Formulating the International Tax Debate: Where Does Formulary Apportionment Fit?

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Document Type
Book Chapter

Publication Date
2020

Abstract

As the contributions in this volume are being written, the Inclusive Framework nations, a group drawn together by the Organisation for Economic Co-operation and Development (OECD) as part of its Base Erosion and Profit Shifting (BEPS) project, are in the midst of a consultation process intended to revise the international corporate tax profit allocation and nexus rules. At the end of May 2019, the OECD released its *Programme of Work to Develop a Consensus Solution to the Tax Challenges Arising from the Digitalisation of the Economy*. At the beginning of June 2019, this Programme was endorsed by the G20 Finance Ministers during their ministerial meeting in Fukuoka, Japan.

To use the OECD's terminology, the proposals under consideration to revise the current nexus and profit allocation rules would create a 'new taxing right' to be allocated to the 'market jurisdiction'. The Programme of Work describes certain technical issues that must be considered when making such fundamental changes to the international tax architecture.

The OECD's work on these major revisions to international tax norms is being undertaken under the auspices of the Inclusive Framework. The Inclusive Framework arose out of a G20 request that the OECD create a body in which all interested countries – regardless of G20 or OECD membership – could participate in the BEPS project on an equal footing. The subsequently developed Inclusive Framework allows interested countries to work with the OECD/G20 on developing standards on BEPS-related issues. As of this writing, over 125 countries have joined the Inclusive Framework and committed to implementing the comprehensive BEPS package. It was clear from the outset that the Inclusive Framework could be used as a stand-in for a world tax organization. In the current OECD project on profit allocation, it is in effect being used in that manner for the first time.

The Inclusive Framework is not currently considering a full move to formulary apportionment, as that term is understood in this volume. Yet evaluation of the proposals under consideration by the Inclusive Framework suggests that each and every one can be improved by reappraising formulary apportionment. Accordingly, the purpose of this chapter is to highlight the relationships between the options under consideration in the current OECD-led process and 'formulary apportionment', as that term is used elsewhere in this volume.

Section 11.02 of the chapter briefly offers some background on the major developments – arguably, tectonic shifts – of the last few years in the international tax arena. Section 11.03 describes the proposals for revising the profit allocation rules that are currently under consideration by the Inclusive Framework. Section 11.04 fleshes out 'straw men' that develop these ideas in greater detail, with the purpose of highlighting that the proposals that are under consideration by the Inclusive Framework at the time of this writing are partially formulary approaches and that lessons from formulary apportionment likely carry over to any partially formulary system that may be developed multilaterally in the future.

Publication Citation

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