

International Tax Reform and Its Effect on Digital Sovereignty

By Jan Winterhalter and Nupur Jalan¹

The OECD's Pillar Two solution is designed to ensure Global Minimum Taxation through a set of interlocking rules. It has been widely criticized for its impact on a country's sovereignty. While the focus of Pillar Two may be to combat profit shifting and tax competition, it does have wider implications on the notion of the digital sovereignty of a country.

1. BACKGROUND — SETTING THE SCENE

1.1 Digital Sovereignty and the Ongoing Discussions Surrounding It

The term “digital sovereignty” has multiple definitions, including the ability of individuals, states, and businesses to control various elements of digital technology.² Digital sovereignty has also been defined as the “control of our present and destiny as manifested and guided by the use of technology and computer networks,”³ Although the definition is somewhat broad, the term combines two subject areas —the *digital realm* and *sovereignty*.⁴

This quest for digital sovereignty is, therefore, a goal shared by companies, public authority stakeholders and, more recently, internet users, citizens, and consumers. Thus, Digital sovereignty is also about the political autonomy for everyone and is not just the question of competitiveness or innovativeness.⁵

The discussions about “digital sovereignty” is held in both politics and academia and thus are influenced by different disciplines, methodologies, and interest. The discussions can generally be structured and identified in two different ways:

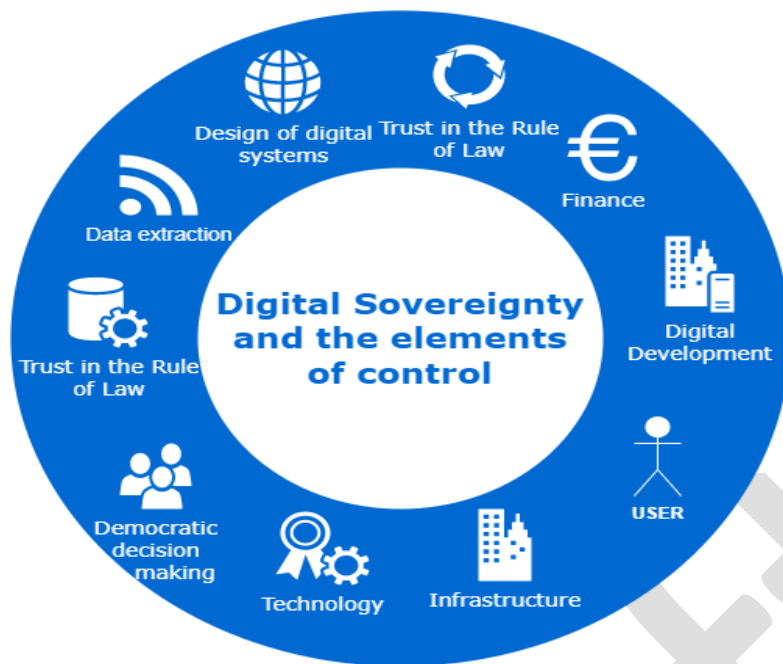
¹ Mr. Winterhalter is a tax lawyer and PhD candidate at the Institute of Tax Law of Leipzig and a research fellow of the Heinrich Böll Foundation. He can be reached at jan.winterhalter@posteo.de. Ms. Jalan is tax professional specializing in corporate tax, international tax and transfer pricing and an interdisciplinary researcher. She can be reached at jalannupur@outlook.com.

² For Moerel and Timmers, digital sovereignty is even not limited to the control of a state over the use and design of critical digital systems and the data generated and stored therein, but also concerns the broader scope of economy (control over essential economic ecosystems) and society and democracy (trust in the rule of law and quality of democratic decision-making); see Lokke Moerel and Paul Timmers. *Reflections on Digital Sovereignty*, Soc. Sci. Res. Network (Jan. 2021). <<https://papers.ssrn.com/abstract=3772777>>

³ Pierre Bellanger, *De la souveraineté en général et de la souveraineté numérique en particulier*, Les Échos, 30 Aug. 2011.

⁴ Deborah Elms, *Digital Sovereignty: Protectionism or Autonomy?* Hinrich Found. Rpt. (Sept. 2021) <<https://static1.squarespace.com/static/5393d501e4b0643446abd228/t/615f394c5533a623afeac00b/1633630545286/Digital+sovereignty+protectionism+or+autonomy+-+Hinrich+Foundation+-+Deborah+Elms+-+September+2021.pdf>>

⁵ Henning Kagermann, Karl-Heinz Streibich, and Katrin Suder, *Digital Sovereignty: Status Quo and Perspectives* (2021).



- Human-centered autonomy, i.e., each individual has sovereignty over their data, and
- State-centered autonomy, i.e., each state has an undisputed power monopoly within its borders⁶ — physically and virtually.

For this article, we have concentrated on the second perspective, i.e., digital sovereignty is the notion of states worldwide, where sovereignty is their exercise of power over a defined geographical area and the population therein. This approach can be best understood by looking at the European Union

(EU) example in the next section.

1.2 The EU and Its Aspiration of Technological Sovereignty as an Essential Path in Protecting European Autonomy in the Digital World and Beyond

Over time, there has been a range of innovations in exploring new technologies, artificial intelligence (AI), and the internet of things (IoT), etc. From the European perspective, the influence of non-EU tech companies has become a concern for EU policymakers, especially concerning their impact on the EU's data economy, innovation potential, privacy and data protection, and the establishment of a secure and safe digital environment.⁷ Therefore, the European Council has stressed that the EU needs to go farther in developing a competitive, secure, inclusive, and ethical digital economy with world-class connectivity and has called for special emphasis to be placed on data security and AI issues.

A range of initiatives have been proposed or are under discussion at the EU level to accelerate the digitalization process and enhance Europe's strategic autonomy in the digital field around three building blocks of (1) building a data framework; (2) promoting a trustworthy environment, and (3) adapting competition and regulatory rules, for example:

- the European proposals for a European cloud infrastructure;
- the EU Network and Information Security Directive; and
- the EU regulation on electronic identification and trust services for electronic transactions, which includes recognizing the electronic means of authenticating citizens.⁸

Policy designed to enhance the bloc's digital strategic autonomy, has already progressed, for example:

- the Digital Markets Act, “ensuring fair and open digital markets”;⁹

6. Henning Kagermann, Karl-Heinz Streibich, and Katrin Suder, *Digital Sovereignty: Status Quo and Perspectives* (2021).

⁷ Madiaga Tambiama, *Digital Sovereignty for Europe*, Eur. Parl. Res. Serv. (2020); Lokke Moerel and Paul Timmers. *Reflections on Digital Sovereignty*, Soc. Sci. Res. Network (Jan. 2021).<<https://papers.ssrn.com/abstract=3772777>>

⁸ Lokke Moerel and Paul Timmers. *Reflections on Digital Sovereignty*, Soc. Sci. Res. Network (Jan. 2021).<<https://papers.ssrn.com/abstract=3772777>>

⁹ *The Digital Markets Act: ensuring fair and open digital markets*, European Commission.<https://ec.europa.eu/info/strategy/priorities-2019-2024/europe-fit-digital-age/digital-markets-act-ensuring-fair-and-open-digital-markets_en>

- the Digital Services Act, “ensuring a safe and accountable online environment”; and
- the Data Governance Act (DGA), enabling companies to reuse public sector data such as health or environmental data in a manner consistent with privacy and intellectual property rules.¹⁰

European regulators are increasingly aware that data is essential in transformative technologies such as AI and seek to establish global standard-setting rules to govern how and from where data can be gathered and used. A prominent example in this direction is the success of the General Data Protection Rules (GDPR), which also aims to indirectly retain sovereignty over data and make EU citizens more aware of their rights and protections for the use of their data.¹¹ Also, the GAIA-X Initiative, which develops a software federation system that can connect several cloud service providers and data owners together that would give users sovereignty over their data, demonstrates that the EU sees technological sovereignty as essential in protecting European autonomy in the digital world and beyond. Similarly, many regions/countries in other parts of the world are taking some other measures to retain their digital sovereignty.

These regulatory measures within the realm of data protection, data localization, or competition law can be easily linked with the digital sovereignty. But we strongly argue that the concept of tax sovereignty also has an essential impact on the notion of digital sovereignty.

From tax perspective, it appears that while Governments are trying to gain sovereignty in all dimensions but are ready to give up their tax sovereignty in the name of tax cooperation under OECD's Pillar solution. Needless to say, the taxation of the digital economy is also an integral part of the regulation of the digital space and cannot be overlooked from the digital sovereignty perspective.

1.3 Tax Regulation as an Integral and Necessary Requirement for Digital Sovereignty

So, what has digital sovereignty to do with tax sovereignty?

In literal sense, tax sovereignty usually entails the autonomous power of the state to levy taxes. In times of Globalization and linked trade (digitally and physically) it might not surprise that within the international tax system we have several kinds of measures (e.g., for mitigating or eliminating international double taxation and stimulating international trade): some of them are unilateral and driven by each nation's sovereign (e.g., the parliament), the others are bilateral, and still others are multilateral, driven by multilateral organizations like the OECD, G20, EU, or UN¹². But let's ask the question: why do we have all these measures, and not, for instance, only unilateral measures?

This shows that countries were never entirely tax sovereign (for example, countries give up tax sovereignty when they agree to abide by certain practices or to tax or not tax certain items per a tax treaty signed with a partnering country). But historically, bilateralism has been the constant trend of tax treaties¹³. Multilateralism and the resulting cooperation has been mainly in administrative and technical (information exchange, administrative assistance, etc.) rather than substantive. But with the OECD/G20 BEPS project, the current international tax landscape is facing challenges and changes unprecedented for the past several decades, with those actors intending to enhance cooperation and multilateralism to cope with the challenges, while over one 137 countries are locked in a complex negotiation to decide how states should divide the entitlement to tax income from cross-border economic activities.

¹⁰ Frances Burwell et al., *Will Europe Become a True Digital Power*, *The Nat'l Interest* (Jan. 21, 2022). <<https://nationalinterest.org/feature/will-europe-become-true-digital-power-199690>>

¹¹ Alex Scroton, *EU Judges GDPR an Overall Success, but Changes Still Needed*, *TechTarget* (Jan. 24, 2020). <<https://www.computerweekly.com/news/252485105/EU-judges-GDPR-an-overall-success-but-changes-still-needed>>

¹² Keigo Fuchi, *Unilateralism, Bilateralism, and Multilateralism in International Taxation*, 59 *Japanese Yearbook of International Law* 216–228 (2016)

¹³ A New Age of Multilateralism in International Taxation?, <https://papers.ssrn.com/abstract=2733964> (last visited Jun 24, 2022)

But what does this result of “multilateralism” mean for the question of tax sovereignty? Are states now willing to cooperate on taxes, as Quentin suggests, in many ways, including to submit to supranational sovereignty like the OECD?¹⁴

It is pertinent to note right tax system could help meet the fiscal requirement of an adequate regulation/subvention of a country’s own digital industry. Rightly stated, “The ability to control tax policy enables a State to meet its functional duties (revenue raising and fiscal policy design) and support its two important democratic norms — democratic accountability and democratic legitimacy.”¹⁵ But if we focus on the question of digital sovereignty, we argue that not being able to control taxation mechanisms fully, not being able to independently ease competition, or build up its own digital industry, might be a heavy barrier to achieving a true digital strategy and sovereignty¹⁶.

In the following section, we lay down why we think tax sovereignty is an integral requirement of digital sovereignty, and we therefore analyze how the ongoing Pillar solution will affect digital sovereignty of nations around the world.

2. TAXATION OF THE DIGITAL ECONOMY AND ITS EFFECTS ON DIGITAL SOVEREIGNTY

2.1 Taxation of the Digital Economy

The fight against Base Erosion and Profit Shifting (BEPS) was said to be important because BEPS opportunities not only threatened the integrity of the corporate income tax by creating unintended competitive advantages and distorting investment decisions but, most importantly, also damaged voluntary tax compliance systems for all taxpayers, including individuals.¹⁷ These concerns have been intensified by the potentially large amounts of global profits being earned by emerging digital e-commerce businesses with enormous sales and a vast customer base without corresponding revenue gains for market jurisdictions.¹⁸

Therefore, International tax reform has been a topic of discussion in government institutions, industry, and academia worldwide over the last few years.¹⁹ The taxation of digital transactions has raised a lot of controversies (mainly because the digital economy systematically disconnects place of business from place of consumption), which are onerous to solve. The discussion revolves around how international taxation can be reformed to provide a reasonable and stable system in the 21st century.

Now, for the first time, such reform is becoming a reality as more than 137 countries have reached an agreement on the implementation of Pillar One and Pillar Two. Pillar One deals with the international allocation of taxing rights and aims at shifting some profits from multinational enterprises’ (MNEs’) resident jurisdictions to the market jurisdictions.²⁰ Pillar Two, the Global anti-Base Erosion (GloBE)

¹⁴ David Quentin, What Is Tax Sovereignty For? SMART (May 11, 2017).<<https://www.smart.uio.no/news/what-is-tax-sovereignty-for.html>>

¹⁵ Kuldeep Sharma, *The Tax Sovereignty Principle and Its Peaceful Coexistence with Article 12B of the UN Model Tax Convention*, The South Centre, Tax Cooperation Policy Brief (2021).<<https://www.southcentre.int/tax-cooperation-policy-brief-14-june-2021/>>

¹⁶ Madiega Tambiama, Digital Sovereignty for Europe, Eur. Parl. Res. Serv. (2020)

¹⁷ João Félix Pinto Nogueira et al., *The OECD Public Consultation Document ‘Global Anti-Base Erosion (GloBE) Proposal — Pillar Two’: An Assessment* (2019).<<https://papers.ssrn.com/abstract=3644238>>

¹⁸ Nupur Jalan and Jan Winterhalter, *Analysing Value Creation and the Value Chain of Data Businesses*, 4 Int’l Tax Studies 2 (2021).

¹⁹ For an overview, see *id.*; Regarding the U.S. tax reform, see Hannelore Niesten, *Unravelling the Recent U.S. Tax Reform: A Paradigm Shift in the International and EU Tax Landscape*, 58 Euro. Tax’n (2018); Antonio Martinez, *The U.S. Tax Reforms and the WTO*, Working Paper do Boletim Ciências Económicas 52 (2019).

²⁰ Itai Grinberg, *User Participation in Value Creation*, British Tax Rev. 407–420, 1 (2018); Michael Lennard, *Act of Creation: The OECD/G20 Test of ‘Value Creation’ as a Basis for Taxing Rights and Its Relevance to Developing Countries*, 25 Transnat’l Corps. 55–84 (2018); Christians Allison, *Taxing According to Value Creation*, 90 Tax Notes 1379–1383 (2019); Marcel Olbert and Christoph Spengel, *Taxation in the Digital Economy — Recent Policy Developments and the Question of Value Creation*, ZEW — Centre for European Economic Research Discussion Paper (2019); Hartmut Förster, Stefan Greil, and Arnim Hilse, *Taxing the Digital Economy — The OECD Secretariat’s New Transfer Pricing A-B-C and Alternative Courses of Action* (2019);<<https://papers.ssrn.com/abstract=3484919>> Jan Winterhalter and Andreas Niekler, *How to Tax Data in the Context of International Taxation, Part 1*, Kluwer Int’l Tax Blog (2020).<http://kluwertaxblog.com/2020/08/13/how-to-tax-data-in-the-context-of-international-taxation-part-1/?doing_wp_cron=1598441452.7549939155578613281250>

rules, pertains to the adoption of a global minimum corporate income tax for multinationals.²¹ The way these Pillar solutions have come up reflects that they deal not just with digital taxation.

The OECD has stated that the “main purpose of international tax cooperation was to end the undesirable proliferation of unilateral taxes — a ‘race to the top’ in which small, open economies hastened to impose taxes on foreign multinationals.”²² The problem here with the reform might be that it could prove unfavorable to the EU — or any other country without a strong exporting digital economy — in the long term.

The African Tax Administration Forum (ATAF), having stated in the past that it is extremely challenging for many developing countries to fully participate in the Inclusive Framework process and to ensure that the new rules are the right fit for African countries, is now concerned that the complexities in this proposal may result in some countries committing to new rules without a complete understanding of the revenue and investment implications for them.²³ Accordingly, the United Nations Conference on Trade and Development states that “investment policymakers urgently need to review their incentives packages, for both existing and new investors. Some fiscal policy options to promote investment remain, including amplifying the benefit to investors of the so-called substance-based carve-out; shifting to incentives that are less affected by Pillar II; or reducing taxes that are not covered by Pillar II, to the extent that they have a bearing on investment decisions.”²⁴

Even if global minimum taxation is going to reduce international tax competition, no explanation has been offered for how it will strengthen residence country taxation that requires international cooperation or how ending tax competition will yield cooperative gains for all countries.²⁵ Overall, addressing the international tax competition is pertinent, but it cannot deprive states of their legitimate right to exercise their taxing powers for policy and regulatory purposes if no harmful practices and real abuse by taxpayers are at stake.²⁶

But if the corporate income tax rate is globally standardized, then the natural income rates might be lowered in a race to the bottom, accelerated by new working behaviors and the incentive of states to attract highly skilled workforce with additional benefits, possibly leading to a loss in taxing rights and substance — above all, in developed states with high natural income rates or, again, by tax havens such as Dubai. The countermove of nations (above all within the EU) might then be to attract MNEs with research and development (R&D) incentives, e.g., in the form of patent boxes. Further, with no carve-outs for tax incentives, Pillar Two would impact the tax incentives granted by the developing countries.²⁷

Additionally, while there could be the right momentum for the introduction of a Global Minimum Tax, a reform addressing the challenges of taxing the digital economy and leading to tangible improvements like a comprehensive Pillar One solution could get lost in the whirlpool of events. On the other hand, the interlocking rules in Pillar Two are too complex to understand.

But what happens if this appeasement policy prevents further discussion on several other areas of digital and data taxation not covered by the proposals and has indirect implications on other regulations, such as the proper valuation of highly valuable intangibles?²⁸ Will the Pillar solution cause

²¹ Michael P. Devereux, *Made in America Tax Reform?* Oxford Univ. Centre for Bus. (4 May 2021). <https://oxfordtax.sbs.ox.ac.uk/article/made-in-america?dm_i=17AR,7CUYA,4BCPZN,TUWNI,1>

²² Wei Cui, *What Does China Want From International Tax Reform?* 103 *Tax Notes Int'l* 141–151, 141 (2021).

²³ ATAF, Media Statement on the Outcomes of the Inclusive Framework Meeting 29 to 30 January 2020. <<https://www.ataftax.org/media-brief-inclusive-framework-jan-2020>>

²⁴ James Zhan et al., *World Investment Report 2022 - International Tax Reforms and Sustainable Investments* (Unctad) XV (2022).

²⁵ Wei Cui, *New Puzzles in International Tax Agreements* 1 (2021). <<https://papers.ssrn.com/abstract=3877854>>

²⁶ Belisa Ferreira Liotti, *Limits of International Cooperation: The Concept of ‘Jurisdiction Not to Tax’ from the BEPS Project to GloBE*, 76 *Bull. for Int'l Tax'n* 63 (Feb. 2022), IBFD.

²⁷ Pasquale Pistone et al., *The OECD Public Consultation Document ‘Global Anti-Base Erosion (GloBE) Proposal — Pillar Two’: An Assessment*, 74(2) *Bull. for Int'l Tax'n* (2019).

²⁸ See Dan Ciuriak and Eurallyah Akinyi, *Taxing Capital in the Age of Intangibles* (Social Science Research Network) (2021), <<https://papers.ssrn.com/abstract=3920763> (last visited Apr 1, 2022)

countries to refrain from setting their agenda besides the narrow focus on the *tax reform of the century*?

2.2 The Negative Effects on the Digital Sovereignty Debate

To answer those questions, we have laid down the negative effects of these Pillar solution on the digital sovereignty debate.

First, there is the *resource* problem: Implementing new rules accompanied by a comprehensive technical commentary shall raise challenges from countries and MNEs worldwide, allowing to anticipate that there might be much attention and resources already gone in finding the appropriate mechanics of implementing these proposals.

Secondly, there is the *scapegoat* problem: Arguing against the narrative of a “harmful tax practice” from “renegade tax haven states” might appear to breach the consensual and righteous code of conduct.²⁹ Even if countries want to implement a Global Minimum Tax and have time and money left to fight for shaping their digital agenda, this debate can be silenced and immobilized with reference to the reform process and success already done (as mentioned earlier). Suppose they renounce their exclusive right to tax but get reasonable compensation in the form of Pillar One instead. In that case, this form of international consensus or law might not result in a loss of sovereignty, as a *do-ut-de*³⁰ mechanism is crucial for international relations and the success of reform is based on the goodwill of a substantial part of the worldwide community.

Thirdly, there is the *support your own digital troops* problem: If we take this thought about sovereignty one step further, where antitrust and competition issues persist— and which are not going to disappear in the digital world — might be hardly addressed.³¹ Additionally, a government’s support for its own digital economy through tax incentives regarding R&D or other exemptions might appear as a circumvention of the minimum tax rate. Even new data protection rules requiring some data localization in the respective jurisdiction could be seen as aimed at weakening the U.S. and Chinese digital economy sectors, again breaching the fragile multilateral and desirable consensus in a world of crisis, potentially restarting the blame game.

The following might even be a heavy barrier to achieving a true digital strategy:³² To grow (for example) European digital eco-systems and companies, the EU needs legislative and political tools to ensure that its member countries become less dependent on non-European providers — but if the ongoing under taxation of US- and Chinese-resident digital MNEs prevails and legislative action is restricted in scope, then the loss of control over (European) data and regulation of their digital environment might be a counter push against digital sovereignty and a values-based approach to global digital cooperation. Additionally, the digital transformation is presenting new challenges for the tax system already, but in the not-too-distant future, the growing space industry/metaverse, etc., and the problem of how to tax these most immobile versions of the digital economy will accelerate, requiring many political instruments to effectively address and regulate it with cross reference to other regulatory areas such as competition or environmental law.

And, even if the Global Minimum Tax is arguably desirable from a general point of view, it will lead to a trade-off between tax competition and taxing the digital economy according to where the value is created. When talking about taxation of the digital economy, we always have to consider its effects on digital sovereignty.

²⁹ See Lorraine Eden and Robert Kudrle, *Tax Havens: Renegade States in the International Tax Regime?* 27 Law & Policy 100–127 (2005).

³⁰ “I give that you might give” (Latin).

³¹ Of course, one could argue that competition is not in the telos of taxes. But despite the principle that taxation must be neutral, a non- or under-taxation of digital data driven MNEs is clearly a breach.

³² Madiega Tambiama, *Digital Sovereignty for Europe*, Eur. Parl. Res. Serv. (2020)

This heavily depends on the different interests at stake. Thus, in the following paragraphs, we have laid down the politics of the involved stakeholders, to explain why we think that the interests at stake are not pointing in “a digital sovereignty for all” direction.

Affected Stakeholders and Their Interest

United States of America

The role of the United States in case of the international taxation dates back to the 1920s when American government started taking a part in the attempt of the League of Nations to develop a model bilateral tax treaty.³³ US politics plays an important role for any policy changes in international tax regime — the ongoing Pillar One and Pillar Two work is testimony to it. Thus, any such policy move is critically dependent on US support and leadership.

Indeed, since the 1960s the broad contours of international tax cooperation have been defined by changing US policy preferences. One US aim has been creation of competitive advantage for US multinationals by making it easier for them to reduce their tax liabilities on foreign activities and foreign profit, leading to trillions of dollars piling up in low taxed jurisdictions, largely untaxed.³⁴

However, the plan would be vulnerable to offshoring if there continued to be a relatively low effective tax rate on foreign income, as US companies would be incentivized to undertake their productive activity elsewhere, moving “American” jobs abroad — hence, the “Made in America” tax plan targets this very possibility.³⁵ But the proposed minimum tax rate potentially creates a competitive disadvantage for US based multinationals relative to their non-US competitors, who may not face such a high tax rate;³⁶ and hence, the solution is clearly to try to persuade the rest of the world to do likewise and therefore have all states introduce minimum tax rates.³⁷

Accordingly, Yellen stated that “the current international tax system has eroded national sovereignty in ways that have real and measurable impacts on American workers and families,” and that Pillar 2 will aim at “ensuring that countries compete with one another on more positive bases, such as the education and training of the labor force, stability of the legal system, and ability to innovate – areas in which the United States has a comparative advantage.”³⁸

But although there are motivating factors for embarking on business environment reforms, losing the right to tax future technology and data-driven industries is not one of them. This counts even more as the U S government reacts to globalization and the allocation of economic activities from the U.S. to the Chinese government by clearly aiming to build a two-pronged economy: a dynamic, internationally competitive innovation sector and a domestically oriented machine for employment and distributed prosperity, the so-called “Bidenomics.”³⁹

As Gurule and O`Neil argue, the time to pass international tax reforms included in the Build Back Better Act⁴⁰ is now:

[I]f Congress fails to pass these reforms it would be a lose-lose-lose: encouraging continued profit shifting and offshoring of investment and jobs, while yielding no competitive benefit for US MNEs, and potentially contributing to the failure to invest in solutions to some of our

³³ Sol Picciotto, *International Business Taxation: A Study in the Internationalization of Business Regulation* (Electronic ed.: Sol Picciotto 2013). <<https://www.taxjustice.net/cms/upload/pdf/Picciotto%201992%20International%20Business%20Taxation.pdf>>

³⁴ Michael P. Devereux et al., *Taxing Profit in a Digital Economy*, Oxford (1st ed. 2021).

³⁵ *Id.*

³⁶ *Id.*

³⁷ Biden-Harris Fact Sheet, *The Biden-Harris Plan to Fight for Workers by Delivering on Buy America and Make It in America* <<https://joebiden.com/wp-content/uploads/2020/09/Buy-America-fact-sheet.pdf>>

³⁸ Alex Hunter, ed., *Global Minimum Corporate Tax Protects National Sovereignty: Janet Yellen*, TPNews (June 10, 2021). <<https://transferpricingnews.com/global-minimum-corporate-tax-protects-national-sovereignty-janet-yellen/>>

³⁹ Noah Smith, *Bidenomics: Ein neues Paradigma für eine neue Zeit*, Blätter (Mai 2021). <<https://www.blaetter.de/ausgabe/2021/mai/bidenomics-ein-neues-paradigma-fuer-eine-neue-zeit>>

⁴⁰ H.R. 5376, approved by the House Nov. 15, 2021, motion to reconsider laid on the table.

*biggest long-term competitive concerns. In contrast, these reforms can advance the OECD minimum tax agreement and create a more competitive tax environment for U.S. MNEs, deterring the incentive to shift profits and offshore factories and jobs, while funding critical investments toward more sustainable and equitable growth.*⁴¹

Avi-Yonah follows this route of thought, adding that the current U.S. GILTI tax is fatally flawed, as the rate is too low, there still exists tax avoidance incentives, and it creates an incentive to shift real investment and jobs offshore — in stark contrast to the Bidenomics strategy.⁴²

People's Republic of China

Avi-Yonah and Xu argue that the Chinese government has participated in developing and implementing the BEPS project. They expect China to act consistently and coherently, taking whatever measures necessary to guarantee the successful implementation of the BEPS package in collaboration with the global community.⁴³ That might be partly explained by China's desire to ease trade tension and to obtain reciprocal market access in foreign markets, and by its lowered need for protectionist policies.⁴⁴ Nevertheless, the rhetoric of common cause with developing countries is contradicted by actions that maximize China's share of the tax "pie"; and a willingness to court the OECD based on the leverage gained from a flirtation with outside options.⁴⁵

China is also seeking market power within the international domain mirroring the actions of US in the past. As the Chinese government tries to follow this example of a technology-driven export sector, increasingly based on safeguarded IP rights⁴⁶ — best demonstrated by its "Made in China 2025" agenda and expansion of multilateral trade agreements such as its Comprehensive and Progressive Trans-Pacific Partnerships (CPTTP) — it could find political desirability in losing taxation rights on its expanding digital sector in the form of BAT⁴⁷ across the world.

European Union, European Commission, and UK

The EU Commission is trying to solidify the internal market and focus on an innovative export sector. As for an internal market, a uniform tax rate is an obvious advantage. They also want to increase the taxation on the digital economy by getting rid of what they see as an unfair competitive advantage for U.S. and Chinese MNEs.⁴⁸ The EU Commission has been suggesting a European Minimum Tax based on a common consolidated tax base already in the 1990s. However, being part of the global tax reform solution, on December 22, 2021, the European Commission published the proposed directive for implementing Pillar Two in the EU,⁴⁹ although the implementation is expected to be deferred (viz. GloBE applies to fiscal years starting December 31, 2023).⁵⁰

In the past, most EU countries have agreed to implement *global minimum taxes*. Nevertheless, in light of Hungary's veto in the last Ecofin meeting (which has the lowest corporate tax rate of 9% among the

⁴¹ Ryan Gurule and Santiago O'Neil, *Failing to Further the OECD Agreement Would Be a Lose-Lose-Lose*, 106 Tax Notes Int'l 1039–1043.

⁴² Reuven Avi-Yonah, *Why Does the United States Need the Global Minimum Tax?* (2022). <https://media-exp1.licdn.com/dms/document/C4E1FAQH3nynm43FakA/feedshare-document-pdf-analyzed/0/1654859355060?e=1656547200&v=beta&t=8Pi2m1drRAbx7FXw2iTHrsydeGsFW_3TMIqqt8QIOY>

⁴³ Reuven Avi-Yonah and Haiyan Xu, *China and BEPS*, 7 Laws 4 (2018).

⁴⁴ Wei Cui, *What Does China Want From International Tax Reform?* 103 Tax Notes Int'l 141–151, 141 (2021).

⁴⁵ Martin Hearson and Wilson Prichard, *China's Challenge to International Tax Rules and the Implications for Global Economic Governance*, 94 Int'l Affairs 1287–1307 (2018).

⁴⁶ Sven Hilbig, *Alle gegen China?* Blätter (Feb. 2021). This is quite contrary to former accusations that China is stealing technology. <<https://www.blaetter.de/ausgabe/2021/februar/alle-gegen-china>>

⁴⁷ Baidu, Alibaba, and Tencent (big Chinese internet firms).

⁴⁸ European Commission, *Communication from the Commission to the European-Parliament and the Council: Business Taxation for the 21st Century* (2020).

⁴⁹ European Commission, *Proposal for a Council Directive on Ensuring a Global Minimum Level of Taxation for Multinational Groups in the Union*, COM 823 final (Dec. 22, 2021).

⁵⁰ Ireland has announced increase in tax rates to 15% for MNEs meeting €750 million threshold; 12.5% to be retained for MNEs below threshold and is also considering DMT.

EU), one can wonder what the trade-off will be even within the EU must be to reach the unanimity requirement.

Developing Countries

From the perspective of developing countries, even introducing Global Minimum Tax in combination with a Pillar One-like reform appears not too desirable as one-size reform cannot fit all — not even with the extra leeway in the threshold given to developing countries for application of Pillar One. Further, Pillar One would apply only to about 100 companies globally in initial years of implementation. Undoubtedly, developing countries lose substantial revenues every year to corporate tax avoidance, exacerbated by globalization and digitalization.⁵¹ Additionally, analyses show that the convenience of a Global Minimum Tax proposal to foster economic development comes with other costs, as tax incentives might not be per se harmful, and the extra tax revenue for developing countries is either modest or does not exist due to a lack of resident digital MNEs.⁵²

While Hearson et al. argue that developing states might be able to overcome limited market power through socio-technical resources like expertise and professional networks,⁵³ Magalhaes and Ozai are rather skeptical, stating that “technocratic approaches are set to fail less-developed nations for as long as we continue to overlook the background causes of weak taxation at both the national and international levels. These involve difficulties in applying complex rule sets and the way global tax policy is developed, who influences the process, and the resulting distributive consequences.”⁵⁴ Resource and capacity constraints are other challenges often faced by developing country and the implementation of global minimum tax will need ample resources for its proper implementation. Pillar Two (especially QDMT — qualified domestic minimum tax) aims to provide preference to the source state for implementation of minimum tax, but it is yet to be seen how it will evolve in the coming years.

Further, countries need to focus on domestic resource mobilization to meet not only their internal goals only but also sustainable development goals. According to the United Nations: “Improving the taxing rights of lower-income countries also contributes to their ability to mobilize revenue, which is a fundamental requirement to finance the achievement of sustainable development goals.”⁵⁵ Pillar Two solutions could therefore prevent governments from funding their important financial priorities in the future. Accordingly, Liotti states that “Jurisdiction not to tax should not be undermined by international cooperation measures that are (solely) aimed at strengthening the jurisdiction of other states to tax cross-border income.”⁵⁶

Low Tax Jurisdictions

Not surprisingly, low-tax jurisdictions consider a Global Minimum Tax a breach of national sovereignty, or simply a barrier for their business model.⁵⁷ But, importantly, even for low-tax nations such as Singapore it is argued that investors are attracted for many non-tax reasons, such as its stability,

⁵¹ Jeroen Lammers, *Can Developing Countries Do Better Than the Unified Approach?* The Int'l Centre for Tax and Development (ICTD). <<https://www.ictd.ac/blog/developing-countries-unified-approach-digital-economy-tax/>>

⁵² Tarcisio Diniz Magalhaes and Ivan Ozai, *A Different Unified Approach to Global Tax Policy: Addressing the Challenges of Underdevelopment* (2020). <<https://papers.ssrn.com/abstract=3667717>>; Jeroen Lammers, *Less is More — Can Developing Countries Gain Tax Revenue by Giving up Taxing Rights?* (2020); <<https://papers.ssrn.com/abstract=3669117>> Andrea Riccardi Sacchi, *Implementing a (global?) minimum corporate income tax: An assessment from the perspective of developing countries*, 4 Nord. J. Law Soc'y (2021); <<https://journals.ub.umu.se/index.php/njolas/article/view/188>> Martin Hearson, *Imposing Standards: The North-South Dimension to Global Tax Politics* (2021).

⁵³ Martin Hearson et al., *Developing Influence: The Power of 'the Rest' in Global Tax Governance*, Rev. of Int'l Pol. Econ. 1–24 (2022).

⁵⁴ Magalhaes and Ozai, above n. 54.

⁵⁵ UN Comm. of Experts on Int'l Cooperation in Tax Matters, *The Role of Taxation and Domestic Resource Mobilization in the Implementation of the Sustainable Development Goals*, UN Doc. E/C. 18/2018/CRP.19 (2018).

⁵⁶ Belisa Ferreira Liotti, *Limits of International Cooperation: The Concept of 'Jurisdiction Not to Tax' from the BEPS Project to GloBE*, 76 Bull. for Int'l Tax'n 63 (Feb. 2022), IBFD.

⁵⁷ See Patrick Emmenegger and Hanna Lierse, *The Politics of Taxing the Rich: Declining Tax Rates in Times of Rising Inequality*, J. of Euro. Pub. Policy, 29:5, 647–651 (2022).

geographical location, and other “soft” factors: e.g., its strong rule of law, skilled workforce, and focus on bilingualism.⁵⁸

2.3 Different Scenarios

But even if we consider the interests at stake, assuming they are rightly identified, the simple question remains: how will the international tax system proceed? Naturally, there are no simple straight-line answers.

Complexity of the international tax system:

The complexity of the international tax system results from a wide variety of phenomena: First, it is a political question on various levels, which leads to, second, the difficult legal task of balancing the interests, where, third, those interests are hard to analyze due to the integration of different disciplines and their technological, cultural, economic, ecologic, institutional dimensions into their social structures and institutions, affecting a variety of stakeholders.

For example, the discussion is also one of foreign policies and the question of how much free trade in times of globalization and digitalization is possible if the former superpowers are heading towards protectionism and new players on the horizon are not (yet) willing to take over their place.

Within or aside with the foreign policy, the debate for the fair share of the tax pie comes along with the question of distributive justice, e.g., in the development aid policy. This debate is dominated by a tenacious conflict of the “1920’s agreement”, in which developed countries played a critical role in setting the rules. By that, so it is said, they laid the foundation for the tax system which is affecting developing countries even today. The discussion starts with this rather historical argument but follows the power structures and negotiates the question from if the OECD as an elite club still ought to be the rule maker of today’s tax system, over democratically deficits in the established international tax system, to the final and most important question of how to attribute profits of MNEs between states fairly.

This does not only affect the international policies but also has implications for national policies. The debate of distributive justice appears to be between small and medium sized enterprises (SME) and MNE as well as regional and worldwide acting enterprises. It even shapes the picture of “we as the people against the upper class” as it is said that the “little man from the street” has to pay more taxes than companies owned by the richest people of the planet and gives challenges to explain why the digitalized globalization is not only a project of already wealthy cosmopolitans but also a project of the majority of the often-assumed globalization losers.⁵⁹

Within this international framework, but mostly on a state level, different interests of different states or organizations (see above) contrast with each other, all trying to reflect their specific agenda on the international level. This might not be an easy task, as they all must balance a variety of interests, partly opposed to each other. Their diplomacy relies either on the fact that they are a so-called market state or resident state, hosting either routine functions like mere production or logistics or even only the consumer as a market, or they are hosting non-routine functions like Research & Development or intangibles. Some might be more dependent on Foreign Direct Investments, some more or less on (Foreign) Corporate Taxation, some host rather local SME than global MNE, some a merger of everything previously mentioned – although the global value chains rather reflect the hegemonial structure of the Global North with its high end production and property of intangibles in form e.g. of patents, and of the Global South as minor value contributor with its routine functions in the sense of a extended workbench.

So, within this complexity, where are we heading?

⁵⁸ Eng Kiat Loh, *The Global Tax Deal From A to Z*, 104 Tax Notes Int’l 779–783 (2021).

⁵⁹ Populism and the Economics of Globalization, <https://papers.ssrn.com/abstract=2999538> (last visited Jun 24, 2022)

We have laid down some assumptions, narratives, or paths, which might result in different scenarios with a higher or lower chance of coming true, depending on the strategy of nations worldwide.

The one scenario argues along the promise of protectionism and delinking to reach true digital sovereignty, the other scenario argues along the promise of a new Global Digital Transformation which could be achieved if we combine the new reform of the century with other regulatory measures in the digital realm worldwide.

The Path Along With Protectionism and Delinking: The Promise of Its Own Digital Sovereignty

The notion of “sovereignty” has been discussed before. Already after the first world war the globalization trend was reversed, and after the 1929 crash ideas based on the theory of List⁶⁰ it became popular that nations do not primarily have to participate in the international division of labor in order to achieve economic prosperity – all they need are self-sufficient large economies⁶¹.

But for the Global South the notion of “sovereignty” is better represented through the alternative given by Amin, who argues for a “de connexion” of third-world countries / the Global South, as they cannot hope to raise living standards if they continue to adjust their development strategies in line with the trends set by a fundamentally unequal global capitalist system over which they have no control — thus their only hope is to “delink” from the global system⁶². Amin argues that China is perhaps the only BRICS⁶³ country that is trying to combine two conflicting things, namely a national sovereign project and tax globalization⁶⁴.

In this sense, digital sovereignty might mean a serious departure from the global free trade system, with all its barriers to foreign direct investment and cross-border data flow — leading to a new era of national protectionism to develop the technical and political infrastructure apart from the GAFAM, NATU, and BATX internet powerhouses. And with “serious departure” it is not meant a kind of “soft” cultural domination or paternalism - Amin actually means that there is no capital flow or even advice, e.g., also no technology flow or developing aid, to reach full independency so that each nation (from the Global South) can find its own path without the Global North.

Although the task might seem to be overwhelming and impossible for a country, if one follows this route of thought, the argument here is that by establishing its own information and communications technology (ICT) infrastructure and regulation, there might be a form of independence with offers new ways of developing a completely new path to its own sovereignty.

The counterargument, which might be challenged,⁶⁵ but comes as natural as the modern world is that: free trade and its trickle-down effect bring forward a strong case against delinking in a world where capital (and partly labour) is globalized and where the rise of the intangibles and its data and technology-driven businesses play an increasing role.

⁶⁰ Accordingly, countries should not open their borders to advanced foreign competition until their own capitalist modernization process has produced competitive companies, see Friedrich List, *Das nationale System der politischen Ökonomie*, 1841.

⁶¹ Christoph Scherrer, *Krieg und Abschottung: Das Ende der Globalisierung?*, *Blätter für deutsche und internationale Politik*, 6 p.83-89 (2022).

⁶² Samir Amin, *Delinking: Towards a Polycentric World*, Zed Books, 1990.

⁶³ Brazil, Russia, India, China, and South Africa

⁶⁴ Ingrid Harvold Kvangraven, *A Dependency Pioneer — Samir Amin*, 2017, p. 12–17.

⁶⁵ Fiona Macmillan, *What Happens as Technology Travels on the Global Value Chain?* *Afronomicslaw.org* (Nov. 12, 2020). <<https://www.afronomicslaw.org/index.php/2020/11/12/what-happens-as-technology-travels-on-the-global-value-chain>>

The Path Along With Uncertainty: The Promise of Integration Within a Global Digital Transformation

But the path we are facing today and will probably continue to face is the path of uncertainty. The most recent reform options, unthinkable for decades and shielded along “quiet politics”⁶⁶ — are probably going to happen and, as Elliffe argues, as the absence of an articulated theoretical basis for taxation means both uncertainty and instability in the international tax framework, it might be some time until the system has stabilized.⁶⁷

This new international tax framework will indirectly affect other regulatory means: as taxation of (digital) MNEs is crucial for global trade, at least there will be an unspoken standardization process to make the tax reform work. But this will happen rather as a byproduct than because of clear intention, as there appears to be no straightforward strategy, let alone a long-term one which could survive governmental change. The only sure thing regarding the interests of the affected stakeholders is that the most powerful actors are heading to a mixture of “force and nudging” for the free flow of the digital economy with low taxation for companies like GAFAM or BATX and low regulation in other areas to the detriment of digital sovereignty.

But, International tax reform can provide an opportunity for regulation of the digital economy at large. If the affected stakeholders use the standardization process necessary to make the “reform of the century” work in order to discuss matters such as an R&D incentive for the digital transformation in light of the resource crisis,⁶⁸ data protection and data localization laws,⁶⁹ and even utopian scenarios like open cross-border data sharing⁷⁰ — then the promise of integration within a global digital transformation could come true.

Probably unintentionally, the European Commission is following this path with its most recent attempts to regulate the digital economy in its entirety (without having in mind that their regulatory approaches in the area of General Data Protection Regulation or competition law could be combined with efforts in the taxation of the digital economy).

3. FINAL REMARKS: INTERNATIONAL COOPERATION SHOULDN'T DIMINISH DIGITAL SOVEREIGNTY

Making laws for itself is a country's indication of its sovereignty⁷¹ — independence that is not subject to any superior power and cannot be restricted against its will. Hence, a country acting within the sphere of its jurisdiction is, in principle, free to shape its national tax legislation concerning taxes because of its sovereignty.⁷² Such sovereignty allows countries the right not only to make decisions only about the general features of their tax systems but also to frame special measures from time to time to make their country attractive to multinationals for foreign direct investment.⁷³

The promise of its own digital sovereignty is insofar heavily interconnected with the concept of what global justice requires, as van Apeldoorn argues, and the BEPS initiative is unlikely to meaningfully

⁶⁶ Margarita Gelepithis and Martin Hearson, *The Politics of Taxing Multinational Firms in a Digital Age*, J. of Eur. Pub. Policy 1–20 (2021).

⁶⁷ Craig Elliffe, *The Brave (and Uncertain) New World of International Taxation Under the 2020s Compromise*, 14 World Tax J. 1–15 (2022).

⁶⁸ See Stefan Greil, *Sustainable Transfer Pricing — Sustainability Factors as Missing Variables in Value Creation and Profit Allocation?* Zeitschrift für Umweltpolitik & Umweltrecht 150–188 (2021).

⁶⁹ See Rishab Bailey and Smriti Parsheera, *Data Localisation in India: Questioning the Means and Ends*, Social Science Research Network (2018). <<https://papers.ssrn.com/abstract=3356617>>

⁷⁰ See Jan Winterhalter et al., *Data as Taxes: A Blueprint for a Technical, Institutional, and Normative Framework for the Data Economy to Pay Taxes in Data*, Fraunhofer ISST-Report 31 (2021).

⁷¹ Sovereignty has been described as a supreme power to govern a particular territory without interference, especially without interference from other government and countries. Sovereignty is more of “legal power” and not of economic power. Thus, sovereignty is the power of the state to protect legal independence.

⁷² Vikram Chand et al., *International Tax Competition in Light of Pillar II of the OECD Project on Digitalization*, Kluwer Int'l Tax Blog (May 14, 2020). <<http://kluwertaxblog.com/2020/05/14/international-tax-competition-in-light-of-pillar-ii-of-the-oecd-project-on-digitalization/>>

⁷³ Aleksandra Bal, *Tax Incentives: Ill-Advised Tax Policy or Growth Catalysts?* <<https://www.ibdt.org.br/RDTIA/en/1/tax-incentives-iii-advised-tax-policy-or-growth-catalysts/>> RDTI Atual, 2016 — Special Edition: Internacional tax principles in BRICS and OECD countries. Needless to say, the sovereignty of countries has never been wholly absolute, as they are participants in an international framework. Thus, the agreement to abide by transnational and international laws at times may mean renunciation of some sovereign rights.

address this injustice.⁷⁴ Accordingly, it cannot be expected that curbing tax competition will bring the fiscal self-determination of low-income countries even close to that of high-income countries — and will fail to even improve on it in a reliable way.

The BEPS project clearly stated “[t]ax policy is not only the expression of national sovereignty but it is at the core of this sovereignty, and each [country] is free to devise its tax system in the way it considers most appropriate” — seems this objective is lost among all the political discussion going around in the Pillar solution.⁷⁵ Some even said that “the propaganda of proposing global tax harmony is merely another malevolent ploy in the strategy of the global elite to gain control over the free-market economies.”⁷⁶

So, can we say the sovereign nation have the right to design its tax policies that promote economic activity, improve employment rates, attract foreign investment, and enhance international competitiveness in the nation? Or, in other words: is the reform of the century to the detriment of the notion of digital sovereignty? One has to admit that even without the Pillar solution, countries were not entirely sovereign and were influenced by the policy choice of dominant players/ global political power, and some countries had the edge over others. Needless to say, innovation, cooperation, and cross-border dealings are essential to remain competitive in this digital era — yet countries should have digital sovereignty and power should not be “transferred to few economies of the world for playing a dictator’s role, or should we say giving up sovereignty for tax cooperation outweigh the benefits gained by cooperation and multilateralism,” as Liotti argues.⁷⁷

If we assume that countries are not trying to delink from the rest of the world, and if we are not seeing a form of re-shoring but the carrying on of global value chains as a means of business as usual, then the best way for achieving true digital sovereignty might be to use the reform of the century as a platform to design the digital economy in a broad scope and to invent new flexible rules for the digital and data economy in its entirety.

After all, the essential question will be how not only major players such as the U.S., EU, China, India but also “the rest of the world” could build a consensus by compromising on the institutional and substantive aspects of the multilateral tax order for achieving true digital sovereignty without a substantial detriment to the rest of the world.

⁷⁴ Laurens van Apeldoorn, *BEPS, Tax Sovereignty and Global Justice*, 21 *Critical Rev. of Int’l Soc. and Pol. Philosophy* 478–499 (2018).

⁷⁵ OECD, *Addressing Base Erosion and Profit Shifting*, Primary Sources IBFD (2013), p. 28.

⁷⁶ Denis Kleinfeld, *Why Globalisation of Tax Will Never Take Place*, IFC (2022). <<https://www.ifcreview.com/articles/2022/march/why-globalisation-of-tax-will-never-take-place/>>

⁷⁷ Belisa Ferreira Liotti, *Limits of International Cooperation: The Concept of ‘Jurisdiction Not to Tax’ from the BEPS Project to GloBE*, 76 *Bull. for Int’l Tax’n* 63 (Feb. 2022), IBFD.