



Budget Model

Revenue and Profit Shifting for the U.S. in a Global Minimum Tax Agreement

Summary: PWBM estimates that tax policy changes in low-tax countries in response to the recent OECD global minimum tax deal could cost the U.S. as much as 50 percent of its minimum tax revenue.

Key Points

- The October 8th agreement among 136 countries to impose a minimum tax rate of 15 percent on their corporations' foreign income could help curb the exploitation of tax havens by both U.S. and foreign corporations while lessening harms to U.S. competitiveness.
- However, if low-tax countries respond to the minimum tax by increasing their own tax rates on U.S. multinationals, U.S. revenues from the minimum tax would be lower than projected. PWBM estimates that responses by low-tax countries could cost the U.S. as much as 50 percent of its minimum tax revenue.
- This agreement would not end international tax competition. U.S. tax rates and incentives to locate intangible assets in the U.S. will determine whether multinationals respond by repatriating mobile profits or by pursuing more aggressive tax avoidance strategies.

The [October 8th agreement](#) by 136 countries negotiating through the Organisation for Economic Co-operation and Development (OECD) on reforms to the international tax system marks another step forward for a proposed 15 percent global minimum tax, referred to as Pillar 2. Under Pillar 2, all countries would ensure that their multinational enterprises pay a tax rate of at least 15 percent on foreign income by levying a "top-up" tax on those that paid less than 15 percent to other countries.¹ Key details of the tax remain to be worked out, and its implementation likely faces significant legislative and technical hurdles. But if it is adopted, the minimum tax would transform the global tax environment, presenting opportunities and risks for the United States.

Proposed Changes

U.S. multinationals are already subject to a minimum tax on foreign income under the Global Intangible Low-Taxed Income (GILTI) regime enacted in 2017. Other countries with major multinational enterprises generally exempt most or all of their foreign income from taxation. Widespread adoption of the Pillar 2 regime would move toward leveling the playing field for U.S. businesses by ensuring that foreign multinationals also face a minimum tax on their foreign income.

However, the proposed Pillar 2 regime imposes a higher [effective minimum tax rate](#) than the current GILTI regime. Though Pillar 2's 15 percent tax rate is only moderately higher than the rate on GILTI, it adopts a more restrictive approach to determining taxable income and tax credits.² Under GILTI's broader approach, U.S. multinationals can still [benefit from shifting profits to affiliates in low-tax countries](#). Pillar 2 largely eliminates these benefits and makes it much more challenging for multinationals to exploit tax havens.

Recent proposals from the [Biden administration](#) and the [House Ways and Means Committee](#) would align the U.S. minimum tax on GILTI with Pillar 2's narrow approach to income and credits. The House proposal includes other changes to GILTI that are consistent with Pillar 2.

Both plans also raise the tax rate on GILTI above the 15 percent rate that foreign corporations would face under Pillar 2, with potentially significant consequences for U.S. competitiveness:

- The administration proposed raising the minimum tax rate on U.S. multinationals' foreign income to 21 percent. If other countries do not adopt Pillar 2, a rate that high would put U.S. multinationals at a significant disadvantage relative to foreign corporations and reinforce incentives to shift profits out of the U.S. Even if Pillar 2 is widely implemented, U.S. firms would face much higher global taxes than foreign competitors and would respond in ways that harm the U.S. tax base.
- The House proposed raising the tax rate on GILTI to between 16.6 and 17.4 percent. In the absence of Pillar 2, rates that high would put U.S. multinationals at a competitive disadvantage and lead to erosion of the tax base. However, if Pillar 2 is adopted and all multinationals are subject to a minimum rate of at least 15 percent, the resulting tax rate differential of around 2 percentage points would not meaningfully disadvantage U.S. firms and there would not be a strong incentive to shift income out of the U.S. tax system.

Minimum Tax Revenue and the Response of Tax Havens

The [concentration of global profits](#) in low-taxed foreign affiliates of major corporations – generally on Caribbean Islands or in small European Union member states – is the result of a decades-long competition among countries to attract the mobile profits of multinational enterprises by offering tax benefits.³ Under Pillar 2, the home countries of multinational enterprises would offset these benefits, imposing additional tax until the overall rate reaches 15 percent regardless of the tax rate levied by a tax haven. The difference between the haven tax rate and the minimum rate – which currently accrues to businesses as higher after-tax profits – would be captured by the home countries as minimum tax revenue.

PWBM has estimated that, relative to current law, assuming no change by other countries:

- If the U.S. [conformed GILTI to the Pillar 2 proposal](#), its minimum tax revenue would rise by \$140 billion over the 2022-2031 budget window.
- If the U.S. adopted the House proposal for GILTI, its minimum tax revenue would rise by more than \$200 billion over the 2022-2031 budget window.
- If the U.S. adopted the administration proposal for GILTI, its minimum tax revenue would rise by more than \$600 billion over the 2022-2031 budget window.⁴

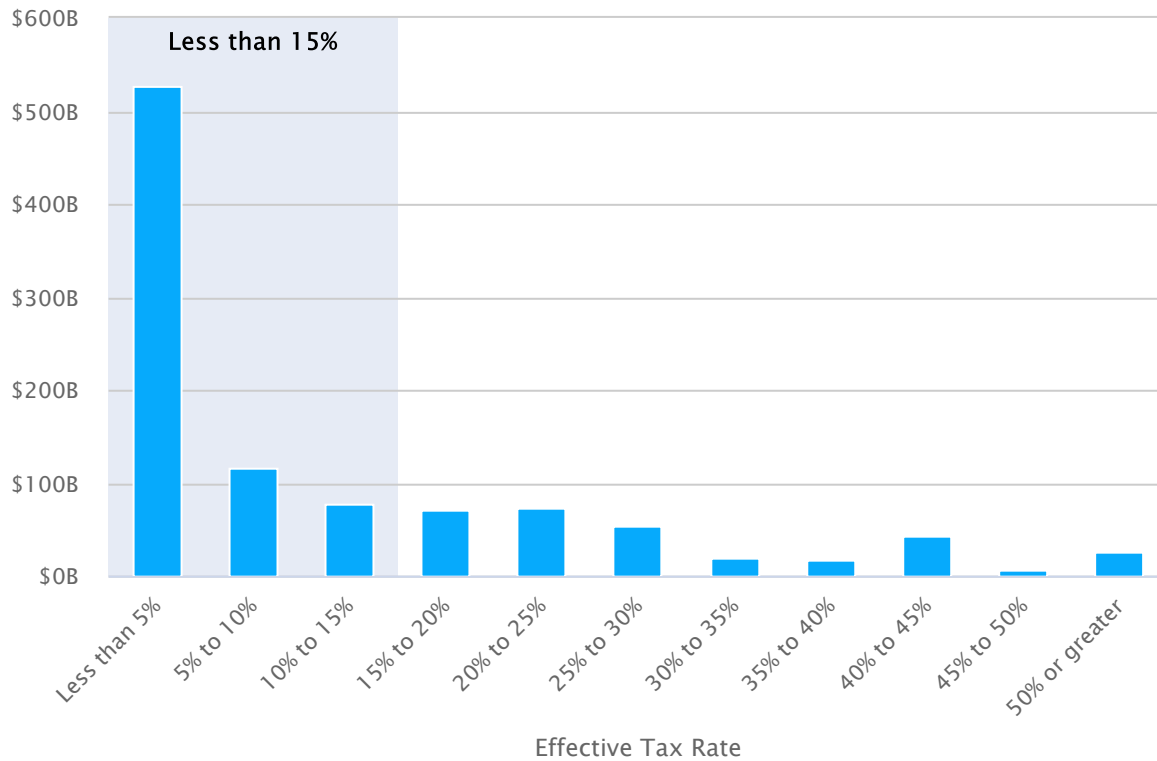
Consistent with conventional practice for revenue estimates, PWBM generally does not forecast policy changes by foreign governments. PWBM's revenue estimates, therefore, reflect other countries' current tax treatment of U.S. multinationals. But tax policy abroad often responds to changes in U.S. policy or the global tax environment, and it is likely that widespread adoption of Pillar 2 would lead low-tax countries to adjust policy in ways that reduce U.S. revenues. PWBM estimates that these responses could cost the U.S. as much as 50 percent of its minimum tax revenue.

If Pillar 2 were implemented globally, a business with mobile income would, in principle, be neutral as to whether the income is reported in a tax haven or in any other country with a tax rate of 15 percent or less. Countries that attracted "paper" profits solely for tax planning purposes would then see that income leave. In practice, many existing profit shifting arrangements would likely remain in place for several years at least, either because they involve real investments in haven countries that are costly to relocate or because tax havens provide advantages beyond the low-income tax rates targeted by Pillar 2.

Under these circumstances, a tax haven that leaves its tax rate on foreign affiliates below 15 percent would effectively be subsidizing the revenues of multinationals' home countries (such as the U.S.) while deriving none of the benefits of its low tax rate. Raising its tax rate on foreign affiliates up to 15 percent would not affect multinationals' overall tax burden or incentives to shift profits; the increased taxes paid to the haven country would be offset one-for-one by reductions in minimum taxes paid to their home countries.

Figure 1. Foreign Income of U.S. Multinationals by Effective Tax Rate of Foreign Affiliate, 2018

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Source: PWBM based on IRS *Statistics of Income* data from Form 9975, Country-by-Country Report.

Figure 1 shows that the vast majority of U.S. businesses’ foreign affiliate income is taxed at a foreign effective rate below 15 percent. If these tax rates rise, the costs to the U.S. in terms of minimum tax revenue could be significant. PWBM estimates that U.S. multinationals paid \$21 billion in minimum taxes on GILTI in 2018.⁵ Modifying GILTI to align more closely with Pillar 2 would raise additional revenue – around \$14 billion more per year under full conformity and \$20 billion more under the House proposal – but would also increase the amount of revenue lost if tax havens raise their rates.

The extent to which foreign countries would respond to the new global regime by increasing tax rates is highly uncertain. To assess the likely impact on U.S. revenues, PWBM considered several scenarios for both the U.S. minimum tax rate (ranging from 15 percent to 21 percent) and the responsiveness of policy in low-tax countries. These scenarios assume that low-tax countries would try to reclaim some revenue while maintaining a tax rate advantage. Based on these scenarios, PWBM estimates that U.S. revenue from the minimum tax could be as low as 50 percent of what it would be if low-tax countries retained their current tax rates. The minimum tax would still raise substantial revenue, but this analysis highlights the considerable uncertainty around conventional revenue estimates when U.S. tax policy interacts with foreign tax policy.

Tax Competition Under a Global Minimum Tax

Global implementation of the Pillar 2 agreement would largely end profit shifting to low-tax foreign affiliates – the dominant form of international tax avoidance in recent decades – but tax competition between countries would continue in other forms. The global minimum tax does not apply to income of multinationals reported in their home jurisdiction. In principle, U.S. multinationals could retain most of the advantages of tax havens by inverting their ownership structures and transitioning from being U.S. corporations (with small U.S. profits and large profits in low-taxed foreign affiliates) to foreign corporations (with large “domestic” profits in a tax haven and small profits in a now-foreign U.S. affiliate). Countries can also compete on taxes not covered by Pillar 2, which includes payroll, property, and environmental taxes, or through permissive business regulation.

These forms of tax competition are less potent and direct than low-income tax rates, but the experience of recent decades suggests that multinationals will exploit any tax differential if it is sufficiently large. Countries seeking to attract the mobile profits of multinationals in a post-Pillar 2 environment would have several tools at their disposal with which to create large differentials. In particular, [intellectual property \(IP\) regimes](#) that provide preferential tax rates for income from mobile assets like patents and software would remain and likely expand following implementation of Pillar 2. Even without an inversion, multinationals with foreign income in high-tax countries that also offer reduced rates under an IP regime could blend the high- and low-tax income to avoid minimum tax liability on shifted profits from intangibles. Other tools such as cost-sharing agreements can achieve similar outcomes.

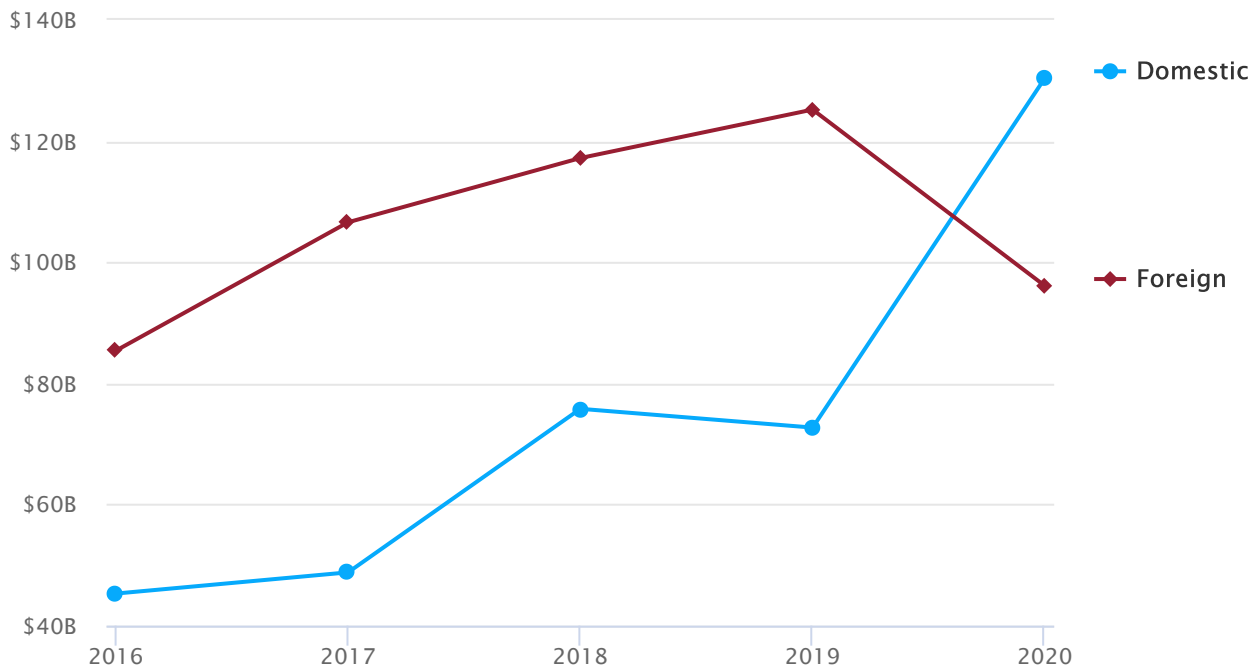
Highlighting the importance of income from intangibles for minimum tax regimes, PWBM estimates that almost \$16 of the \$21 billion in U.S. taxes on GILTI in 2018 was paid by corporations in the information and manufacturing sectors alone, industries where much of the value is generated by high-return and highly mobile intangible assets. Raising the tax burden on this income too far above what it can achieve elsewhere risks pushing it out of the U.S. tax system altogether.

Yet the response of U.S. multinationals to the implementation of GILTI and other tax changes in 2018 suggests that U.S. policymakers have tools to ensure that multinationals adjust to the new global environment by repatriating mobile profits rather than by pursuing new and more aggressive tax avoidance strategies. U.S. adoption of the GILTI regime was paired with a reduction in the U.S. statutory corporate tax rate from 35 to 21 percent and the creation of a U.S. IP regime in the form of the deduction for Foreign-Derived Intangible Income (FDII).⁶ PWBM and [others](#) have shown that U.S. multinationals substantially increased the share of their worldwide income reported in the U.S. after 2018, particularly in sectors with substantial intangible income. The combination of a higher tax rate on foreign income and lower domestic tax rates appears to have succeeded in bringing at least some mobile profits back to the U.S.

The mechanics of this shift are illustrated through the tax rates paid by five of the largest U.S. multinational corporations since 2016. These five were selected because they were reported as engaging in substantial profit shifting before 2018 and because they included detailed tax rate information in their annual financial statements.⁷ Figure 2 plots the total domestic and foreign pretax income reported by the five companies. In the years leading up to 2018, foreign income grew about twice as fast as domestic income. Between 2017 and 2020, domestic income rose sharply, exceeding foreign income in 2020 for the first time in at least a decade. This increase was linked explicitly to the repatriation of intangible assets in some of the companies’ financial statements.

Figure 2. Total Pretax Income of Five Major U.S. Multinationals

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Source: PWBM based on annual Form 10-K filings from Apple, Microsoft, Alphabet (Google), Facebook, and Intel.

Table 1 shows how the effective tax rate paid by the five companies responded to the changes in tax policy in 2018 and the subsequent rise in domestic income.

- Row 1 shows the statutory corporate tax rate, which fell from 35 to 21 percent.
- Row 2 shows the tax benefit the corporations obtained by shifting profits to low-tax foreign countries. Before 2018, this benefit amounted to a 12-percentage point reduction in their tax rate. It fell in half in 2018, due largely to the imposition of the minimum tax on GILTI and also to the rising domestic share of income. It then fell in half again in 2020, to just 3 percent points, as the companies sharply reduced their foreign income and increased their domestic income.
- Row 3 shows the impact of the FDII deduction. Since its introduction in 2018, the tax benefits obtained through FDII have grown rapidly, amounting to a 2-percentage point reduction in the tax rate. The FDII benefit likely played a role in the decision to repatriate intangible assets.
- Row 4 shows the tax savings attributable to the federal tax credit for research and development. These also rose beginning in 2018, probably reflecting the shifts in intangible assets and related activities.
- Row 5 shows the impact of temporary elements of the tax changes in 2018, which consists mainly of the one-time transition tax on accumulated foreign earnings.

Row 6 combines all other factors affecting the five corporations' final tax liability, and row 7 shows the final effective tax rate.

Table 1. Reconciliation of Statutory and Effective Tax Rates for Five Major U.S. Multinationals

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		2016	2017	2018	2019	2020
1	Federal statutory rate	35.0	35.0	23.1	21.0	21.0
2	Foreign earnings taxed at lower rates	-11.8	-12.3	-5.9	-4.5	-2.8
3	Foreign-derived intangible income deduction	0.0	0.0	-0.8	-1.1	-1.8
4	Research and development credit	-1.1	-1.2	-1.6	-1.5	-1.6
5	Impact of the Tax Cuts and Jobs Act	0.0	14.8	7.4	-0.1	0.0
6	Other	-1.4	-2.6	-0.7	1.6	0.3
7	Effective tax rate	20.7	33.6	21.5	15.5	15.2

Source: PWBM based on annual Form 10-K filings from Apple, Microsoft, Alphabet (Google), Facebook, and Intel.

Note: Years reflect each corporation's fiscal year, which in some cases differs from the calendar year. All values are simple averages of the five corporations.

What motivated these corporations to repatriate intangible assets and income between 2018 and 2020? The biggest factor by far was the 14-percentage point reduction in the statutory rate, which on its own provided a tax benefit for domestic income worth more than shifting tens of billions in income to low-tax countries before 2018. The introduction of the GILTI regime also meaningfully and sharply limited the rewards to such profit shifting, though these companies still derived a significant benefit in 2020 from the low minimum tax rate on GILTI. While the overall impact of FDII remains moderate, it has grown rapidly since 2018 and appears to have been effective at targeting incentives for repatriation to the most mobile intangibles.

The example of these five companies illustrates how a combination of minimum tax rates on foreign income and low domestic tax rates can induce profit shifters to bring mobile income back to the U.S., boosting the U.S. tax base rather than eroding it. Movement in the United States and globally towards a more comprehensive minimum tax on foreign profits presents an opportunity to recapture more of the income that has flowed to tax havens over decades. But it does not spell the end of international tax competition, and how much of that income ends up in the U.S. will depend as much on the domestic tax environment as on the global.

This analysis was conducted by [Alex Arnon](#). Prepared for the website by [Mariko Paulson](#).

1. Daniel Bunn of the Tax Foundation provides a [good overview](#) of the full agreement. [↩](#)

2. GILTI is currently taxed at rates between 10.5 and 13.125 percent (depending on the foreign tax rate paid). These rates are scheduled to rise to between 13.125 and 16.4 percent beginning in 2026.

Under GILTI, income and tax credits are determined on a worldwide (or aggregate) basis, treating a multinational's global operations as a single consolidated entity. Under Pillar 2, income and tax credits are determined on a country-by-country basis, treating a multinational's operations in each country as distinct entities. ↩

3. For small or even medium-sized economies, becoming the nominal home to a share of the vast profits of major multinationals can generate significant revenue even with a very low tax rate. Moreover, profit shifting arrangements often lead to at least some real investment. Though small relative to the scale of global corporations, these investments can be an important source of employment and business activity for host countries. ↩

4. PWBM [previously estimated](#) that the administration proposal would raise more than \$700 billion. The estimate has been revised down primarily due to data updates, and to lesser extent model improvements. ↩

5. PWBM's estimate of taxes on GILTI involves some uncertainty, largely due to a lack of data on utilization of foreign tax credits against GILTI liability. PWBM therefore estimates a range for taxes on GILTI of \$18 to \$24 billion in 2018, with a central estimate of \$21 billion. ↩

6. FDII differs from most other IP regimes in that it applies to a broader range of income but provides a smaller reduction in the tax rate. ↩

7. The five multinationals are Apple, Microsoft, Alphabet (Google), Facebook, and Intel. ↩