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Policy Brief

Global Minimum Tax: Policy Impact on Investment Promotion and Incentives in ASEAN Member States

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Key Messages:

- The Global Minimum Tax (GMT) aims to address base erosion and profit shifting by multinational enterprises. As of 28 May 2024, 147 jurisdictions, including seven Association of Southeast Asian Nations (ASEAN) Member States, have agreed to the Organisation for Economic Co-operation and Development (OECD)/Group of Twenty (G20) Inclusive Framework.
- The GMT imposes a minimum corporate income tax rate of 15% on multinational enterprises with revenues above €750 million. This policy will impact ASEAN Member States, which have varied corporate tax rates and rely heavily on tax incentives to attract foreign direct investment.
- ASEAN Member States may need to explore outcome-based deductions or incentives, such as research and development grants, infrastructure reimbursement, and cost-based incentives, to maintain competitiveness.
- Effective implementation and administration of the GMT will also be crucial.

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The Association of Southeast Asian Nations (ASEAN) Member States are some of the most important foreign direct investment destinations in the world. Investment in ASEAN Member States covers all four pillars of investment typology: natural resources, market-seeking, export oriented, and strategic assets. Key sectors – such as semiconductors, tourism, consumer products, e-commerce, banking, and commodities (e.g. nickel) – are expected to benefit from this trend. Many of the investors in ASEAN are multinational enterprises, and multinational enterprises earning €750 million or more in two of the four fiscal years, are now subject to the Global Minimum Tax (GMT) in more than 140 jurisdictions around the world. With the introduction of the GMT, ASEAN Member States must rethink their incentives and investment promotion strategies to maintain their competitive edge over other foreign direct investment destinations around the globe.

1. Introduction

The Global Minimum Tax (GMT) is a significant policy initiative aimed at addressing the challenges of tax competition and profit shifting by multinational enterprises (MNEs). This policy has far-reaching implications for investment promotion and incentives in the Association of Southeast Asian Nations (ASEAN) Member States (AMS). The GMT, set at a minimum rate of 15%, seeks to ensure that MNEs pay a fair share of taxes in the jurisdictions where they generate revenues, reducing the incentive for profit shifting to low-tax countries.

The GMT presents both opportunities and challenges for investment promotion in AMS. Firstly, the policy aims to create a more level playing field by discouraging MNEs from shifting profits to low-tax countries, thereby ensuring that countries with higher tax rates are not disadvantaged. This could lead to a more stable and sustainable tax environment, which is essential for long-term investment planning (VEPR et al., 2020).

Secondly, investment promotion could be increasingly challenging in the short term (ASEAN Finance Ministers and Central Bank Governors, 2023). The imposition of a minimum tax rate could make certain jurisdictions less attractive for investment, particularly those with lower tax rates (Ardin, 2023). This could lead to a reduction in foreign direct investment (FDI) in countries that have historically relied on tax incentives to attract investment (DBS, 2021). For example, Indonesia, which has relied heavily on tax holidays and other incentives to attract FDI, may see a decline in investment with the reduction of the effectiveness of these incentives (Ardin, 2023).

Thirdly, the GMT could create a significant shift in the investment landscape, with MNEs re-evaluating their operational structures to comply with the new tax regime. This could lead to a reallocation of investment away from low-tax countries and towards countries with more favourable tax environments.

Fourthly, the GMT could lead to a reduction in tax revenues for countries that have historically relied on tax incentives to attract investment, without any counterbalance tax measures such as the Qualified Domestic Minimum Top-up Tax Mechanism. Some studies suggests that this could lead to significant implications for government budgets and the ability of governments to fund essential services and infrastructure projects. For instance, the loss of tax revenue could hinder the ability of governments to invest in critical infrastructure, such as ports and special economic zones, which are essential for attracting and retaining investment (DBS, 2021). However, this requires further study, especially after the implementation of the GMT in certain AMS.

2. Global Minimum Tax

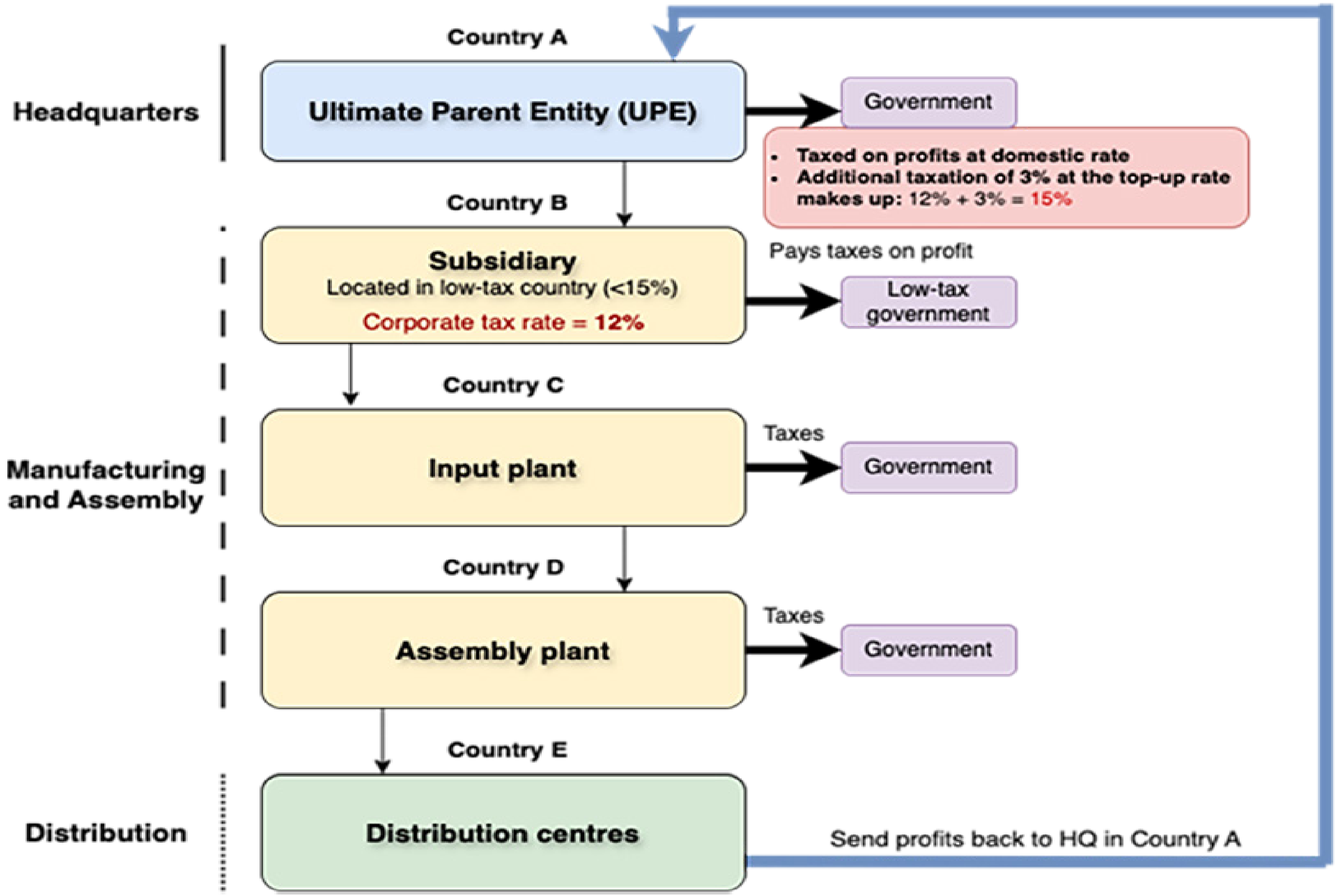
The GMT is also known as Pillar Two of the framework on Global Anti-Base Erosion Model Rules (GloBE), published by the Organisation for Economic Co-operation and Development (OECD) and the Group of Twenty (G20) in January 2020. The main purpose of GloBE is to address base erosion and profit shifting amongst many MNEs, as shown in Figure 1. As of 28 May 2024, 147 jurisdictions have agreed to the OECD/G20 Inclusive Framework on base erosion and profit shifting (OECD, 2024a), including seven AMS (Brunei Darussalam, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam).

The Inclusive Framework was followed by the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (BEPS MLI). The OECD and the G20 concluded the Multilateral Convention to Facilitate the Implementation of the Pillar Two Subject to the Tax Rule (STTR MLI) in September 2023. As of 24 June 2024, 103 jurisdictions have signed and ratified the MLI, including five AMS (Indonesia, Malaysia, Singapore, Thailand, and Viet Nam) (OECD, 2024c). However, the United States remained outside the GloBE system.

The GloBE Pillar 2 rules apply only to MNEs with revenue of €750 million or more. GloBE mandates a minimum corporate income tax rate of 15%. The GMT is calculated using a jurisdictional blending approach, rather than being confined to a single jurisdiction. Under the GloBE framework, jurisdictions participating in the arrangements may impose a top-up tax to bridge the gap where other jurisdictions apply a lower tax rate. For example, if Country A imposes a corporate tax rate of 10% or 0% due to incentives, Country B may apply a top-up tax to raise the effective rate to the minimum level. The ultimate parent entity (UPE) is responsible for ensuring the 15% GMT is paid. If the UPE is located outside a GMT jurisdiction, its subsidiary within the GMT jurisdiction becomes responsible for paying the minimum tax.

Calculation is based on 2 of the 4 years preceding the tested year. So, for example, assuming that country A imposes the GMT in 2025, it must work backwards 4 years towards 2021. In those 4 years, country A must work on the 2-year average where the minimum revenue of the MNE concerned is €750 million and above. Hence, each country has to adopt a tracing mechanism to trace the revenue and the UPE of each MNE investing or operating in

Figure 1: Avoidance of MNEs Shifting Profits to Low-Tax Countries and Territories



HQ = headquarters, MNE = multinational enterprise.
Source: Author's analysis, based on Djankov and Hufbauer (2021).

the country. Tracking is easier on MNEs listed on stock exchanges by examining their annual reports and consolidated group accounts. However, some MNEs are privately owned, making it more difficult to identify the UPEs, while others are based in tax havens.

Some organisations are excluded from the GMT (Figure 2), including government bodies such as sovereign wealth funds, international or non-profit organisations such as pension funds, insurance companies, international shipping companies, and real estate funds. However, MNEs that hold this kind of investment funds or real estate funds may not be excluded from the GMT.

3. Corporate Income Taxes in AMS

ASEAN has been one of the most attractive investment destinations in the world. Although more than half of the FDI to ASEAN goes to Singapore, investment in other AMS such as Indonesia and Viet Nam is also growing (Figure 3).

All AMS utilise fiscal incentives such as tax exemptions or tax holidays to attract FDI. Hence, the total tax collection revenue as a percentage of gross domestic product (GDP) in AMS is generally lower than the Asia-Pacific or OECD average (Figure 4).

Figure 2: Exclusion from GMT

Liable

- UPE, which is not controlled by another entity
- Based on financial accounts; applying IFRS or equivalent accounting norms
- Consolidated groups (companies and branches outside parent jurisdiction)
- All entities normally covered in the consolidated accounts of UPE
- EU will include purely domestic groups

Excluded

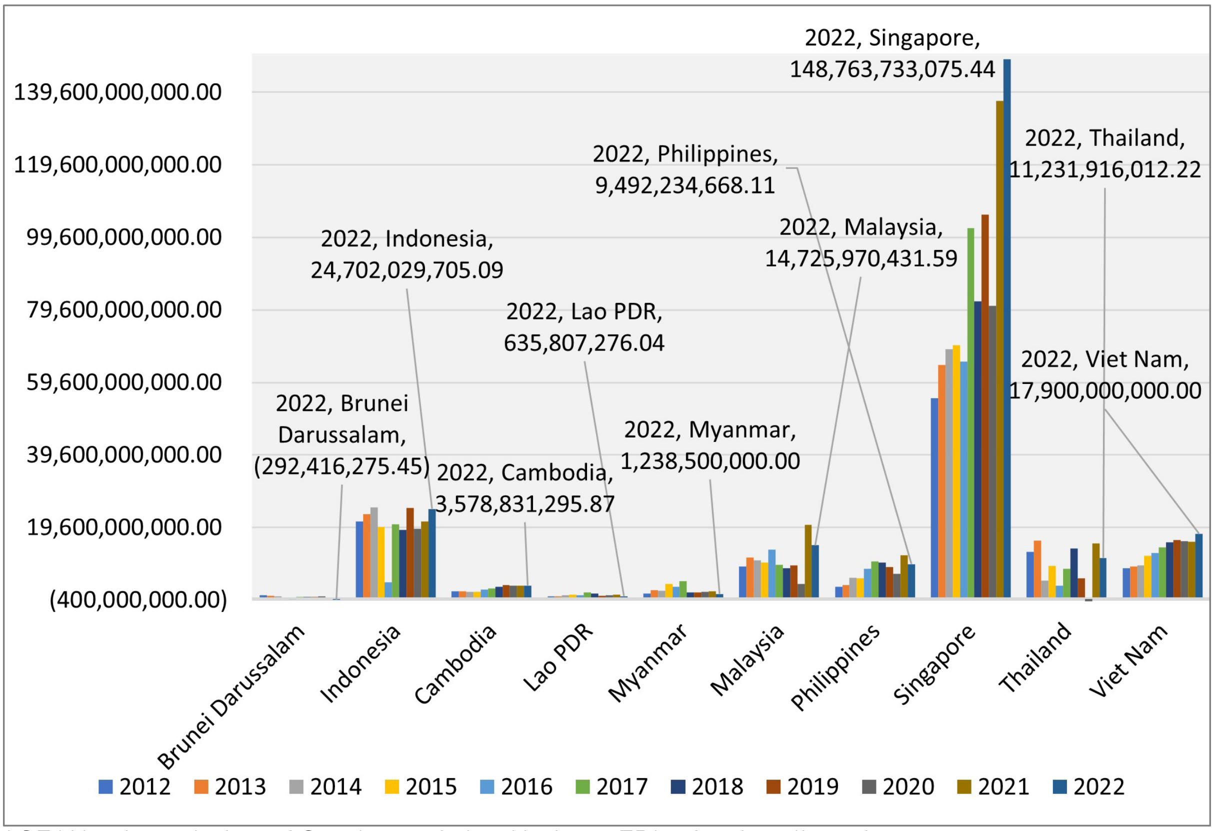
- Government bodies (e.g. sovereign wealth funds)
- International or non-profit organisations
- Pension funds and insurance companies
- International shipping income
- Investment funds and real estate funds are excluded if they are at the top of the ownership chain (i.e. UPE)
- Maintain tax neutrality
- Do often not prepare consolidated accounts
- Taxation at investor level
- But MNE held by fund may be a non-excluded entity

EU = European Union, GMT = Global Minimum Tax, IFRS = International Financial Reporting Standards, MNE = multinational enterprise, UPE = ultimate parent entity.

Source: Authors' analysis.

Figure 3: FDI Inflows to ASEAN, 2012–2022

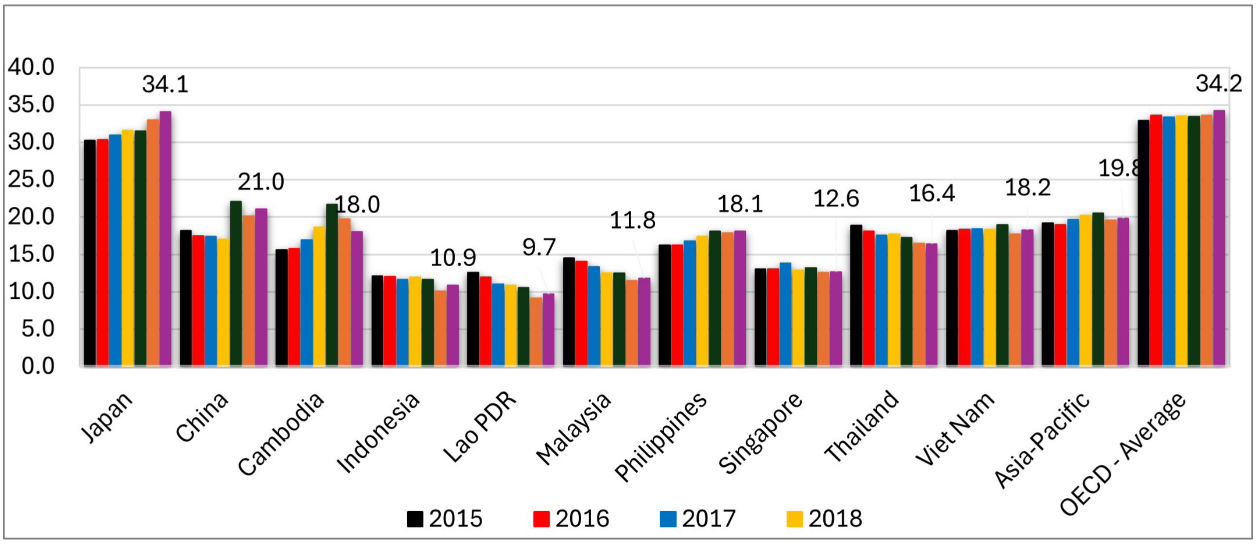
(US$)



ASEAN = Association of Southeast Asian Nations, FDI = foreign direct investment.

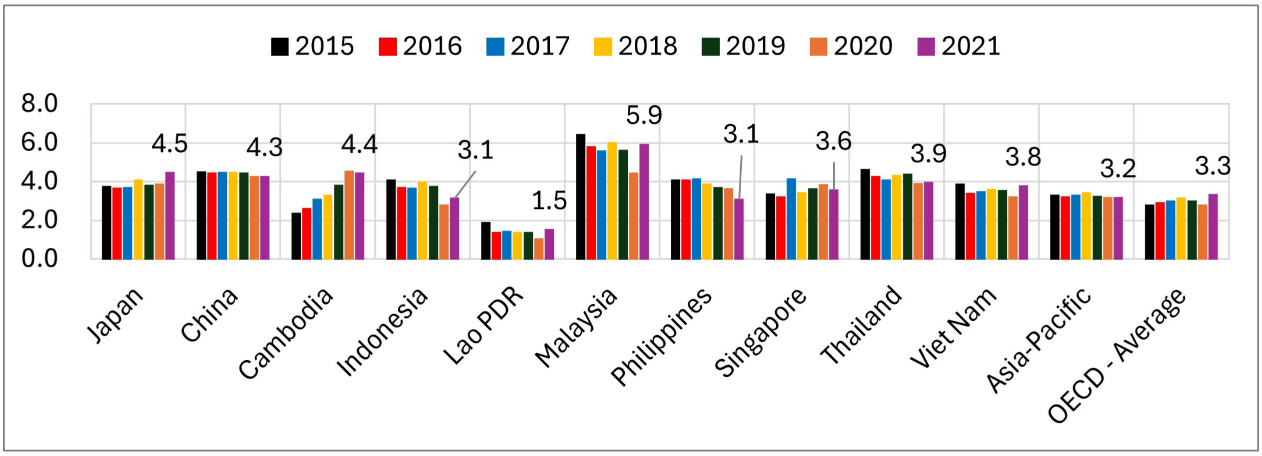
Source: UNCTAD (2023).

Figure 4: Tax Collection as a Percentage of GDP, ASEAN Member States



ASEAN = Association of Southeast Asian Nations, GDP = gross domestic product, OECD = Organisation for Economic Co-operation and Development.
Source: OECD (2024b).

Figure 5: Taxes on Income, Profits, and Capital Gains as a Percentage of GDP



ASEAN = Association of Southeast Asian Nations, GDP = gross domestic product, OECD = Organisation for Economic Co-operation and Development.
Note: No data for Brunei or Myanmar.
Source: OECD (2024b).

The tax revenue collection of the Lao People's Democratic Republic (Lao PDR) is about 9.7% of GDP, compared with 10.9% in Indonesia and 11.8% in Malaysia. Cambodia, the Philippines, Singapore, Thailand, and Viet Nam collected higher taxes than Indonesia, Lao PDR, and Malaysia, but still below the Asia-Pacific average of 19.8% and the OECD average of 34.2%.

In terms of corporate tax performance in ASEAN, Malaysia has the highest percentage, at 5.9% of GDP, followed by Cambodia at 4.4%, Thailand at 3.9%, Viet Nam at 3.8%, Singapore at 3.6%, Indonesia at 3.1%, and Lao PDR at 1.5% (Figure 5). In terms of income tax rate, Singapore charges the lowest corporate tax rate at 17%, followed by Brunei at 18.5%, Indonesia at 22%, Malaysia at 24%, and the Philippines at 25%.

4. GMT and the Implications on Investment Promotion and Incentives in ASEAN Member States

Taxation is purely within the purview of the national jurisdiction of each AMS. The same applies to investment promotion activities and investment incentives, which are covered under the national laws and policies of each Member State. Although investment promotion is one of the four pillars of the ASEAN Comprehensive Investment Agreement (ACIA), it is limited to cross-linking the websites of investment agencies in ASEAN, enhancing production networks and industrial complementation, and organising joint investment missions as well as briefings and seminars on investment opportunities and policies.[1]

Many countries utilise fiscal incentives such as tax holidays in attracting FDI. However, low taxes are not necessarily the first in the list of preferences or priorities for investment decision makers (World Bank, 2020). Investors mainly look for talent and skills, microeconomic stability, political stability, and legal and regulatory environments (World Bank, 2020).

Furthermore, GMT policy limits the scope of tax incentives. While GMT applies to certain UPEs, it does not prevent AMS from offering differentiated incentives to entities below the GMT threshold. Therefore, AMS may choose to set a 15% corporate tax rate universally or allow investors not subject to GMT to benefit from more favorable incentives. Taxation issues remain within the national jurisdiction of each AMS, as international investment agreements generally exclude taxation policies from their scope. For example, the ACIA, under Article 3.4, specifically excludes the application of the agreement to any taxation measures, except transfers of funds and expropriation and compensation, and subsidies or grants provided by a Member State.

Apart from the tax incentives, AMS may explore other options, through outcome-based incentives or tax credits, such as providing research and development grants, as well as alternative tax measures for foreign direct investors in new technologies related to climate FDI, semiconductors, electric vehicles, and artificial intelligence. AMS need to be mindful in providing grants as they may be classified as 'state aid', which is a sensitive issue as it can be categorised as subsidies, which may run afoul of World Trade Organization agreements.

Other options include providing reimbursement for infrastructure works, such as last-mile infrastructure to investors' locations; and lowering the rate of direct taxes such as value-added tax. AMS may also explore providing more generous tax deductions or cost-based incentives. These are normal deductions in the tax system, including accelerated depreciation and additional tax deductions. AMS could also provide incentives for investors in specific/priority sectors that are labour/capital intensive, or compensation for investors in special economic zones/regions for recovering losses incurred in the initial stages of operations (Medina, 2023).

Apart from exploring incentive options, AMS need to address the administration of the GMT. One requirement, as discussed above, is the need to track the MNEs falling under the GMT threshold. Some MNEs may look into restructuring, e.g. through spinoffs of some of their entities, retaining a minimum percentage of ownership, or starting new businesses elsewhere.

In terms of promotion, AMS may need to be more creative. They may need to identify promoted sectors and link them to potential investors. Promotional activities must be followed by efficient and effective investment facilitation. Investors require strong support from various levels of government, such as simplified entry requirements, investment implementation support, regulatory transparency, and efficient infrastructure.

5. Implementation of the GMT by ASEAN and Alternatives to Attract FDI

Several ASEAN Member States, including Malaysia, Singapore, Thailand, and Viet Nam, have made strides to implement GMT within their domestic tax systems:

[1] The main objective of the ACIA is to create a free and open investment regime in ASEAN, based on international best practices. The ACIA was signed on 26 February 2009, entered into force on 29 March 2012, and was subject to further amendments.

- Malaysia introduced GMT through Part XI of the Income Tax Act 1967, establishing GloBE rules and a Domestic Top-Up Tax (DTT) effective from 1 January 2025.
- Viet Nam enacted GMT through Resolution No. 39/2023/UBTVQH15, applying additional corporate income tax in line with global anti-base erosion rules, effective 1 January 2024.
- Singapore introduced the Multinational Enterprise (Minimum Tax) Bill 2024 in Parliament on 9 September 2024, to introduce a domestic top-up tax, with debate expected in the next parliamentary session.
- Thailand published draft legislation to adopt GloBE on 1 March 2024.

Under Malaysia's Income Tax Act, Part XI applies to Malaysian corporate entities, including Labuan entities, that are part of MNEs meeting the GMT threshold in at least two of the four preceding financial years. Part XI defines an MNE group as any group including at least one entity or permanent establishment outside the UPE's jurisdiction. Entities within the scope of GloBE must file an information return and Top-Up Tax return, along with maintaining relevant records.

Certain entities are excluded from this definition in Malaysia, such as government entities, international organisations, non-profits, pension funds, UPE investment funds, UPE real estate investment vehicles, and entities that are at least 85%–95% owned by one or more excluded entities, apart from pension services.

Under Malaysian tax law, the DTT applies to a low-taxed corporate entity in Malaysia if its jurisdictional effective tax rate is below 15%. The Multinational Top-Up Tax (MTT) applies to the UPE in Malaysia for its low-taxed corporate entities in other jurisdictions with effective tax rates below 15%. Additionally, Malaysia's law includes a de minimis exclusion: MTT is deemed zero if the average GloBE revenue in a jurisdiction is under €10 million or the average GloBE income or loss is under €1 million. MTT for safe harbour jurisdictions is also deemed zero if the jurisdiction qualifies for GloBE safe harbour under the GloBE Implementation framework.

The GMT has reduced reliance on tax holidays as a primary tool to attract FDI. Therefore, AMS must refocus on factors that more directly impact investor decisions, such as macroeconomic and political stability, talent development and availability, competitive labor costs, rule of law, transparency, and robust physical and digital infrastructure. Additionally, AMS should strengthen their tax administration systems to enhance tax governance and address any system loopholes effectively.

6. Conclusion

This policy brief has shown that the GMT is only applicable to MNEs with revenue over €750 million, calculated over the 2 years preceding the year of the assessment. The GMT is not applicable to certain types of investors, such as government-owned investors and MNEs earning less than €750 million. Hence, AMS may need to explore options beyond tax incentives to promote and attract MNEs falling under the GMT thresholds. AMS could offer tailor-made non-fiscal incentives and grants, while enhancing talent development, reducing the cost of doing business through reduced regulatory burdens, and providing an efficient investment facilitation system.

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