensive Tax Reform for 2015 and Beyond*, (Dec. 2014) available at 2014 TNT 239-25.

corresponding willingness to fund corporate tax reforms by increasing the deficit and without requiring a full offset.⁴⁸

On the macro level, the motivators for U.S. enactment of TCJA were similar to the drivers for BEPS, with a U.S. flavor. These included the significant growth over the prior decades in the share of U.S. corporate profits from overseas,⁴⁹ the growing importance of the role of both foreign markets and (cheaper) foreign labor for manufacturing by U.S. businesses; the rise in importance of global supply chain structures, and the increased value to companies of intangibles and highly mobile intellectual property.

What did it accomplish?

One clear metric of TCJA's accomplishments is the amount of cash repatriated from overseas. Bureau of Economic Affairs data indicates that the amount of quarterly repatriations is structurally higher post TCJA, and hundreds of billions were repatriated to the U.S. in the years immediately following the law's enactment.⁵⁰

A specific TCJA provision that has had clear quantifiable effects is the deduction for foreign derived intangible income, or FDII, enacted to effectuate Congress' goal of encouraging U.S. businesses to repatriate their IP back to the United States – or to keep it here.⁵¹ Marty Sullivan of Tax Notes has looked at how companies' benefits from FDII – which started off relatively small – have grown significantly since 2018.⁵²

Other features of TCJA that facilitated a trend of inbound profit shifting include the 14-point rate cut and the GILTI tax, both of which, combined with FDII, made the United States a more attractive location for intellectual property relative to

⁴⁸ See Dylan Moroses, Luca Gattoni-Celli, and David Van Den Berg, *House May Adopt Senate Budget Resolution to Hasten Tax Reform*, 2017 TNT 203-4 (Oct. 23, 2017).

⁴⁹ See Mark P. Keightly, *An Analysis of Where American Companies Report Profits: Indications of Profit Shifting*, Cong. Rsch. Svc. R42927 (Jan. 18, 2023).

⁵⁰ See Bureau of Econ. Affairs, *International Transactions, International Services, and International Investment Position Table 4.2 (U.S. International Transactions in Primary Income on Direct Investment)*, available at <https://apps.bea.gov/iTable/?reqid=62&step=6&isuri=1&tablelist=57&product=1#eyJhcHBpZCI6NjlsInN0ZXBzIjpBMSwYLDYsNi0sImRhdGEiOltbInRhYmxlbGlzdCIsIjU3Il0sWyJwcm9kdWN0IiwMSJdLFsiRmlsdGVyXyMxIixbljAiXV0sWyJGaWx0ZXJfIzUiLFsiMSJdXSxibkZpbHRlc8jMyIsWyJwIiwIdLFsiRmlsdGVyXyM0IixbljAiXV0sWyJGaWx0ZXJfIzUiLFsiMCJdXV19> (last accessed Mar. 27, 2024).

⁵¹ See Senate Budget Cmte. *Explanation of the Tax Cuts & Jobs Act*, available at 2017 TNT 234-27. See also Mindy Herzfeld, *FDII and Export Subsidies: Trade Politics*, 94 *Tax Notes Int'l*, 1043 (Jun. 10, 2019).

⁵² Martin Sullivan, *Did FDII Raise Revenue for the U.S. Treasury?* 180 *Tax Notes Federal* 571 (Sept. 4, 2023).

other countries.⁵³ Support for the proposition that the base broadening and anti-base erosion measures of TCJA had some effect can be found in the fact (as accounting researchers have demonstrated) that the effective tax rates of multinationals – on average – decreased much less than the 14 point rate reduction that the law introduced, and that the effective tax rates of domestic companies decreased much more than those of multinationals.⁵⁴

Another positive outcome of TCJA is the sharp decrease in the number of inversions and foreign acquisitions of U.S. companies; Obama era regulations also may deserve at least a little credit here.

But its also difficult to draw a line from TCJA to an increase in U.S. economic growth, with the picture distorted by Covid. In 2016, U.S. GDP grew at just a 1.7 percent rate, and in 2017 at 2.2 percent, while the growth rate in 2018 was higher at 2.9 percent. But it then dropped back down to 2.3 percent in 2019, and in 2020 – reflecting the effects of Covid, it grew at just 2.2 percent. It then went into overdrive in 2021, with a 5.9 percent growth rate. Unemployment has gone down from before enactment of TCJA, from 4.8 percent in November 2016, to 3.8 percent in December 2023, but there are a multitude of factors impacting those numbers.⁵⁵

Law changes introduced by BEPS and TCJA alone would have been enough to keep tax practitioners and tax administrators busy for years. But they were not sufficient for politicians, who took no break from proposing radical reforms of international tax laws. By 2018, the OECD-led international reforms had entered a new phase – the 2-pillar project.

Pillars

⁵³ Martin Sullivan, *Did FDII Raise Revenue for the U.S. Treasury?* 180 TAX NOTES FEDERAL 1571 (SEPT. 4, 2023)

⁵⁴ Martin Sullivan, *IP Transfers and Profit Shifting*, 181 Tax Notes Federal 1541 (Nov. 27, 2023). Regarding specific companies, Sullivan has noted that the “share of Alphabet Inc.’s worldwide profits that were booked in the United States rose from 44 percent in 2016-2019 to 85 percent in 2021-2022. The increase for Microsoft Corp. was from 36 percent to 58 percent. For Meta Platforms Inc., the increase was from 33 percent to 90 percent. And for chipmakers Qualcomm Inc. and Nvidia Corp., the increases were, respectively, from 42 percent to 94 percent and from 39 percent to 84 percent.” See Mindy Herzfeld, *Tariffs, Taxes, and Trade: Shifting Dynamics*, 94 Tax Notes Int’l 795 (May 27, 2019). See Timothy Dowd and Paul Landefeld, *The Business Cycle and the Deduction for Foreign Derived Intangible Income: A Historical Perspective*, 71 Nat’l Tax J. No. 4 (2018).

⁵⁵ See Patrick J. Kennedy, Christine Dobridge, Paul Landefeld, and Jacob Mortenson, *The Efficiency-Equity Tradeoff of the Corporate Income Tax: Evidence From the Tax Cuts and Jobs Act* (Oct. 31, 2022); Martin Sullivan, *Economists Find Little Growth and Worsening Inequality From TCJA* 182 TAX NOTES FEDERAL 2307 (Mar. 25, 2024).

Although in 2015 the OECD had suggested that it was prepared to take a wait-and-see approach on whether the BEPS recommendations adequately met countries' digital tax concerns, it soon revisited that position after a number of countries took unilateral steps to address the problem.⁵⁶

But if BEPS was presumably inspired by efforts to address cross-border planning opportunities, and TCJA was about correcting the distortions created by the difference between the U.S. tax system and those around the world, it's harder to find principles underlying the 2-pillar project. The OECD has ascribed the need for the project as addressing unfinished business from BEPS – most importantly, the failure of BEPS to address countries' concerns over – euphemistically – the digitalization of the economy, but more cynically, the rise of U.S. tech companies.⁵⁷ And that might explain pillar 1. But it is harder to find a similar rationale for the take-up of a global minimum tax, just a few years after countries roundly rejected expanded CFC rules in BEPS action 3.

Without strong tax principles and underlying rationales, one is forced to look to the politics of global tax as providing an impetus for the project. One fallout from BEPS was developing countries' impressions that the international tax community had dealt them a raw deal – that a project that was supposed to reset international tax norms -- which historically had tilted taxing rights in favor of colonizing countries -- ended up merely tinkering at the edges.⁵⁸ In less-developed countries, these concerns arose in part due to expectations set by the UN's 2015 Sustainable Development Goals, under which developing countries were supposed to rely less on aid, prompting them to search for new forms of revenue. Where else to find it but in the profits of multinationals?

⁵⁶ Mindy Herzfeld, *Germany Weighs in on Digital Debate*, 92 Tax Notes INT'L 487 (OCT. 29, 2018). At the 2018 G-20 meeting in Buenos Aires, leaders released a communique committing to “work together to seek a consensus based solution to address the impacts of the digitalization of the economy on the international tax system with an update in 2019 and a final report by 2020.” Mindy Herzfeld, *BEPS Implementation, TCJA Responses Top 2019 Agenda*, 92 Tax Notes Int'l 1265 (Dec. 24, 2018).

⁵⁷ Mindy Herzfeld, *BEPS Implementation, TCJA Responses Top 2019 Agenda*, 92 Tax Notes Int'l 1265 (Dec. 24, 2018).

⁵⁸ See, e.g., Amanda Athanasiou, *BEPS Measures Called 'Interim Step' for Developing Countries*, 2019 WTD 52-10 (Mar. 18, 2019); Julie McCarthy, *A bad deal for development: Assessing the impacts of the new inclusive framework tax deal on low- and middle-income countries*, Brookings Global WP No. 174 (May 2022) available at https://www.brookings.edu/wp-content/uploads/2022/05/Tax-and-Bad-Deal-for-Development_Final.pdf.

Disgruntled countries have initiated a push at the United Nations to form an alternative framework for consideration of global tax reforms. See UN General Assembly Res. 78/230, *Promotion of inclusive and effective international tax cooperation at the United Nations* (Dec. 22, 2023).

Once again, one can look to EU integrationist goals – and EU treaty challenges – as inspiration for pillar 2 of BEPS 2.0. Large EU countries had rejected CFC rules posed by action 3 of BEPS partly due to concerns about EU treaty limitations, as expressed in the *Cadbury Schweppes* decision.⁵⁹

In 2020, the Biden administration – with its progressive agenda -- was added to this brew. Administration officials saw in the global minimum tax a way to achieve their domestic goals of raising the U.S. corporate rate and encouraging onshoring by U.S. businesses, and a means of accomplishing their overarching objectives of addressing wealth and income inequality and restoring U.S. manufacturing.⁶⁰ The Biden administration also wished to highlight – in contrast to the Trump presidency - its commitments to multilateral engagement. Participation in the OECD-led project fulfilled the administration’s domestic economic policy objectives as well as allowing them to position themselves as friendly parties on the international stage.⁶¹

Although victory on an international tax deal allowed Democrats to spin a narrative of successful multilateral cooperation,⁶² the policy objectives of pillar 2 were never really articulated – is it about taxing profits where value is created or tax harmonization?⁶³ Likewise, the lack of principles behind the reallocation of profits across countries required under pillar 1 have been hidden behind complex formulas so that no country can see where they are disadvantaged.

What Might the 2-Pillar Project Accomplish?

⁵⁹ *Cadbury Schweppes plc v. Inland Revenue Commissioners*, ECJ Case C-196/04 (2007).

⁶⁰ See Testimony of Secretary of the Treasury Janet L. Yellen Before the Committee on Ways and Means, U.S. House of Representatives (Jun. 8, 2022). Available at 2022 TNTF 111-14.

⁶¹ All these aims were articulated repeatedly by Treasury Secretary Janet Yellen, who emphasized at her first G-7 finance ministers meeting in 2021, “the Biden administration’s commitment “to multilateralism to solve global issues.” Mindy Herzfeld, *The Democrats’ New Mantra: Tax Harmonization*, 101 Tax Notes Int’l 1095 (Mar. 1, 2021) (“other countries ... welcomed the administration’s explicit rejection of the past four years of U.S. unilateralism.”). See also Chris Giles and James Politi, *Janet Yellen Signals US Return to Multilateralism in First G7 Meeting*” (Feb. 12, 2021), reporting that the United States’ positive tone in the meeting “raised hopes in other capitals that the chance of reaching agreement this year in difficult areas of global policy such as climate, digital taxes and help for the poorest countries had improved significantly”.

⁶² Mindy Herzfeld, *The Democrats’ New Mantra: Tax Harmonization*, 101 Tax Notes Int’l 1095 (Mar. 1, 2021). “In February 12 remarks to the Tax Council Policy Institute, Neal reiterated that harmonizing international corporate tax rates “ought to be a priority.”” *Id.*

⁶³ “The OECD received hundreds of pages of comments from close to 200 commentators ... in industry groups and individual companies, business consortiums in different countries, professional membership organizations and individual advisory companies, and civil society organizations. ... Many comments highlighted the project’s lack of clearly defined goals and noted that the failure to articulate its objectives raised serious questions about its merit and chance for success.” Mindy Herzfeld, *GLOBE: A Process in Search of a Purpose*, 97 Tax Notes Int’l 367 (Jan. 27, 2020).

The global minimum tax is just now coming into effect in 2024 in Europe and a few other countries, and so it is difficult at this point to say what it might accomplish; meanwhile, pillar 1 remains in negotiation and, given that U.S. ratification is a condition of it coming into effect, will very likely never be implemented.⁶⁴

The OECD has suggested that over \$2B of low-taxed profits of multinationals each year will be subject to the minimum tax,⁶⁵ and has predicted that adoption of the global minimum tax will raise approximately between \$150-192 billion annually. But emerging data about where that tax will be collected – in what are referred to as “investment hubs” or historical low-taxed regimes -- raises questions about the project’s goals.

Meanwhile, those headline numbers mask a much more complex picture. Because the OECD model rules only apply to companies with 750 million euros in revenues, it creates a strong incentive for companies to remain below that threshold. And because certain types of tax credits get more beneficial treatment than others under the rules, countries have reasons to revise their existing tax preferences to achieve maximum benefit. At the same time, the project’s focus on tax incentives as compared to all other types of government preferences inevitably will prompt countries to creatively repackage tax incentives into other types of subsidies.⁶⁶

So the real question is not how much revenue the global minimum tax will raise, but how much it will change the landscape of countries’ efforts to compete for both domestic and foreign investment, and how it will change companies’ decision making when deciding where to build a factory, where to hire people, and where to undertake R&D. Any attempt to predict those effects remains theoretical at this time. In the meantime, there’s a risk that corporations will become a scapegoat of a poorly drafted set of rules and of governments that don’t want to give up on the ability to compete to attract investment. Because countries will still offer inducements to those looking to invest their money, and businesses will continue to take advantage of those efforts.

⁶⁴ Mindy Herzfeld, *The OECD Consults on a New Tax World Order*, 93 Tax Notes Int’l 702 (Feb. 18, 2019).

⁶⁵ Felix Hugger, Ana Cinta Gonzalez Cabral, and Pierce O’Reilly, *Effective Tax Rates of MNEs: New Evidence on Global Low-Taxed Profit*, OECD Taxation Working Paper No. 67 (Nov. 2023)); Martin Sullivan, *Big Increase in OECD Estimates of Profit Subject to Pillar 2 Tax*, 181 Tax Notes Federal 1921 (Dec. 11, 2023).

⁶⁶ See Emma Agyemang, *Global minimum tax on multinationals goes live to raise up to \$220bn*, FT (Jan. 1, 2024): ““Tax competition will not die — it will shift to subsidies and credits,” [William] Morris said.”

One other consequence seems inevitable from global adoption of the OECD minimum tax rules, which is the amount of power that this agreement grants to an international bureaucracy operating with little oversight. The OECD has to date released three tranches of administrative guidance interpreting the model rules, through a process that in no sense receives the type of parliamentary debate or political review that the model rules themselves did, or that we expect from the domestic rulemaking process. OECD bureaucrats now have enormous sway over domestic tax laws and taxpayers – in countries enacting the rules, and those that are impacted by them.⁶⁷

Some thoughts on what this project has not achieved: it is not likely to bring about stability in the international tax system; it has not brought about an alignment among developing and developed countries on the validity of the proposals, and it has not brought the OECD the worldwide legitimacy that it was looking for.

Tech, The UN, and Moore

Before concluding, we will spend just a few minutes on some other topics that have recurred regularly in my writing for Tax Notes over the past decade.

Tech: Digital, + Crypto, + AI

The interaction of tech developments and tax policy is a broad topic that includes the rise of tech giants, which underlies the entire BEPS project as well as the 2-pillar project; the emergence of alternatives to fiat currency. Crypto -- which provides an opportunity for tax practitioners, policy makers, and administrators to revisit some fundamental questions underlying tax systems. The growth of artificial intelligence was the subject of the keynote panel earlier today. As a society, we're only at an early stage of wrestling with the large questions use of AI poses for ethical decision making, and – specific to the tax area – the impact machine learning may have on workers' mobility, jobs – and relatedly, the income tax base and countries' revenues. Of all the topics covered today, this area seems most likely to be a constant for the next 10 years.

⁶⁷ Another curious aspect of countries' adoption of a global minimum tax is how it fits in with other macro trends. One is the retrenchment from globalization, which might mitigate the need for a global minimum tax in the first place. Another is the fact that countries simultaneously with binding themselves to greater uniformity of domestic tax laws, countries are renewing the use of tax measures to advance industrial policy goals, illustrating the inherent tension between the desire to eliminate or minimize tax competition and the pressures to maximize foreign investment. Martin Sullivan, *U.S. Multinationals Are Becoming Less Multinational*, 181 Tax Notes Federal 1711 (Dec. 4, 2023) (describing how “a decade-long trend of shrinkage in foreign share of U.S. multinationals' worldwide activities continued through 2021”).

The UN and International Tax Governance

As alluded to above, another topic that's been a recurring theme is the question of the appropriate forum for international tax governance. Although tension between the UN and the OECD in the international tax rulemaking area has been a constant over the past 10 years, the UN's efforts to take on a larger role in this space – which have recently begun to bear fruit – is another aspect of the fallout from the OECD's 2-pillar project.⁶⁸

Moore

I'll close with a brief mention of the *Moore* case currently pending before the Supreme Court.

Although the case raises some basic questions about basic principles of our income tax system, it too can be viewed as an outgrowth of the trends highlighted above, of a political system attempting to grapple with the challenges of taxing cross-border income fairly and in a way that doesn't impede international commerce. One can trace the *Moore* case – which is derived directly from enactment of TCJA – to the expansion of efforts to tax U.S. persons on foreign earnings.

The implications of a decision in *Moore* in favor of the taxpayer have been written about extensively, and will not be repeated here. But I would like to highlight the work of another Tax Notes colleague – Joe Thorndike, who, together with Ajay Mehrotra of Northwestern University, has written about tension within the organized tax bar over its dual roles of client advocacy and champions of sound tax policy, and described how ABA tax section leaders have in the past “opted for discretion over valor, choosing to neither indict nor defend proposals that undermined the tax system, its fairness, or its revenue productivity.”⁶⁹

Which brings us to the conclusion.

IV. Tax Lawyers' Role in Globalization and its Fallout

⁶⁸ Mindy Herzfeld, *The U.N.'s Role in Rewriting International Tax Rules for the Digital Age*, 94 Tax Notes Int'l 601 (May 13, 2019).

⁶⁹ Joseph J. Thorndike and Ajay K. Mehrotra, “*Who Speaks for Tax Equity and Tax Fairness?*” *The Emergence of the Organized Tax Bar and the Dilemmas of Professional Responsibility*, 81 Law & Contemp. Problems 203 (2018).

The cross-border tax planning trends that ultimately gave rise to BEPS and other responses by international organizations and domestic legislatures didn't arise in a vacuum, but were part and parcel of the larger macro-economic and geo-political forces that changed business practices and facilitated inter-government competition over foreign direct investment. But tax lawyers cannot and should not be viewed as mere reactors to these trends. In developing novel planning strategies together with corporate taxpayers, they played a role in facilitating global business structures, motivating political concerns over the stripping of domestic revenue bases. Ultimately, they are left to deal with the fallout as well, which involves political backlash, adoption of complex global tax rules, and uncertainty over their implementation.