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Strategic Incentives for Pillar Two Adoption

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Abstract: I analyze countries' strategic incentives for adopting elements of the OECD's Pillar Two proposal for reforming international taxation. I treat the three components of Pillar Two—the Income Inclusion Rule (IIR), the Under-Taxed Profits Rule (UTPR), and the Qualified Domestic Minimum Top-Up Tax (QDMT)—as independent of one another. Countries are assumed to make strategic decisions about whether to adopt each component simultaneously with other countries facing similar choices, each aiming to maximize its own objectives.

I argue that although Pillar Two's designers aimed to maximize strategic interactions among participating countries, overall, remarkably few incentives for adoption emerge. In particular, contrary to what many have supposed, there is no revenue or other conventional incentive for adopting the UTPR, and certain unusual ideological motives are needed. Further, neither QDMT nor IIR adoption is necessarily a rational response to the UTPR, therefore even assuming specific ideological motives, UTPR adoption incentives may be lacking. I also show that no IIR adoption incentives arise from the apparent competition among parent jurisdictions to apply IIRs, and because Pillar Two designers implicitly postulate mutually incompatible incentives—sometimes countries are assumed to be national-income-maximizing and other times not—IIR and QDMT adoption incentives are indeterminate.

Overall, the narrative perpetrated by proponents of Pillar Two, that a country that fails to adopt the IIR, UTPR, or QDMT would be leaving "money on the table," is unfounded. Moreover, this narrative—that countries should adopt Pillar Two as a defensive measure so as to prevent other countries from predating on their tax bases—is in obvious tension with the OECD's previous efforts (especially before the October 2021 political statement) to cast Pillar Two as a cooperative endeavor.

Introduction

In October 2021, the Organization for Economic Cooperation and Development (OECD) announced an agreement among over 130 countries on a "Two Pillar" proposal to reform international corporate income taxation.[1] In 2022, the OECD and the key sponsor nations of the agreement turned to its "implementation". Pillar Two of the 2021 global tax deal—a proposal for a "global minimum tax"—is said to have made the greatest advance in such implementation.[2] In this paper, I lay out a conceptual

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[i] Author email: wei.cui@ubc.ca. I am grateful for discussions of the paper with Reuven Avi-Yonah, Peter Merrill, Michael Lennard and Noam Noked. All errors, however, remain my own and should not be attributed to others.

[1] OECD, STATEMENT ON A TWO-PILLAR SOLUTION TO ADDRESS THE TAX CHALLENGES ARISING FROM THE DIGITALISATION OF THE ECONOMY (Oct. 8, 2021) [hereinafter OECD October 2021 Statement].

[2] OECD, TAX CHALLENGES ARISING FROM THE DIGITALISATION OF THE ECONOMY – GLOBAL ANTI-BASE EROSION MODEL RULES (PILLAR TWO) (Dec. 20, 2021) [hereinafter the Pillar Two Model Rules]; OECD, TAX CHALLENGES ARISING FROM THE DIGITALISATION OF THE ECONOMY – COMMENTARY TO THE GLOBAL ANTI-BASE EROSION MODEL RULES (PILLAR TWO) (Mar. 14, 2022).

scheme for understanding countries' incentives for adopting elements of Pillar Two (also known as the Global Anti-Base Erosion or GLoBE rules). Specifically, I assess certain claims that have been made regarding the design of the GLoBE rules, to the effect that the rules contain novel enforcement mechanisms that increase incentives for countries to adopt them.[3] The basic question the paper seeks to answer is: does Pillar Two offer incentives that increase the likelihood of its adoption?

In my analysis, Pillar Two has three distinct components: the Income Inclusion Rule (IIR), the Under-Taxed Profits Rule or UTPR, and the Qualified Domestic Minimum Top-Up Tax (QDMT). I treat the three components as independent: any component(s) may be adopted without the other(s). I present countries as deciding whether to adopt (any of) them simultaneously with other countries facing similar choices. Countries are assumed to act strategically: each tries to maximally achieve its own objectives, given the expectation that other countries will act the same way.

My analysis therefore proceeds as though no country, at the beginning of 2022, was required to adopt any of the components of Pillar Two, notwithstanding the fact that, in October 2021, 137 countries in the OECD Inclusive Framework agreed to a political statement. For many observers of the OECD process, this premise simply describes reality: until some more definitive agreement is entered into (e.g. with at least signatures by participating countries, if not ratifications by domestic legislatures), Pillar Two is not legally or otherwise binding on any country.[4] This understanding was in fact explicitly expressed by some countries actively preparing for Pillar Two implementation.[5] Nonetheless, many commentators express the contrary view that the issue of whether some version of Pillar Two will be widely adopted is settled ("the train has left the station."). But regardless of how one interprets commitments implied by the OECD October 2021 Statement, it is notable that, in trying to persuade reluctant countries to join in 2022, many political leaders advocating for Pillar Two implementation frequently appeal to national self-interests. They often speak as though the global minimum tax, once properly understood, is something that would be irrational not to adopt.[6] This suggests a self-

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[3] Some elements of such design, and commentaries thereon, can already be found in OECD, TAX CHALLENGES ARISING FROM DIGITALISATION – REPORT ON PILLAR TWO BLUEPRINT (Oct. 14, 2020) [hereinafter Pillar Two Blueprint].

[4] *See, e.g.*, Scott Wilkie, *Next Steps for the OECD Pillars: Moving From a Political Deal to an Enforceable Law*, 104 TAX NOTES INTL 889 (Nov. 22, 2021); Michael Lennard*, Boats Against the Current? Tax Multilateralism in Turbulent Times,* 106 TAX NOTES INTL 1157 (May 30, 2022).

[5] The Swiss government, for example, proposed a constitutional amendment in January 2022 to facilitate Pillar Two implementation. Yet it confirmed that "jurisdictions are under no political or legal obligation to adopt [the OECD] rules." *See* Federal Department of Finance of Switzerland, Q&A ON THE IMPLEMENTATION OF THE OECD MINIMUM TAX RATE IN SWITZERLAND (Jan. 13, 2022), https://www.efd.admin.ch/dam/efd/en/steuern-international/umsetzung-oecd-mindesteuer/q-a-oecd-midesteuer.pdf.download.pdf/20220601-q&a-det-ch-en.pdf. *See also* Amanda Athanasiou, *New Zealand Officials Undecided on Pillar 2 and DST,* TAX NOTES (May 6, 2022), https://www.taxnotes.com/tax-notes-today-international/base-erosion-and-profit-shifting-beps/new-zealand-officials-undecided-pillar-2-and-dst/2022/05/06/7dgfn (New Zealand's willingness to implement Pillar Two is conditional on other countries' implementation). A widely discussed fact is that the United States, the leading sponsor of Pillar Two in 2021, may not be able to pass domestic legislation to implement it.

[6] *See* Elodie Lamer, *Opposition to Pillar 2 Proposal Shrinks at ECOFIN Meeting*, TAX NOTES (Mar. 16, 2022), https://www.taxnotes.com/tax-notes-today-international/corporate-taxation/opposition-pillar-2-proposal-shrinks-ecofin-meeting/2022/03/16/7d8vy (EU Tax Commissioner Paolo Gentiloni cited as claiming that if any country fails to implement the IIR before other countries implement the UTPR, it will lose tax revenue to such other countries); Stephanie Soong Johnston, *OECD Pillar 1 Implementation Now Expected for 2024, Cormann Says,* 106 TAX NOTES INT'L 1191 (May 30, 2022) (OECD Secretary-General Mathias Cormann cited as arguing that once there's a critical mass of countries on board, "it becomes very hard not to become part of it because essentially, you leave money

understanding among Pillar Two designers that the best argument for its adoption is not that a failure to adopt breaches some recent international agreement, but that it would go against enlightened self-interest. It is this understanding that this paper aims to probe.

It should be emphasized that understanding Pillar Two adoption incentives is critical from a social scientific perspective. Even if countries both agreed to and actually implement Pillar Two, why they do so still require an explanation. Without such an explanation, any social scientific examination of international taxation in the aftermath of the 2021 global tax deal would need to take an entirely unprecedented and unanticipated regime that emerged in 2021 as given. This seems obviously unsatisfactory. Yet at this point, no such explanation has been attempted. My goal is to investigate whether such an explanation may have anything to do with the design of the GloBE rules, when countries are assumed to act strategically in their self-interests.

Overall, the paper concludes that while Pillar Two's designers aimed to maximize strategic interactions among participating countries—with rules that incentivize countries to compete to apply IIRs and UTPRs, to use UTPRs to incentivize IIR and QDMT adoption, and to encourage QDMT adoption in reaction to IIRs—remarkably few incentives for adoption emerge. Specifically, the main findings regarding Pillar Two's three components are:

1. Contrary to what many have supposed, there is no revenue or other conventional incentive for adopting the UTPR, and certain unusual ideological motives are needed. Moreover, neither QDMT nor IIR adoption is necessarily a rational response to the UTPR. Therefore, even assuming specific ideological motives, strategic considerations do not favor UTPR adoption because it cannot be expected to be effective in bringing out the desired outcomes.

2. With respect to IIR adoption, Pillar Two promoters increasingly appeal to two mutually incompatible kinds of incentives. Countries are sometimes assumed to maximize national income, but Pillar Two design has weakened the incentives for such countries to implement IIR-like rules. At other times, countries are assumed not to maximize national income, but the strength of alternative motives is unclear.

3. Whether QDMT adoption is a rational response to the IIR depends on why countries adopt the IIR: ambiguity regarding IIR adoption incentives therefore also renders QDMT adoption incentives indeterminate. Moreover, QDMT adoption is generally not a rational response to the UTPR.

A direct implication of these findings is that the narrative, suggested by many commentators on Pillar Two, that a country that fails to adopt the IIR, UTPR, or QDMT would be a "sucker" or leaving "money on the table," is unfounded. Further, if, in the next two years, countries proceed to adopt Pillar

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on the table for other countries to collect if you don't adopt Pillar Two."); Elodie Lamer, *Pillar 2 Needs a First Mover, Saint Amans Says,* TAX NOTES (June 14, 2022), https://www.taxnotes.com/tax-notes-today-international/corporate-taxation/pillar-2-needs-first-mover-saint-amans-says/2022/06/14/7dkm7 (Director of OECD Centre for Tax Policy and Administration Pascal Saint-Amans cited as explaining adoption incentives as "if somebody just grabs the tax — your tax — well, you will not let it go. You will act yourself.")

Two, the reasons they do so may be attributed to the intrinsic attractions of Pillar Two's goals,[7] or aspects of the political process by which the agreement on Pillar Two is reached,[8] but *not* to purported incentives arising from Pillar Two's design. It would not make sense, for instance, to interpret countries' QDMT adoption as a rational response to the risk of UTPR adoption, if such a response is demonstrably *not* rational. At the same time, if the process by which countries come to agree to Pillar Two implementation is very idiosyncratic, any success achieved by Pillar Two may also not be easily generalizable to other international agreements.

This paper contributes to the emerging legal and economic literature on the 2021 OECD tax agreement by filling important gaps. In particular, the adoption incentives for the components of Pillar Two have yet to be systematically studied. Several recent papers by economists assume that low-tax source countries will raise CIT rates in reaction to IIRs, and examine the welfare properties of such rate increases.[9] These normative analyses do not examine IIR (or UTPR) adoption incentives, and therefore depict a landscape of international taxation that emerges from a *deux ex machina* transformation. Arguably, such analyses eschew any explanatory ambition.[10] Some legal scholars have suggested that QDMT adoption may be a rational response to IIR and UTPR,[11] but they do not analyze the incentives for IIR or UTPR adoption, and therefore implicitly take IIR or UTPR adoption as given. By contrast, this paper does not take the adoption of any of the Pillar Two components as given, and shows that QDMT adoption incentives may depend on the nature of IIR adoption incentives.[12] Finally, assuming that countries react to IIR adoption strategically, some have argued for alternative designs for the IIR, taking its objectives as given.[13] This paper applies the assumption of strategic interactions among nations more broadly to illuminate adoption incentives for all three components of Pillar Two, including the IIR itself.

The rest of the paper proceeds as follows. Section I illustrates the IIR, UTPR and QDMT components of Pillar Two with a basic stylized example. Section II then examines the adoption incentives

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[7] For an evaluation of the intrinsic appeal of Pillar Two as an agenda for international tax cooperation, see Wei Cui, *New Puzzles in International Tax Agreements*, forthcoming in TAX LAW REVIEW (2022).

[8] It may be relevant, for example, that Pillar Two agreement process is dominated by tax administrators and finance bureaucrats, as opposed to politicians in normal domestic legislative procedures. See discussion in Section V. Although these alternative explanations are not standard fare in positive explanations of international taxation, their relevance is enhanced by analyses that show that conventional assumptions of Nash-optimization fail to explain observed behavior.

[9] *See* Eckhard Janeba & Guttorm Schjelderup, *The Global Minimum Tax Raises More Revenues than You Think, or Much Less,* CESIFO WORKING PAPERS No. 9623 (Mar. 7, 2022); Niels Johannesen, *The Global Minimum Tax,* CENTER FOR ECONOMIC BEHAVIOR & INEQUALITY WORKING PAPER 01/22 (Jan. 13, 2022); Shafik Hebous & Michael Keen, *Pareto-Improving Minimum Corporate Taxation,* CESIFO WORKING PAPERS No. 9633 (Mar. 12, 2022).

[10] In adopting simple normative criteria (i.e. revenue or national income maximization), the cogency of such analyses also need to be viewed in light of normative assessments made from non-economic perspectives. For examples of the latter, *see* Lennard, *supra* note 4 (examining the norms of multilateralism); Jinyan Li, *The Pillar 2 Undertaxed Payments Rule Departs From International Consensus and Tax Treaties,* 174 TAX NOTES FEDERAL 1695 (Mar. 21 2022) (assessing UTPR against existing international legal norms).

[11] Noam Noked, *The Case for Domestic Minimum Taxes on Multinationals,* 174 TAX NOTES FEDERAL 819 (Feb. 7, 2022); Michael P. Devereux, John Vella, & Heydon Wardell-Burrus, *Pillar 2: Rule Order, Incentives, and Tax Competition,* OXFORD UNIVERSITY CENTRE FOR BUSINESS TAXATION POLICY BRIEF 2022 (Jan. 14, 2022), https://ssrn.com/abstract=4009002.

[12] While the IIR can be analogized to familiar anti-deferral rules, and the reasons for and against adopting such rules are well known, I consider what additional incentives are introduced by Pillar Two.

[13] Chris William Sanchirico, *Should a Global Minimum Tax be Country-by-Country?*, 175 TAX NOTES FEDERAL 549 (Apr. 25, 2022).

for the UTPR—the component of Pillar Two most likely to be perceived as introducing novel enforcement mechanisms, and discussion of which has generated perhaps the most confusion. Because this paper's findings regarding UTPR adoption may be surprising to some readers, Section II further discusses potential objections to the assumptions in my analysis. Section III then discusses adoption incentives for the IIR, while Section IV does the same for QDMT. Section V highlights an important tension within the OECD's narratives about whether cooperative or strategic considerations drive Pillar Two adoption. It then identifies several other features of the OECD political process besides the design of the GloBE rules that may increase the likelihood of Pillar Two adoption.

I. The Three Components of Pillar Two: A Schematic Example

The OECD Pillar Two proposal has garnered global attention from policymakers and tax professionals. Summaries of its main provisions and explanations of technical details are consequently easy to find. Instead of repeating such summaries, the following schematic example illustrates the main features and intended effects of Pillar Two's three components.

Consider four types of countries. First, Countries X and Y host operating subsidiaries of multinational enterprises (MNEs) and have relatively high corporate income tax (CIT) rates. MNE subsidiaries in both countries display effective tax rates (ETRs)—as calculated according to the Pillar Two Model Rules, which starts with book income but allows a number of adjustments—that are above the Pillar Two minimum of 15%. Second, Country Z also hosts MNE subsidiaries, but imposes a low CIT rate that, along with perhaps other tax preferences, results in ETRs lower than 15% among MNE subsidiaries. Third, Country U is a large economy and hosts MNE headquarters (referred to in Pillar Two as ultimate parent entities or UPEs). Country U offers tax incentives to the operations of both domestic and foreign MNEs, such that many MNE group companies operating there have ETRs below 15%. Fourth and finally, a tax haven country H hosts holding companies in MNEs groups (referred to in Pillar Two as intermediate parent entities or IPEs), which are subject to ETRs of close to 0%. Countries X, Y, Z, U, and H are representatives of their types, each of which types contains many other members. One can imagine, for example, X and Y are France and Germany; Z is Ireland or Switzerland; U is the U.S. or China; and H is Luxembourg, Hong Kong, or Bermuda.

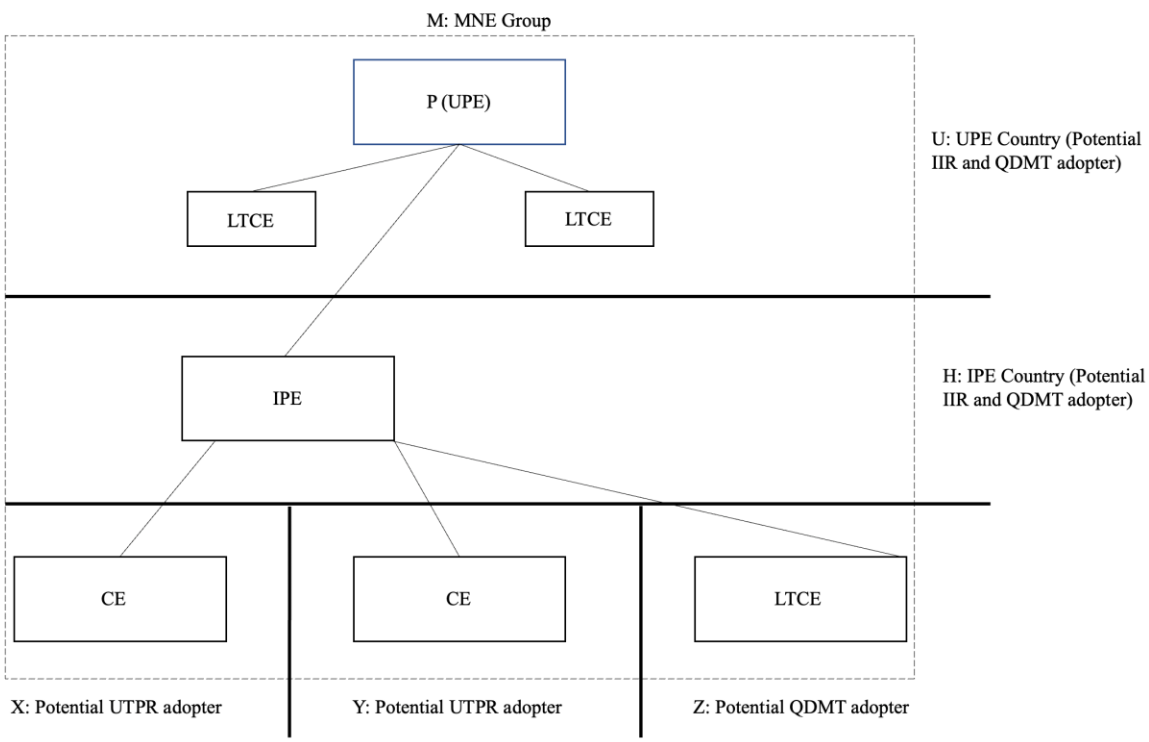
Pillar Two only applies to certain large MNEs: in particular, covered MNE groups must exceed a EUR 750 million annual revenue threshold, must not be excluded entities (e.g. investment funds), and must not be from the exempted industries (e.g. shipping).[14] Controlled entities within the covered MNE groups are referred to as Constituent Entities or CEs, and CEs with ETRs below 15%—which in the above example can be found in countries Z, U and H—are considered low-tax CEs or LTCEs.

We can now describe Pillar Two's three main components. The GLoBE rules are intended to ensure that a covered MNE group bears a minimum 15% of ETR in each jurisdiction in which it operates. One way to achieve this outcome is through the application of the IIR. Suppose an MNE group (M) has its UPE, P, in Country U; has operating subsidiaries in Countries X and Y; and has an LTCE in Country Z. If U, as the "UPE" jurisdiction, adopts the IIR, it would impose a "top-up" tax on P, corresponding to the difference between the 15% minimum ETR required by Pillar Two and the actual ETR displayed by the

[14] A similar revenue threshold used for country-by-country reporting under the OECD's previous Base Erosion and Profit Shifting (BEPS) project covered close to 6,000 MNEs around the world, OECD, OECD CORPORATE TAX STATISTICS, at 36 (3d ed. July 29, 2021), https://www.oecd.org/tax/tax-policy/corporate-tax-statistics-third-edition.pdf.

Country Z LTCE.[15] The top-up tax imposed on P in Country U but in respect of the Country Z CE, along with any Country Z tax already imposed on that LTCE, would ensure that the Country Z CE's profit is subject to an aggregate minimum 15% rate.

Figure 1: Illustrative Example of Country Types



Suppose Country U does not adopt the IIR. This would mean that the Country Z CE still enjoys a lower-than-15% ETR. Pillar Two envisions two types of remedies. First, if P holds the Country Z LTCE through a holding company in Country H, and if Country H adopts the IIR, Country H would impose a top-up tax on that IPE in respect of the undertaxed profit of the Country Z CE. That is, Country H can substitute for Country U in imposing the IIR. Second, if Country H also fails to adopt the IIR, Country X or Country Y, or the two collectively, can step in and impose the UTPR in respect of the under-taxed profit of the Country Z CE. They would collect a top-up tax from the Country X or Country Y operations of M corresponding to the tax that was not paid in Country Z.

While the IIR can raise the aggregate ETR of an LTCE outside the UPE jurisdiction to 15%, it is not designed to do so to LTCEs in UPE jurisdictions. This means that M will continue to have LTCEs in Country U. According to the Pillar Two Model Rules, Country X or Country Y, or both jointly, is allowed to collect additional top-up taxes in respect of the low-taxed profit of Country U LTCEs by applying the UTPR.[16] Such UTPR top-up taxes are to be collected from M's CEs in Country X and Country Y, respectively.

[15] There is a "substance-based carveout" based on tangible assets and payroll in Country Z that reduces the amount of the top-up tax.
[16] Indeed, such Country U LTCE may include P, the ultimate parent entity itself.

Finally, a QDMT may be adopted by Country Z or Country U. Country Z may adopt a QDMT to raise the ETR of M's operating subsidiary located there to 15%. If it does so, Country U would no longer be allowed to apply the IIR in respect of the Country Z CE (the latter would not be an LTCE). For the same reason, Country X or Y would no longer be allowed to impose a UTPR top-up tax on the CEs located in them in respect of the profit of the Country Z CE. Country Z could also have precluded the application of IIR or UTPR with respect to the MNE subsidiary operating in it by raising the general CIT or cut back tax preferences. However, the QDMT allows Country Z to avoid such general policy changes, by offering a more targeted response to IIR or UTPR imposition. Similarly, Country U could apply a QDMT to raise the ETRs of LTCEs operating in it to the 15% minimum, thereby precluding the application of UTPR in Country X or Y in respect of Country U CEs.

Two preliminary remarks should be made regarding the above example. First, the example describes IIR and UTPR as applying in the absence of any profit shifting. One need not assume, for example, that profits are being shifted out of Countries X, Y, Z or U through tax avoidance and tax planning. Low ETRs may characterize CEs of MNE groups simply because of different tax rates and policies of the different countries. The implementation of the global minimum tax may reduce MNEs' incentives to engage in tax avoidance, if their profits are subject to a 15% rate no matter where they are shifted to. But the goal of Pillar Two is not only to change MNE behavior, but also to affect the policies of nations—as illustrated by potential QDMT adoption.

Second, while I believe the above example accurately captures the intended logic of Pillar Two, this logic should not be assumed to be intuitive or compelling. Some readers may already find a coherent story: it may seem obvious that Countries Z and U may be forced to adopt the QDMT in response to the IIR or UTPR. Other readers, however, may feel that something is missing. The next few sections will argue that things are indeed missing, but that should not be because the above depiction of the logic of Pillar Two is inaccurate. Rather, arguments about whether Pillar Two works in terms of incentives should take the above depiction as a common point of departure.

II. Incentives for UTPR adoption

I begin the analysis of Pillar Two adoption incentives by considering the UTPR. This choice—as opposed to starting with the IIR or QDMT—is based on three considerations. First, the UTPR is designed to incentivize IIR and QDMT adoption, but not as a strategic response to the IIR or QDMT. Among Pillar Two's three elements, UTPR adoption is thus least affected by uncertainties about what other countries will do.[17] Second, the UTPR is considered by many as Pillar Two's most novel aspect. It is therefore central to assessing the incentives generated by Pillar Two design. Third, the incentives for adopting UTPR have been the least examined by existing commentary, and as I will argue, both proponents and critics of the UTPR seem to have mis-interpreted the UTPR's novelty.

1. UTPR adoption is costly and requires ideological motives

It is essential to get one basic fact about the UTPR right. Consider UTPR adoption by Country X in Section I's schematic example. The UTPR requires X to impose a top-up tax on an MNE's subsidiary in X, just because the MNE's subsidiaries in other countries (i.e. Countries Z and U) are subject to low tax on

[17] That UTPR adoption represents less of a strategic response to other countries than IIR and QDMT may be hidden by the fact that, in the OECD's Pillar Two implementation timeline, UTPRs become effective later than IIRs.

their profits. However, unlike parent companies that may be subject to the IIR top-up tax because of under-taxed profits earned through foreign subsidiaries, the subsidiary in Country X generally has no direct or indirect ownership of, control over, or access to the profits of, other subsidiaries in the same MNE group. Country X' UTPR thus can only be levied on the inputs, outputs, or profits in the MNE's operations in X. What the UTPR thus requires X to do is to tax the MNE subsidiary in itself more heavily when subsidiaries of the same MNE are taxed lightly elsewhere.

This, at least, is how the UTPR is explicitly designed. The UTPR does not entitle an adopting country to make CEs in other countries legally liable for the top-up tax it imposes. The same can be said about the IIR, of course, but the difference is that the IIR adopting country levies a tax on a taxpayer—P in our example—that has access to the profits of CEs in other countries as ultimate owner. By contrast, the UTPR affects CEs in other countries at most in an indirect way. When Country X applies a top-up tax to P's Country X CE, it immediately imposes a penalty in P's investment in Country X. It does also reduce the value of tax savings elsewhere: $1 of "under-taxation" of profits (e.g. through tax incentives) in Country Z, for example, directly leads to $1 of penalty (the UTPR top-up tax) in Country X. Nonetheless, the penalty is in the first place borne by P's operation in Country X.

Surprisingly, many discussions of the UTPR perpetuate the idea that the UTPR gives the adopter country a right to dip into a pot of undertaxed profit when other countries fail to adequately tax such profit. Such an understanding may have made sense when the UTPR was designed as an under-taxed *payment* rule: if Country X refrains from taxing a payment made from it because of the expectation that the payment would be sufficiently taxed in the recipient country, then a rule that allows Country X to tax such payment when the recipient country fails to adequately tax it shifts the tax base back to Country X.[18] As Section I noted, however, the UTPR in the Pillar Two Model Rules may apply even in the absence of profit shifting or tax arbitrage.

The idea that UTPR adoption provides costless access to profit elsewhere can be found in arguments made by both proponents[19] and critics[20] of Pillar Two, as well as in many professional exegeses of Pillar Two mechanics. An example of the latter is the interpretation of the allocation of top-up tax amounts among UTPR-adopting jurisdictions. In the Pillar Two Model Rules, if a certain amount of top-up tax is identified for an LTCE in Country Z, if the UPE jurisdiction fails to impose an IIR, and if Countries X and Y, where MNE's other subsidiaries are located, both adopt the UTPR, then Countries X and Y can each collect a top-up tax amount with respect to the under-taxed profit of the Country Z LTCE. The top-up tax amount is allocated among X and Y in proportion to the tangible assets and payroll of the MNE subsidiaries in X and Y. If Country X does not collect the UTPR top-up tax, it "loses" the UTPR percentage to Country Y: Y "gets" to collect the entire top-up tax. Some commentaries have suggested

[18] This characterization may apply to the subject-to-tax rule under Pillar Two, to anti-hybrid rules under BEPS Action 2, and to anti-tax-arbitrage rules in general. However, the possibility of profit shifting from Country X may sometimes be a pre-condition for investment in X: in such cases anti-arbitrage rules have the same negative effect on investment as raising tax rates.
[19] *See, e.g.*, Lamer supra note 6 (EU official claiming that countries failing to implement the IIR before other countries implement the UTPR would lose tax revenue to such other countries).
[20] Li, supra note 10 (suggesting that the UTPR is a tax sharing rule that "effectively shift" tax bases from some countries to others).

that this aspect of Pillar Two design incentivizes countries to adopt UTPR,[21] because not doing so would leave money on the table.

This is an outright illusion. Neither Country X nor Country Y has access to the profit earned by the LTCE in Country Z (or to the profit earned in each other). All they can do is to tax (more heavily) the profit (or input or output) of the MNE subsidiary that they each host. *But they could always have done that*. Doing so does not become less costly for either country by pretending that the additional tax on local operations is actually a tax on under-taxed profits elsewhere, or that it is "precluding" some other country from taxing their local operations more heavily. The narrative that one would be a "sucker" if one does not adoption UTPR (and "surrenders" one's UTPR percentage to others) relies on such pretense, but since the pretense is groundless, the narrative is incoherent.

Once the illusion of a sudden, new access to tax bases elsewhere is dispelled, it becomes clear that adopting the UTPR is not a dominant strategy (i.e. a sensible thing to do regardless of what other countries do). Again, the UTPR requires the adopting country to tax the MNE subsidiary in itself more heavily when subsidiaries of the same MNE are taxed lightly elsewhere. If this were generally a rational thing to do, there would have been no tax competition. Instead, it seems that for it to be rational for a country to adopt the UTPR, both of two things have to be true. First, the country must have sufficiently strong preferences regarding MNEs' ETRs in other countries. Second, the UTPR must be effective in bringing about outcomes that satisfy these preferences.

The particular preference required for UTPR adoption may be a preference that the ETRs of LTCEs in other countries increase, or that they increase as a result of changes such other countries' tax law and policy. It seems that such preference would also need to be present even if other countries' tax policies have no direct impact on the UTPR-adopting country's own revenue (or national income). This desire must moreover be sufficiently strong that the country is willing to act on it, even if by imposing a heavier tax burden on the MNE operations it hosts than it would have in the absence of this "other-regarding" desire.[22] Such a preference is perhaps best thought of as ideological in nature, and as distinct from other considerations of national welfare. Preferences of this kind certainly have not featured in standard analyses of international taxation before. Even if they seem to capture political sentiments in some countries now, one may wonder how enduring they will turn out to be. Moreover, how widely shared such ideological preference is among nations that participate in Pillar Two is also open to question.[23] But if the required ideological preference is not widely shared, then UTPR adoption should be relatively rare.

Nonetheless, I will assume that the ideological preference characterizes some countries that advocate Pillar Two adoption. Even then, however, the preference does not directly dictate UTPR adoption: UTPR adoption is rational, even given this peculiar preference, only if UTPR can effectively

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[21] KPMG, INCLUSIVE FRAMEWORK BEPS AGREEMENT- POLICY PERSPECTIVES (last visited June 10, 2022), https://home.kpmg/xx/en/home/insights/2021/12/inclusive-framework-beps-agreement-20-december-2021.html.

[22] It is commonly assumed that tax rate increases in one country have positive externalities for other countries (by driving investment away from the former country). In this sense, countries always prefer other countries to raise tax rates. However, this is not an "other regarding" preference.

[23] Consider, for example, the UK, Canada and Japan, three G7 countries that are among the leading sponsors of the 2021 OECD tax deal. In these countries' international tax policies prior to 2021, there is little evidence that they promoted high corporate tax rates in *other* countries.

induce other countries to change their tax law and increase the ETR of the CEs they host. When might such conditions hold?

2. Conditions for UTPR success

Suppose Country X is interested in making Country Z raise tax rates, reduce tax incentives, or otherwise ensure that MNEs' CEs in Z are subject to a minimum 15% ETR. X applies the UTPR to the Country X subsidiaries of MNEs that also operate in Country Z. For a given MNE, M, the top-up tax X imposes makes investment in X less attractive, but it also reduces the worth of tax incentives in Z. The question then becomes: under what conditions would M prefer not being subject to $1 of UTPR in X to being given $1 of tax benefit in Z? This is an important question: M may *not* prefer being relieved of the UTPR in X—it may rather pay tax in X than in Z, or it may be indifferent between paying $1 of tax in X or Z. In such cases, it is not clear what Country Z gains by raising taxes in response to Country X's UTPR.

When might M prefer paying tax in Z rather than in X? This seems to make sense when—and only when—M's investment in X is less elastic with respect to tax than its investment in Z. By elasticity, I mean how much less (more) M is willing to invest in X given a small increase (decrease) in X's tax rates.[24] When such relative elasticities hold, M bears more of the burden of X's top-up tax than it enjoys the benefit of tax incentives in Z. It would thus prefer giving up tax benefits in Z in exchange for eliminating the UTPR liability in X.

To make the hypothesis of such a channel realistic, it helps to postulate in addition that as a host of relatively inelastic investments, Country X did not impose the revenue-maximizing level of tax: this is because the inelasticity of MNE investment in X means that X always could have taxed MNEs more. But perhaps X is willing to forebear such imposition,[25] and it is only the incentive to make MNEs pay more tax elsewhere that motivates X to impose a higher level of tax (which it is willing to remove once MNEs paid more tax elsewhere).

This potential channel for UTPR effectiveness invites at least three questions. First, when would it be generally true for X to host more inelastic investments than investments in low tax countries? Second, when is collective UTPR adoption beneficial for adopting countries? And third, why should Country Z do anything—why should it not just allow any MNE impacted by X's UTPR to forego tax benefits in Z, instead of generally increasing ETRs for all MNEs operating in Z by increasing tax rates, curtailing tax preferences, and so on?

a. Average relative elasticities

[24] Note that in the discussion below, unless specifically stated, elasticity characterizes decisions to vary the amount of investment depending on tax rate changes—variations on the *intensive* margin. If X's tax rate is high enough, M may also decide not to invest in X at all, given fixed costs. However, the argument below depends not on M's response to X's UTPR on such *extensive* margin of investment. Because of relative elasticities on the intensive margin, M may decide to continue to invest in X, but still prefer to pay tax there instead of in Z. That is sufficient to render X's UTPR ineffective.

[25] It is not clear what would have motivated such forbearance. One possibility is that it may help sustain an international norm by which no country taxes MNE investments at the revenue maximizing level. In any case, this assumption implies that UTPR adoption may well raise revenue.

Consider the following answer to the first question. UTPR-imposing countries are likely to be high tax countries, and the fact that they are high-tax countries may suggest that investments in them are less sensitive to taxation. The opposite might be said of the low tax countries in which MNEs operate—they may have low tax rates because they host on average more elastic investments. Is this plausible? Referring to the hypothetical example above, some may believe that investments in France and Germany are on average less elastic than investments in Ireland, but how do they compare to investments in the U.S. and China?

At best, one might hypothesize that the UTPR can be effective for Country X to adopt if MNE investment in X is significantly more inelastic, on average, than MNE investment in countries where MNE operations enjoy low ETRs. This argument is based on average investment elasticities. It does not suggest that all MNE investments in X are more inelastic than MNE investments in Z. Wherever investments in X are more elastic than investment in Z, the MNE's response to the UTPR is to reduce investment in X, rather than pay more tax in Z. Here, it is worth noting that the application of UTPR cannot discriminate between countries and investments, especially if it is untied from payment.

b. Does joint adoption help?

As to the second question, the benefit of joint UTPR adoption may come from two distinct channels. First, the elasticity of investment may be an increasing function of the effective tax rate: the higher the tax rate, the more elastic the investment response. For a given amount of top-up tax associated with an LTCE elsewhere, if that amount is shared among UTPR-adopting countries, then the top-up tax applied by each country is lower, which could make the UTPR more effective by keeping investment response in the low elasticity range. Yet this is an awkward argument: nothing in Pillar Two requires a UTPR country to apply the maximum amount of top-up tax allowed by the UTPR. The UTPR rules set a cap on the top-up tax that may be applied, not a floor. Therefore, a UTPR country could always unilaterally adjust the UTPR tax and not apply it when it bears on investments outside the effective range of elasticities.[26]

Second, the more countries adopt the UTPR, the fewer choices MNEs have for escaping the UTPR by moving investment to UTPR-free locations. MNEs' elasticity at the extensive margin is thus reduced for each UTPR country. However, the more countries adopt UTPR, the fewer there are also of low-tax countries: the elasticity of investment in such countries may also diminish, which could offset the decrease in investment elasticity in UTPR-adopting countries. The benefits of joint adoption may therefore be ambiguous. Nonetheless, if low tax countries far outnumber UTPR adopting countries, then the few countries that would adopt the UTPR may benefit from joint adoption.

Despite these potential benefits of joint adoption, it is worth noting that joining a UTPR-coalition does *not* benefit any country that already has higher average MNE investment elasticity than the countries (such as Country Z) hosting LTCEs. Suppose Country Y is such a country. Y would not have been in a position to adopt an effective UTPR on its own. If Y joins a UTPR coalition, some UTPR percentage

[26] Moreover, the presence of other UTPR-adopting countries may also increase the elasticity of investment for a given UTPR-adopting country. This is because if other countries adopt UTPR, the UTPR percentage allocated to X will depend on the level of tangible assets and employees in X (relative to tangible assets and employees in other UTPR adopting countries). An MNE could reduce its UTPR liability in X by reducing tangible assets or employment (but possibly only to increase its UTPR liability elsewhere). If no other country adopts UTPR, by contrast, the MNE would not be able to reduce its UTPR liability in X, unless it terminates operation in X altogether.

would be allocated to it. But the MNE would prefer paying UTPR in Y to giving up an equal dollar amount of tax benefits in Country Z, since by assumption, the MNE bears a lower share of the tax increase in Y than the share of tax benefits it enjoys in Z. Y's adoption of UTPR therefore would not be effective. Therefore, not all countries interested in adopting the UTPR can benefit from joint adoption.

c. Why should low tax countries respond?

The third question is even more critical for understanding the conditions of UTPR effectiveness. From the perspective of Country Z that hosts LTCEs, only some MNEs may be subject to UTPR: this depends on in which other countries the MNEs operate, and whether any of them adopts UTPR. In addition, only some of the investments in Z may be characterized by higher elasticity than investment in UTPR-adopting jurisdictions.[27] For other MNEs and investments, the taxpayers may prefer not to give up the tax benefits Z offers. Z should therefore hesitate to change its tax laws for all MNEs within Pillar Two's scope.

Moreover, those MNEs that prefer giving up Country Z's tax benefits may simply cease to respond to Z's tax incentives. But it does not follow that it would be rational for Z to raise taxes on such MNEs and investments, given that, by hypothesis, the tax burden would mostly not be borne by the MNEs, but by less elastic factors such as local labor.[28] This all suggests that while the UTPR may succeed in reducing MNEs' drive to aggressively reduce their ETRs in other countries, it may not succeed in making other countries change their tax laws.

This last argument may appear to be contradicted by pronouncements from the U.K., Swiss and Irish governments in early 2022, indicating that they are considering imposing top-up taxes on domestic LTCEs in anticipation of other countries' imposition of UTPRs.[29] Such statements appear to imply that even the expectation of UTPR is already leading some countries to change their tax law in reaction. But it is important to understand the reasoning offered by these governments. Some assert that by imposing a top-up tax on domestic LTCEs, LTCE host countries can help MNEs reduce the "compliance burden" associated with UTPRs. It is not clear, though, why there is room for significant compliance burden reduction.[30] More importantly, the Swiss government suggested that while top-up taxes imposed on domestic LTCEs can raise local ETRs and eliminate UTPR liability elsewhere, Swiss cantons can find other ways to compete and make their jurisdictions attractive to foreign investors. While unclear what this entails, one interpretation is that the intended response to UTPR is some kind of *work-around* such that,

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[27] This is especially true of CEs in large economies like the U.S. and China benefitting from tax incentives.

[28] Country Z could always have taxed such inelastic factors more, just as the UTPR jurisdiction could always have taxed inelastic investments there more.

[29] Government of the United Kingdom-HM Treasury, OECD PILLAR 2- CONSULTATION ON IMPLEMENTATION (Jan. 11, 2022), https://www.gov.uk/government/consultations/oecd-pillar-2-consultation-on-implementation; Stephanie Soong Johnston, *Ireland Ponders Adopting Pillar 2 Domestic Minimum Top-Up Tax*, TAX NOTES (May. 27, 2022), https://www.taxnotes.com/tax-notes-today-international/corporate-taxation/ireland-ponders-adopting-pillar-2-domestic-minimum-top-tax/2022/05/27/7djcd?highlight=ireland%20and%20pillar; Mindy Herzfeld, *Country-by Country Strategies for Implementing Pillar 2,* 175 TAX NOTES FEDERAL 1005 (May 16. 2022), The pronouncements make clear that such top-up taxes are motivated not just by IIR adoption and would be applied to LTCEs with foreign parents even if the parent jurisdictions do not impose IIRs.

[30] Any top-up tax assessed by a UTPR country with respect to LTCEs elsewhere will require calculations based on Pillar Two rules that would presumably also be required in the assessment of the top up tax in the LTCE jurisdiction.

nominally, MNEs are subject to higher levels of taxation, but they are compensated by new (possibly non-tax) forms of benefits.

This raises the question of whether the countries considering UTPR adoption would view this kind of response to UTPR as satisfying their objectives. For example, it is possible that the ideological motivation underlying UTPR adoption is a specific preference for subsidy competition over tax competition.[31] If that is the case, then UTPR may be viewed as effective if it suppresses tax competition while fanning subsidy competition. If, however, the motivation underlying UTPR adoption is to more broadly "level the playing field" for businesses by removing government preferences (whether through tax reductions or subsidies), then the "work-around" response to UTPR should be seen as rendering UTPR ineffective. It should therefore *erode* incentives for UTPR adoption.

To summarize: the conditions under which UTPR can effectively induce other countries to raise tax rates are narrow. The crucial question for UTPR effectiveness is whether, facing a choice between a top-up tax liability in the UTPR-adopting jurisdiction and a tax of equal amount in the previously-low-tax jurisdiction, how MNEs respond. For MNEs that prefer paying tax in the UTPR jurisdiction (e.g. because they can shift more of the tax burden there), the UTPR would not be effective in raising ETRs elsewhere. The UTPR also may fail to be effective if MNEs are indifferent between the two options. Finally, even if MNEs prefer paying more tax in the previously-low-tax jurisdiction, it is not clear that such a jurisdiction should actively respond with tax policy changes. Both the unusual nature of the ideological preference underlying UTPR adoption, and the narrow scenarios for UTPR success, imply that the rationality of UTPR adoption is far from obvious.[32]

3. Is IIR adoption likely to respond to UTPR?

The most natural application of the preceding arguments is to the issue of whether countries hosting LTCEs would adopt the QDMT to respond to other countries' UTPR adoption.[33] This aspect of potential strategic interactions among countries emerging from Pillar Two's design has attracted special attention because of the pronouncements of the UK, Switzerland and Ireland in 2022, which give early emphasis to QDMT adoption: the pronouncements may have lent credibility to the UTPR's effectiveness. It is also a natural interpretation of the claim that the UTPR is a "back-stop" to the IIR: the UTPR comes into effect where IIR fails. Yet some commentators may have believed that the UTPR is intended,

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[31] *See* Noam Noked, *From Tax Competition to Subsidy Competition*, 42 U. PA. J. INT'L L 445 (Apr. 17, 2020). The work-arounds must be sufficiently effective—giving businesses sufficient benefits without incurring much higher costs for the government—for them to be rational substitutes for tax preferences.

[32] One might say that whether the UTPR can be effective crucially depends on the nature of the ideological motives underlying UTPR adoption. If the motivating preference is for MNEs to reduce aggressive tax planning, then UTPR may be effective even if other governments do not respond. Some countries may therefore rationally adopt UTPR conditional on having such preferences. If, however, the motivating preference is to force other countries generally to refrain from offering incentives to attract businesses, it may or may not be successful. Adoption incentives should then be mitigated by the risk of failure. If, finally, the motivating preference is simply to invite some countries to switch from some combinations of tax and subsidy competition to other combinations, then again UTPR may be effective. Without knowing exactly which combinations of tax and subsidy competition are unacceptable and which are tolerated, however, it would also be difficult to assess the strength of the adoption incentives.

[33] The arguments would hold true for both countries hosting LTCEs of foreign multinationals (e.g. Country Z) and those hosting LTCEs of domestic multinationals (e.g. Country U). *See infra,* Section IV.

perhaps even primarily, to generate incentives for IIR adoption. Does the UTPR have such effect? Referring to the Section I example, the question is: If Countries X and Y adopt the UTPR to collect top-up tax amounts calculated by reference to the ETR of M's LTCE in Country Z, should Country U have greater incentives to impose the IIR in respect of the Country Z LTCE?[34]

The reasoning supporting an affirmative answer may be the following. While the UTPR top-up taxes in Countries X and Y merely increase the tax burdens of M's operations in X and Y, this may be viewed by Country U as reducing its own national welfare. If U imposes a top-up tax with respect to the country Z LTCE under the IIR, it would eliminate the Country X and Y top-up taxes under UTPR, while collect more revenue for itself. The benefit of this course of action is easily understood in terms of national income maximization.[35]

But the reasoning here is not as straightforward as it at first appears. Country U can increase its national income in this scenario only if Country Z does not tax its LTCE more (e.g. through the QDMT). If Country Z responds to either the UTPR (imposed by X and Y) or the IIR (imposed by U) by raising the LTCE's ETR, Country U's IIR adoption incentives are unaffected by UTPR adoption in X and Y. That is, the UTPR cannot be effective at the same time in policing low-tax source countries—in the sense of forcing them to abandon ETR-reducing policies—and policing IIR adoption in UPE countries. Any effect the UTPR has in policing IIR adoption would be neutralized by other responses (e.g. the QDMT) to IIR adoption. In other words, UTPR adoption may incentivize IIR adoption only if jurisdictions like Country Z fail to respond to both the UTPR and IIR. This scenario is certainly possible, but it presupposes the ineffectiveness of other incentive mechanisms contemplated by Pillar Two designers.[36]

Fundamentally, the problem here is that while the purported incentive effect of UTPR on IIR adoption works through national income maximization, a country that aims to maximize national income should not generally prefer that other countries levy high taxes on the operations of its own MNEs. Such a country should be averse to IIR adoption, if QDMT adoption is an anticipated response to the IIR. Anyone who takes the incentives effects of UTPR on the IIR adoption seriously, therefore, ought to be very skeptical about IIR adoption incentives that deviate from national income maximization. But commentators who assume the effectiveness of the UTPR seem to give no less credence to the (independent) likelihood of IIR and QDMT adoption. They do not, that is, reject incentives for IIR adoption that are incompatible with national income maximization. This suggests that they are not taking the incentive effects of the UTPR on IIR adoption too seriously.

4. Limits to access to foreign tax bases

The arguments in this Section critically depend on the observation that the UTPR does not give adopting countries access to any new tax base beyond the input, output or profit of MNE operations within themselves. This observation is supported by the text of the Pillar Two Blueprint and Pillar Two

[34] Some may hold that no country would adopt the UTPR without adopting the IIR. As discussed in Section III infra, because IIR adoption may be complementary among nations, one country's IIR adoption already increases another country's IIR adoption incentives. The question here, though, is whether countries may be incentivized to adopt IIR because of UTPR adoption by others, independent of the effect of others' IIR adoption.

[35] If MNEs' choice of HQ countries is less elastic than their choice of where to establish foreign operations, then MNEs may prefer to pay the top-up tax in Countries X and Y rather than Country U. But even if this is the case, Country U may prefer to impose the tax from its own perspective.

[36] For example, it presupposes that the IIR would not incentivize other countries to raise tax rates.

Model Rules. But it conflicts with interpretations of the UTPR—advanced by proponents and critics of the UTPR alike—that portray the UTPR as offering new extraterritorial taxing rights. This gap between the text and the interpretation of the UTPR raises two questions. First, does the gap matter—what if the design of UTPR did allow countries to collect tax from foreign entities? Second, if the gap matters, how did the gap arise—how did a rather obvious point (namely that the UTPR-imposing jurisdiction can only collect tax from MNE operations in itself, it does not dip into a collective pot of MNE profit) escape so many commentators?

The first question essentially asks what if, in the hypothetical example above, Countries X and Y are allowed by the GLoBE rules to collect the UTPR top-up tax from M's CEs in Country Z and Country U. Some critics of the UTPR write as though the UTPR essentially does so, and that this is what is objectionable about the UTPR—its extraterritorial reach is inconsistent with existing tax treaty (and other international legal) norms.[37] But what if, counterfactually, the GLoBE actually did what these critics claim it does: aside from qualms about the breach of traditional international legal norms, could countries' behavior be expected to change?

One view is that even if one disregards existing legal norms, no country can really access a global pot of profit and tax more than the input, output or profit associated with MNE investments in itself. Taxation without nexus is not only norm-violating; it is also futile. Giving countries the "right" to tax MNE profits without sufficient nexus (i.e. in excess of the extent of economic presence in the countries) does not confer any effective benefit on them. Thus, Pillar Two's design cannot be improved—the UTPR's incentive effect cannot be enhanced—even by changing the norms of extraterritorial taxation.

This view holds some appeal in itself. It certainly doesn't seem right to pretend that the *only* constraint on a country's taxing power is what other countries allow it to tax—that as long as countries collectively have access to a given tax base (e.g. all MNEs in the world), how much of the tax base a particular country has access to is purely a matter of political agreement. Such a pretense also seems inconsistent with the assumptions of the analysis offered in this paper. The analysis assumes that countries act strategically as opposed to cooperatively in Pillar Two adoption. Potential adopters of the UTPR can at best induce other countries to raise tax rates (or impose the IIR) through MNE responses to UTPR adoption. They cannot influence other countries by offering to cede profits that they themselves are unable to collect from MNEs in the first place.

However, the view that taxation without nexus is not only illegitimate but also futile challenges not only the design of Pillar Two, but also other international tax reform proposals (e.g. new proposals for formulary apportionment). Perhaps some would reject this view, and hold that just as the norms of extraterritorial taxation should not be taken as exogenously given, the degree to which countries act strategically as opposed to cooperatively should also not be taken as given. That is, proposals of taxation without nexus may postulate a much stronger degree of international cooperation than is consistent with analyses in terms of strategic incentives.[38]

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[37] *See* Li, *supra* note 10; Angelo Nikolakakis, *Bait and Switch — A Reply to Casey Plunket,* 175 TAX NOTES FEDERAL 256 (Apr. 11, 2022).

[38] *See* Mitchell Kane & Adam Kern, *Progressive Formulary Apportionment: The Case for 'Amount D,'* 102 TAX NOTES INT'L 1483 (June 14, 2021) (proposing a type of formulary apportionment, whereby profit allocations are based on novel criteria such as countries GDP per capita, that clearly assumes a cooperative setting).

As noted earlier, however, the idea that countries may embrace Pillar Two based on strategic considerations has been relied on by many advocates of Pillar Two (e.g. whenever they warn potential non-participants about “leaving money on the table”). The assumptions of strategic interaction are not just arbitrarily imposed: they are internal to the Pillar Two discourse. This highlights the second question mentioned at the outset of this subsection: how did many commentators seem to ignore the fact that the UTPR does not create access to new foreign tax bases? One answer is that the OECD itself has consistently promoted readings of the GLoBE rules that project a narrative of cooperation. When such a narrative is unreflectively accepted, it becomes tempting to assume that countries are cooperating under Pillar Two even to an extent that non-cooperative limits on access to foreign tax bases are relaxed. The fact that even *critics* of the UTPR assume that the UTPR entitles adopting countries to tax foreign CEs (which is not possible unless very extensive cooperation is implied), when the UTPR evidently does not do so, is perhaps a testimony to the effectiveness of the OECD’s narrative. Section V below will further examine this narrative.

In summary, this section has argued that one should be skeptical about UTPR adoption incentives for three reasons:

1. UTPR adoption does not give countries access to new tax bases. It is costly and requires countries to harbor policy objectives that are not standardly attributed to them.
2. QDMT adoption is a rational response to other countries’ UTPR adoption only under special circumstances that cannot be generally presumed to be present. The potential ineffectiveness of the UTPR in inducing QDMT adoption should also erode the former’s adoption incentives.
3. IIR adoption may be a rational response to UTPR adoption if nations are assumed to maximize national income. But this assumption undermines other narratives about the why countries should adopt IIR—and is incompatible with the special motives required for UTPR adoption.

The basic problem with the UTPR, therefore, is not (just) that it was introduced into Pillar Two in an illegitimate way or that it is inconsistent with existing legal norms. It is instead that from a self-interested perspective, few countries, if any, should be willing to adopt it. It is likely that a neglect of the first of the foregoing three reasons for skepticism—a casual assumption that the UTPR simply gives countries a free grab at MNEs’ global profit pool—has led to the neglect of the second and third.

III. Incentives for IIR adoption

The IIR can be characterized—though, as I argue below, the accuracy of such a characterization has been diminishing since 2021—as a variant of traditional anti-deferral rules that strengthen residence-based taxation. As such, the unilateral incentives for and against its adoption are well-known. Taxing resident companies’ foreign income (including income earned from foreign subsidiaries) may raise revenue. It is also fair, given that the residence-based corporate-level tax is conventionally understood as a tool for taxing domestic individual shareholders on the basis of the ability to pay. These and other policy rationales have led many countries to adopt anti-deferral rules—such as controlled foreign corporation (CFC) rules and the U.S. Global Intangible Low-Taxed Income (GILTI) regime—without coordination with others.[39] Incentives against adoption may include concerns about

[39] Some governments may also be persuaded by arguments that worldwide taxation enhances efficiency: when combined with deductions for source-country taxes it maximizes national income; when combined with foreign tax credits, it may maximize global welfare by undoing some of the distortionary effects of source country taxes. Countries may also adopt such rules for idiosyncratic reasons. For example, the U.S. initially adopted CFC rules to

administrability, preferences to keep domestic businesses "competitive" in their foreign expansions, and preferences to attract and keep MNE headquarters.[40]

This section does not dwell on these familiar incentives but instead focuses on new (dis)incentives introduced by Pillar Two regarding IIR adoption. Three considerations are highlighted. First, Pillar Two may create greater incentives for IIR adoption by coordinating collective adoption, although it is unclear how much coordination itself enhances the incentives. Second, the fact that Pillar Two gives IPE jurisdictions "the right" to impose IIR if the UPE countries do not offers no new incentive for IIR adoption by UPE countries. Third, because QDMT adoption has become not only a possible but even an explicitly encouraged response to the IIR, IIR adoption incentives may need to be reconceptualized, and different, mutually incompatible incentives have been invoked for IIR adoption. Overall, these considerations suggest that the enhancement of IIR adoption incentives under Pillar Two is at best incremental.

1. Additional adoption incentives from coordination

Pillar Two is intended to ameliorate two purported disincentives against strengthening residence-based taxation. The first postulates that the location of MNE headquarters (HQs) is mobile and there is competition among countries for MNE HQs. Any country that adopts strong worldwide corporate taxation regimes may risk losing out in such competition, but if a sufficient number of countries hosting MNE HQs adopt IIR, the intensity of HQ competition is lowered. The second disincentive may arise if, even without assuming that HQ location decisions are tax sensitive, the strength of worldwide corporate taxation affects the "competitiveness" of a country's MNEs. For instance, one can view a country's decision to subject the foreign income of its MNEs to low taxation as a form of subsidy. Reducing such subsidy by strengthening residence-based taxation may reduce the competitiveness of one's own multinationals, but if other countries also strengthen their residence-based taxation, concerns about the disadvantages of strong residence-based taxation are mitigated.

For these reasons, countries may benefit from coordinated strengthening of residence-based taxation, and Pillar Two may be viewed as offering precisely such coordination. Nonetheless, questions can be raised about these narratives. For instance, one might expect the number of countries engaged in HQ competition to be relatively small. If mitigating HQ competition is the goal, such countries could and should negotiate among themselves to form a small tax cartel, as opposed to enlisting the majority of countries in the world to adopt the GLoBE rules.[41] In theory, the likelihood of broad international IIR adoption under Pillar Two should be less than the likelihood of collective adoption of strong anti-deferral rules among a smaller group of countries (such as the G7). It is also worth noting that there is little past evidence in support of complementarity in the adoption of anti-deferral rules. For example, the U.S. enacted GILTI in 2017. Outside Pillar Two, however, there are few reports of other countries adopting stronger anti-deferral rules in reaction to presumably reduced competition from the U.S. and U.S. multinationals.[42]

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stem capital outflows that destabilized the Bretton Woods system. More recently, it enacted GILTI purportedly to "bring jobs back to America."

[40] However, the limited scope of Pillar Two (see text accompanying note 14 supra) implies that in many countries the IIR would co-exist with anti-deferral rules that have wider application.

[41] Countries hosting foreign MNE investments may even be hurt by the reduction of subsidies from HQ countries.

[42] U.S. multinationals represent at least one quarter of all large multinational in the world.

2. Incentives from competition for IIR adoption?

Beyond any complementarity in IIR adoption by UPE countries, an important question is whether Pillar Two's design introduces additional adoption incentives by creating a competition for IIR adoption between the UPE jurisdiction and jurisdictions where intermediate holding companies reside. Although the UPE country has priority in applying the IIR under Pillar Two,[43] if a UPE countries fails to adopt the IIR, the jurisdiction of an intermediate parent entity (IPE) or partially-owned parent entity (POPE) may apply the IIR and collect revenue that the UPE jurisdiction "foregoes." In such a case, an MNE would still be subject to IIR, and benefit little from the failure of IIR adoption by the UPE country. Does this generate an additional incentive for the UPE country to adopt IIR?

It seems that this incentive is likely to be weak. The location of intermediate holding companies in current MNE structures is highly tax-sensitive. Such locations (e.g. Luxembourg, the Netherlands, Hong Kong, etc.) are generally chosen because they (i) impose low effective tax on foreign-earned profits, while (ii) enjoying a large network of tax treaties that can be used to reduce source-country taxes on payments from operating subsidiaries. By adopting the IIR and imposing top-up taxes on foreign income, they would eliminate the main reasons why MNEs choose them as locations for intermediate holding companies. As long as there are sufficiently many other jurisdictions that do not adopt the IIR, MNEs that are not subject to IIR in their UPE countries would move their intermediate holding companies to these IIR-free jurisdictions and away from those that adopt IIR. This points to incentives against IIR adoption on the part of intermediate holding company jurisdictions. Such disincentives also imply that UPE countries should not fear that, by not adopting IIR, they are leaving "money on the table" to intermediate holding company jurisdictions.[44]

This conclusion should not be surprising. Like UPE countries, countries hosting intermediate holding companies could *always* have adopted IIR-like rules: indeed, in theory they have *stronger* incentives to do so outside Pillar Two because the taxes they impose would be creditable in UPE jurisdictions, giving them effective "priority" over UPE jurisdictions. That such countries have largely not adopted anti-deferrals before (while a significant number of UPE countries have) is consistent with the conjecture that MNE's decisions as to the location of intermediate holding companies are much more elastic (even if not perfectly so) than decisions regarding HQ location. While Pillar Two contemplates that the UPE country's failure to adopt IIR could be remedied by IIR adoption by IPE jurisdictions, it provides no new incentives for IIR adoption in IPE jurisdictions. Consequently, UPE countries should also face no additional incentives for IIR adoption from the fear of "losing priority."

3. IIR adoption (dis)incentives in anticipation of QDMT and UTPR

Although the idea of the IIR originated from anti-deferral rules, since 2021, it has become increasingly problematic to interpret the IIR in terms of the policy justifications associated with these previous rules. This is for two reasons. First, anti-deferral rules are generally a response to—they

[43] This is a change from traditional anti-deferral (e.g. CFC) rules. In uncoordinated regimes, tax liability arising at an intermediate parent level from the application of anti-deferral rules would generally be creditable for a higher-level (e.g. ultimate) parent if the latter is also subject to anti-deferral rules. Effectively, therefore, the anti-deferral rules at the intermediate parent level have "priority".

[44] In other words, IIR non-adoption is a dominant strategy for the intermediate holding company jurisdiction: it is optimal both when the UPE jurisdiction adopts IIR and when the UPE jurisdiction does not adopt IIR.

presuppose—the fact that the foreign income of the taxpayers to whom the rules are applied are often taxed at a low rate. Second, anti-deferral rules also typically incorporate standard foreign tax credit (FTC) rules, which offer double taxation relief while taking the fact of source country taxation as given. By contrast, since the OECD's release of its Economic Impact Assessment of the Pillar Two Blueprint in 2020, and especially since the OECD October 2021 Statement, it has become increasingly common to assume that Pillar Two adoption will result in countries that previously taxed MNE operations at low rates raising their tax rates to the global minimum, either through general changes to the corporate income tax or through QDMT adoption.[45] In other words, as a consequence of Pillar Two adoption, the effective tax rates of many previously low-tax jurisdictions are generally expected to rise. Moreover, foreign taxes are no longer assumed as given: they specifically adjust to the FTC effectively granted by IIR countries.

Whether these expectations are correct in fact requires scrutiny (as Section IV will argue). But regardless of the soundness of such expectations, whether they are held by IIR adopters or not matters a lot to the interpretation of IIR adoption incentives. To begin with, if low-tax countries' tax policy responses are expected, IIR adoption may no longer raise revenue from MNEs' existing operations. If revenue is a key consideration—and it appears that many countries still take IIR's revenue potential to be an important, even if not the only, consideration[46]—then the anticipation of source (or haven) country tax rate increases creates *disincentives* for IIR adoption. Moreover, the relief of double taxation through FTC has traditionally been conceived of as a cooperative policy (albeit implemented unilaterally) that assumes that other countries do not act strategically to enact "soak-up" taxes. However, Pillar Two now envisions a cooperative policy that specifically encourages other parties to act opportunistically.

Most fundamentally, the idea that countries would adopt the IIR *only to subject their own MNEs to greater taxation in other countries* seems to conflict with any supposition that they try to maximize national income. IIR adoption looks like a kind of action that *puts money on the table* for other countries to take: one must better understand why, and which, countries would act this way.

Some commentators may have been inclined to rationalize IIR adoption in terms of traditional policy objectives by arguing that the direct revenue effect for the residence country is secondary. They may claim that the most important benefit of IIR is to get source countries to raise their tax rates, so as to create a floor to tax rate competition. Reduced tax competition would enable high-tax countries to further raise their tax rates, which would generate revenue, even if the IIR by itself does not directly generate revenue. However, such an interpretation of IIR adoption incentives is difficult to reconcile with the actual design of Pillar Two. For example, it has been pointed out that the 15% minimum tax rate is still substantially lower than the corporate tax rates of many UPE jurisdictions. Profit shifting incentives to low tax jurisdictions will therefore remain significant after Pillar Two is implemented. This

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[45] An increase in tax haven country rates to 15% is taken as an exogenous given in all economics models offered in the papers cited in supra note 9.

[46] Chris Hall, *Global tax accord could earn Canada up to $4.5 billion per year*, CBC (Oct. 16, 2022), https://www.cbc.ca/news/politics/chrystia-freeland-global-taxation-1.6213178; Stephanie Soong Johnston, *Singapore May Use OECD Tax Deal Revenue to Stay Competitive,* TAX NOTES (Mar. 3, 2022), https://www.taxnotes.com/tax-notes-today-international/corporate-taxation/singapore-may-use-oecd-tax-deal-revenue-stay-competitive/2022/03/03/7d7nb.

means that UPE countries' ability to further raise tax rates (and revenue) will be uncertain, whereas the loss of national income from the increased foreign taxation of their MNEs is much more certain.[47]

In short, if low-tax (source or haven) countries are expected generally to raise tax rates to the global minimum in response to IIR adoption, it would be difficult to rationalize IIR adoption on the basis of national income maximization. IIR adopters must embrace other policy objectives or principles.[48] Regardless of the precise nature of such alternative objectives, the point is that relatively unusual motivations must be invoked. This immediately raises a question similar to that considered in Section II.1 in relation to the ideological preference required for UTPR adoption, namely how widespread and strong such motivations are. Importantly, the answer to this question is also relevant to predicting how many low-tax countries would respond to IIR adoption. As Section IV discusses, QDMT is a rational response to IIR adoption if the goal of IIR adopters is to induce QDMT adoption. But if goal of potential IIR adopters is national income maximization, then QDMT adoption may not be the best strategy.

Finally, recall two findings from Section II: the UTPR-adopting country is likely not a national income maximizer (Section II.1); and IIR adoption could be a rational response to the UTPR if a country is national-income-maximizing, but it may not be if a country does not try to maximize national income (Section II.3). The first finding implies that no country will adopt UTPR opportunistically (i.e. simply because there is "money on the table"), therefore no country should fear the failure to adopt IIR would leave money on the table to UTPR adopters. The second finding, together with the arguments in this section, has two further implications. First, a UPE country that would respond to other countries' UTPR by adopting the IIR is unlikely to adopt the UTPR itself, and is also unlikely to adopt the IIR if it expects wide QDMT adoption. Second, countries that adopt both the UTPR and IIR are unlikely to be national income maximizers; they are also likely to engage in Pillar Two not in strategic reaction to other countries, but as leaders.

IV. Incentives for QDMT Adoption

The QDMT concept was not originally part of Pillar Two design, but appeared for the first time in the December 2021 Pillar Two Model Rules. Moreover, two types of QDMTs can be distinguished. QDMT I is imposed by a country on a domestic LTCE of an MNE with a foreign parent (Country Z in Section I). QDMT II is imposed by a UPE jurisdiction on any LTCEs it hosts, including both the UPE itself and other domestic subsidiaries (Country U in Section I).[49] Initial commentaries suggested that QDMT I adoption would represent a rational response to IIR and UTPR adoption by other countries,[50] and that QDMT II adoption may be a necessary response on the part of the UPE jurisdiction to UTPR adopted elsewhere.[51]

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[47] *See* Johannesen, *supra* note 9. Janeba & Schjelderup supra note 9 further argue that subsidy competition among high taxed countries may also eliminate any revenue gain from the new ability to raise tax rates brought about by a global tax rate floor.

[48] Some, for example, may see a commitment to the "single tax principle" as driving IIR adoption. See Reuven S. Avi-Yonah, *The Single Tax Principle* (May 27, 2022), https://ssrn.com/abstract=4121180 (

[49] A third type of domestic minimum tax, imposed by a country on purely domestic corporate groups that have no overseas operations, is also discussed and is reflected in the European Union's proposed directive for Pillar Two adoption. Such a tax is viewed as necessary for either QDMT I or QDMT II (or both) to be consistent with non-discrimination provisions under EU law. A domestic minimum tax on corporations was also proposed in the U.S. to achieve purely domestic policy objectives. Such a tax, however, is not a part of Pillar Two implementation.

[50] Noked, *supra* note 11; Devereux et al., *supra* note 11.

[51] Richard Rubin, *Global Tax Deal Would Undercut U.S. Tax Breaks, Businesses Warn,* THE WALL STREET JOURNAL (Feb.3, 2022).

1. QDMT I adoption in response to the IIR

QDMT I adoption has seemed to many a natural response to widespread IIR adoption. By imposing top-up taxes on MNEs in respect of their foreign LTCEs pursuant to the IIR, UPE countries that apply would neutralize the attractions of low tax countries that offer ETRs below 15%. Relative to the choice of leaving the UPE country to collect the top-up tax, the low tax countries would be better off collecting such top-up tax themselves, without the fear of losing any investment. While the OECD made the case for IIR adoption on the basis that it would induce low tax countries to raise source country tax rates generally, it now seems to accept that such countries may simply apply QDMT I to in-scope MNEs.

However, if the objective is to analyze strategic incentives for Pillar Two adoption—the exercise pursued in this paper—widespread IIR adoption itself should not be taken as given. Section III showed that if one starts at a point where the question of whether to adopt IIR is open, Pillar Two design does little in offering a definitive answer to that question.[52] But if only a few UPE countries adopt IIR, while other UPE countries refrain from doing so, a QDMT-I-adopter would risk losing, to QDMT-I-non-adopting countries, investments from all MNEs that hail from IIR-non-adopting countries. QDMT I adoption becomes rational only when sufficiently many UPE countries adopt the IIR.

Yet as discussed in Section III, the expectation of QDMT I adoption reduces the likelihood of IIR adoption among countries driven by the objective of national income maximization. Not only does QDMT I eliminate the direct revenue gain from IIR adoption, but if previously low-tax countries would act strategically to collect "soak-up taxes," they can also be predicted to pursue aggressive tax competition for investment from MNEs outside the scope of Pillar Two, as well as non-tax competition (perhaps even funded by revenue collected through QDMT I) for in-scope MNEs. Both would imply that the indirect revenue gain from IIR adoption would be highly uncertain. Therefore, QDMT I is rational to adopt if it is clear that IIR adopters are not national-income maximizers and instead deliberately wish to put money on the table. But if low-tax countries believe UPE countries are national-income maximizers, QDMT I adoption is not a safe strategy.

This conclusion may shed light on the striking fact that some of the apparent early movers in Pillar Two implementation are low tax countries (e.g. Ireland and Switzerland): by emphasizing their willingness to adopt QDMT I, they may be testing out UPE countries' commitments to a strategy that is not national-income maximizing.

It is not clear how this complex interaction between QDMT I and IIR would resolve itself. One possible intermediate outcome is that some low-tax countries are unable or unwilling to adopt QDMT I. This provides revenue-based incentives for enough UPE countries to adopt the IIR, which in turns leads some low-tax countries to adopt QDMT I in response. Meanwhile, MNEs from UPE countries that do not adopt IIR still find the non-QDMT-adopting countries to be attractive locations. Consequently, both IIR and QDMT adoption remains partial.

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[52] Contrast this with the reasoning in Devereux et al., *supra* note 11 ("a country can introduce a QDMTT *in the safe knowledge* that…the top-up tax would be collected by another country if it is not collected through the QDMTT" (emphasis added)).

2. QDMT I and II adoption in response to UTPR

Section II showed that because UTPR countries cannot generally reach the profit of LTCEs in other countries, it is an illusion that the failure to adopt QDMT I would “leave money on the table” to UTPR-adopting countries. Instead, it often would be irrational for a low tax country to respond to the UTPR adoption elsewhere by adopting QDMT I: this is especially the case if the country hosts many low-elasticity investments and many MNEs not exposed to the UTPR. Further, if QDMT I is used to fund disguised tax competition or equivalent subsidy competition, it may frustrate the original purpose of UTPR adoption for some countries, and thus may diminish the likelihood of UTPR adoption. And if not many countries can be expected to adopt UTPR in the first place, incentives for QDMT I adoption generated by UTPR is also limited.

Similarly, Section II showed that the adoption of QDMT II by a UPE country is not compelled by UTPR adoption in other countries. In many cases, investments in the UPE country may be rather inelastic, and MNEs may well prefer $1 of tax benefit in the UPE country to a $ 1 reduction in the tax penalty imposed in the UTPR country. Moreover, if a UPE country is large (e.g. the U.S. or China), it may not even be feasible for UTPR-imposing countries to collect all the top-up tax associated with LTCEs in the UPE countries. In all of these circumstances, it seems more rational for the UPE countries to persuade the potential UTPR-adopter countries of the futility of such adoption, than to enact QDMT II in reaction to UTPR.[53]

V. Cooperative Explanations of Pillar Two Adoption

So far, we have considered strategic incentives for Pillar Two adoption. As should be clear from the previous sections, what marks decisions as strategic is the fact that actors take other parties’ actions as given in making their own decisions, not the assumption that actors are motivated by what are conventionally conceived as “self-interested” preferences (such as national income maximization). Even allowing diverse motivations, however, it seems difficult to find support for the claim that Pillar Two’s design enhances the likelihood of its adoption by triggering strategic incentives. A major problem is that Pillar Two seems to make inconsistent assumptions as to when countries act on the basis of non-income-maximizing objectives. For example, UTPR-adopting countries must be non-income-maximizing, but they are supposed to expect others to respond to the UTPR in an income-maximizing manner. Likewise, countries expecting other countries to be income-maximizing would only adopt the IIR if they themselves are not income-maximizing. And income-maximizing countries would adopt the QDMT only after ascertaining that other countries are not income-maximizing.

But beyond these inconsistent implicit assumptions about countries’ preferences, the OECD’s depiction of Pillar Two—in the Pillar Two Blueprint, Pillar Two Model Rules and its Commentary, and more generally in its pronouncements about the GLoBE rules—displays a more obvious inconsistency, or

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[53] The adoption of the third type of domestic minimum tax, *see supra* note 49, faces the following argument. Countries always have the choice of taxing their purely domestic corporations more. The fact that they do not so may be taken as some evidence that it may not be optimal for them to do so. If this is the case, it would not be rational for them to enact a purely domestic minimum tax just so that they can enact QDMT I and QDMT II while satisfying existing international obligations regarding non-discrimination. If such obligations are truly binding, they are more likely to diminish the adoption probabilities of QDMT I and QDMT II, rather than increase the adoption probabilities of a purely domestic minimum tax.

deliberate ambiguity. This is an inconsistency or ambiguity about whether countries are acting strategically or cooperatively under Pillar Two.

In many ways, and especially up to the point of OECD October 2021 Statement, the discourse around Pillar Two takes special pains to create a semblance of broad international cooperation, by depicting actions naturally described as strategic in terms of cooperation instead. For example, a basic premise of Pillar Two is that countries would apply IIRs on an orderly basis: UPE countries get to apply them first, IPE countries next, and so on. But this ordering is arguably artificial. IPE jurisdictions have always had the option to adopt IIR-like rules unilaterally (and would enjoy de facto priority in doing so), but may have self-interested reasons not to adopt. Pillar Two is apt to portray such choice as acknowledging UPE countries' priority, rather than strategic non-adoption.[54] Even more obviously, source countries' decisions to raise income taxes in response to residence countries' foreign tax credit regimes have always been understood (disfavored) as a form of strategic action. Since late 2021, however, Pillar Two explicitly counts the adoption of QDMT as a form of cooperative action.

Perhaps the clearest example of Pillar Two's equivocation about what counts as cooperation is its characterization of the GloBE rules as describing a "common approach": countries are not required to adopt the rules, but "if they choose to do so, they will implement and administer the rules in a way that is consistent with the outcomes provided for under Pillar Two, including in light of model rules and guidance." This statement has been widely repeated, but it is almost tautological: what would it mean for a country to adopt rules sufficiently dissimilar from the OECD's model but still adopting the "OECD's" rules?[55] Under this formulation, it is hard to see how countries can *fail* to follow the "common approach": they would always be treated by the OECD as cooperating.

But the OECD's pitch of Pillar Two as a cooperative endeavor seems to have shifted after its October 2021 Statement.[56] In pressuring countries to adopt Pillar Two in 2022, the designers of Pillar Two, whether at the OECD, European Union or the United States, increasingly argue that countries that fail to adopt Pillar Two would lose out to countries that adopt: only adoption is strategically optimal. The narrative that countries should adopt the GLoBE rules as a defensive measure to fend off other countries' predation on their tax bases has come to dominate. This directly contradicts standard understandings of cooperation, according to which *all* would gain from cooperation, and *all* would lose from non-cooperation.[57]

If the previous sections are correct that there is no coherent set of strategic incentives that would lead to widespread Pillar Two adoption, one should be distrustful of this new turn in the OECD's characterization of the proposed global tax agreement. But questioning a prevalent account about the incentives for Pillar Two adoption is not the same as predicting the course of Pillar Two (non-)adoption.

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[54] Similarly, UPE countries could always have enacted IIR-like rules unilaterally (the U.S. GILTI being a most salient recent example), but Pillar Two depicts the adoption of such rules as acts of cooperation.
[55] In addition, countries would "accept the application of the GloBE rules applied by [others] including agreement as to rule order and the application of any agreed safe harbours." This notion of "acceptance" of other countries' adoption is also vacuous. Countries either have legal remedies against other countries' adoption of GloBE-like rules or they don't. If there are legal remedies (such as claims under existing tax treaties), there is no evidence that countries have committed to foregoing such remedies in any court of law. If there are no legal remedies, what would "acceptance" mean?
[56] As suggested in Section II.4, this earlier pitch may have been so successful that even its critics have fallen for the illusion that countries have gained access to new tax bases under the UTPR.
[57] Cui, supra note *7*.

Many commentators on Pillar Two, after all, may truly believe (or at least more so than the designers of Pillar Two themselves) that countries are coming together to support a new international regime, not strategically out of the desire to defend their own self-interests, but cooperatively to advance nations' common interests. If countries are genuinely acting cooperatively (again, more so than is implied by the OECD's equivocations), an analytical framework in which countries are motivated only by strategic considerations will likely have poor predictive power.

This brings us to the question of how best to explain the political agreement that 136 nations are said to have reached in October 2021—whether that agreement in itself offers decisive evidence against the view that countries act mainly strategically in approaching the new global tax agreement. It is actually not hard to imagine that the delegates from many of the participating countries in the OECD's Inclusive Framework were inclined to behave cooperatively, instead of focusing exclusively on national self-interests. Many delegates, being bureaucrats from finance ministries and tax administrations, may have perceived Pillar Two's main goal to be raising taxes in MNEs. Such a project could both directly result in revenue gains for some countries and indirectly lend legitimacy to future domestic tax increases—outcomes that hold common appeal to the professional and career interests of the delegates. It may also have been difficult to distinguish the goals of the Inclusive Framework from other mundane goals of OECD tax meetings, such as the provision of technical training to developing countries.[58] All these could discourage a focus on national self-interest.

Nor is this kind of phenomenon—national delegates acting in a cooperative fashion in setting international tax norms, in seeming disregard of national self-interest—unprecedented. The drafting of model tax conventions at the League of Nations in the 1920s can be viewed in the same light. At the League of Nations,[59] delegates comprising tax specialists and academics, acting in their personal capacities, debated about various ways of relieving double taxation and their relations to principles of inter-nation equity, seemingly in abstraction not only from the self-interest of particular nations but also from the facts that many of the countries they hailed from were only just beginning to collect income taxes, had not yet begun to tax corporations, and faced little political pressure to solve the problem of double taxation. Equitable solutions to the double taxation problem were memorialized without much attention to what specific tax instruments they would be applied to. This, however, has not prevented the work of the League of Nations from being viewed as laying the foundations of the architecture of 20th century international taxation. If one believes in such origin attributions, there is no reason to think that delegates to the Inclusive Framework cannot build a new international tax architecture in a similar cooperative fashion.

At the present, the main question is whether delegate behaviors at the Inclusive Framework—even if they were more properly characterized as cooperative rather than strategic—will be predictive of government decisions in the current stage of Pillar Two implementation. The historical parallel to this question is whether one could have predicted the actual negotiations of the global bilateral tax treaty network from the model conventions drafted by the League of Nations. Unfortunately, international tax scholarship—whether legal, economic, or historical—still sheds little light on these questions.

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[58] See Nana Ama Sarfo and Stephanie Soong Johnston, *A New World Tax Order: The Inclusive Framework and Its Future*, 104 TAX NOTES INTERNATIONAL 975 (November 29, 2021). This and other reports of activities at the Inclusive Framework suggest a high degree of informality in the OECD Inclusive Framework discussions that is difficult to reconcile with the supposition that countries were negotiating towards binding outcomes.

[59] See generally SUNITA JOGARAJAN, DOUBLE TAXATION AND THE LEAGUE OF NATIONS (2018); Michael J. Graetz & Michael M. O'Hear, *The "Original Intent" of U.S. International Taxation*, 46 DUKE L. J. 1021 (1997).