Briefing

International review for October

Speed read

In October, the number of jurisdictions backing a framework for international tax reform reached 136, with all OECD, G20 and EU members (except Cyprus) joining the latest statement. The way should now be clear for the widespread adoption of the two-pillar plan in all major economies. There were some refinements to the position set out in July's statement, with the amount of residual profit to be reallocated to market jurisdictions under pillar one narrowed down to 25% and the pillar two global minimum tax rate set at 15%. In the EU, the Public Country-by-Country Reporting Directive looks set to soon enter into force, with adoption by the European Parliament set to take place imminently. There are also plans to overhaul EU withholding tax procedures, with the European Commission publishing a roadmap on a proposed new EU-wide system to avoid double taxation. Finally, Austria is set to reduce the corporation tax rate incrementally to 23%, funded by a new carbon levy.

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Progress on BEPS 2.0

Tax was very much in the spotlight in October, as previous holdouts Estonia, Hungary and Ireland signed up to the principles of the OECD/G20's BEPS 2.0 programme to address the tax challenges arising from the digitalisation of the economy. All OECD, G20, and EU members (except for Cyprus, which is not an Inclusive Framework (IF) member) have now joined the agreement, paving the way for wide-spread adoption in all major economies. At the time of writing, 136 OECD/G20 IF members in total had backed the two-pillar plan.

On 8 October 2021, these 136 member jurisdictions approved a new statement which updated a previous IF statement from July, providing some additional details on the two pillars and a detailed implementation plan. However, the work is not yet done, and a number of technical details need resolving before the plan is ready for implementation.

Pillar one: allocation of taxing rights

Pillar one reallocates a proportion of the residual profit (profit in excess of 10% of revenue) of the very largest multinational enterprises (MNEs) between their market jurisdictions (Amount A).

It is anticipated that under pillar one, taxing rights on over $125bn will be reallocated to market jurisdictions per year.

In line with the July statement, MNEs within scope of Amount A will be those with global turnover above €20bn and profit before tax of above 10% of revenue. The turnover threshold will be reduced to €10bn after seven years contingent on successful implementation of Amount A.

Per the October statement, whether or not an MNE meets these thresholds will be determined through an averaging mechanism. Whilst no further detail is given on how the averaging mechanism will work, it is not unreasonable to assume that this will involve taking an average of the MNE's revenue and profit before tax over a set number of years to ensure that an MNE does not fall into or out of the scope of Amount A due to an anomalous result.

When it comes to how much profit will be reallocated to market jurisdictions, the October statement settles on 25% of the MNE's residual profit. Previously, a range of 20 to 30% had been given, with different jurisdictions pushing for the higher and lower ends of the range. Landing on 25% was likely a compromise, with many developing countries likely to have preferred a number nearer the top of the range to maximise the profits available for reallocation.

Meanwhile, work continues on Amount B (the standardised return for 'baseline' marketing and distribution activities) and in line with the July statement is scheduled to be finalised by the end of 2022.

The end of unilateral DSTs?

By approving the statement, the 136 member jurisdictions have committed to remove all Digital Services Taxes (DSTs) and 'other relevant similar measures' and to not introduce such measures in the future. The definition of 'relevant similar measures' will be finalised as part of the adoption of the multilateral convention and explanatory statement.

The October statement adds that no newly enacted DSTs or other relevant similar measures are to be imposed on any company from the date of the latest statement, 8 October 2021.

Nevertheless, some jurisdictions are pressing ahead with their unilateral DSTs, to ensure that digitalised businesses are appropriately taxed in the event that the global agreement is delayed or does not come to fruition.

Canada's finance minister is proceeding with plans for a domestic DST, which would levy a 3% tax on the revenues of digital giants. However, the proposed implementation date has been delayed from 1 January 2022 to 1 January 2024 with the hope that the OECD agreement will come into effect before then. If the global reforms have not yet taken effect, the levy will become payable in 2024 in respect of revenues earned from 1 January 2022.

The requirement to remove all unilateral DSTs and similar measures is not popular with all member jurisdictions. Argentina's economy minister has said that developing countries have been 'forced to choose between something bad, and something worse,' with the Secretary of Finance adding that the benefits seen from the two-pillar proposal are unlikely to make up for the commitments, such as the removal of DSTs, that developing countries have had to make.

Pillar two: certainty on global minimum taxation

Pillar two provides a global minimum tax regime through the new global anti-base erosion rules (GloBE) rules.

The GloBE rules comprise (i) an income inclusion rule (IIR), which imposes a top-up tax on a parent entity in respect of the low taxed income of its constituent entity; and (ii) an undertaxed payment rule (UTPR) which denies deductions or requires an equivalent adjustment to the extent the low tax income of a constituent entity is not subject to tax under an IIR.

The October statements confirms that the minimum tax rate for the purposes of both the IIR and UTPR will be 15%. This marks a small yet notable change to the July statement which included a minimum tax rate of 'at least' 15%.

'At least' had been a particular sticking point for Ireland, one of the key holdout jurisdictions. With many jurisdictions favouring a higher minimum tax rate than 15%, Ireland's

concern was that these two words would leave the door open to future increases to the minimum rate. Dropping the phrase has allowed Ireland to accept the deal.

Ireland's minister for finance confirmed in his speech at the Irish Budget 2022 on 12 October 2021 that Ireland would apply the 15% minimum rate when the global deal comes into effect. The current 12.5% rate will continue to apply for businesses with revenues less than €750m. It will be interesting to see what approach other jurisdictions with relatively low corporate tax rates, or generous incentives, such as Singapore, will take now that the minimum rate has been finalised.

Spain's coalition government has agreed on a budget proposal for the 2022 Budget which would introduce a new corporate tax floor of 15% for large businesses. This is one approach that we could see more of following the latest statement. Jurisdictions might also decide to move tax incentives 'above the line' so that they have less impact on the accounting effective tax rate and therefore do not give minimum tax problems.

According to the October OECD/G20 IF statement it continues to be the intention that the GloBE rules will co-exist with the US global intangible low-taxed income (GILTI) regime. However, the statement does not comment on their interaction with the US base erosion and anti-abuse tax (BEAT) regime, which as things stand is inconsistent with the pillar two agreement. Current proposals to amend the BEAT regime, or implement Biden's proposed alternative 'SHIELD', could provide the US Treasury with an opportunity to go some way in reconciling the two, but key differences in their mechanics and thresholds would remain.

Implementation of the pillars

The detailed implementation plan published as an annex to the October statement confirms that Amount A is to be implemented through a multilateral convention to come into effect in 2023. Model rules for domestic legislation to give effect to Amount A will be developed by early 2022.

Meanwhile, model rules giving effect to the GloBE rules, setting out their scope and mechanics, are to be developed by the end of November 2021, with an implementation framework to facilitate their coordinated implementation ready by the end of 2022 at the latest.

Whilst significant progress has been made on the pillars to date, it seems there is still plenty more to do and the hard work is far from over.

EU public country-by-country reporting

The EU's public country-by-country reporting (CbCR) Directive has been several years in the making and looks set to finally enter into force later this year.

On 28 September, the Competitiveness configuration (COMPET) of the Council of the EU adopted the European Council's position based on a qualified majority, with 21 votes in favour, two against (Cyprus and Sweden) and four abstentions. The European Parliament is expected to adopt the position before the end of this month.

The Directive will require multinational groups (both EU and non-EU headquartered) with total consolidated group revenue of at least €750m to publish certain tax, financial and functional information on a country-by-country basis for each EU member state that the group is active in, as well as for countries on the EU lists of non-cooperative and monitored jurisdictions. Businesses should ensure they know what information they will need to disclose and how, and factor in enough time for any additional compliance burden that arises.

Following adoption by the European Parliament, the Public CbCR Directive will be published in the *Official Journal of the European Union*, entering into force 20 days after its publication. EU member states will then have 18 months to transpose the Directive into national law. The rules could therefore become applicable from as soon as mid-2024 with first reporting potentially in 2025.

Businesses should monitor further developments closely on a jurisdiction by jurisdiction basis as some member states may choose to implement the rules before the 18-month deadline, resulting in earlier first reporting.

A new EU withholding tax system?

Sticking with the EU, on 28 September 2021 the European Commission published a roadmap for a new EU system to avoid double taxation. Inefficient withholding tax procedures are seen by the Commission as one of the remaining barriers to cross-border investment, estimated to cost as much as €8.4bn annually.

The new initiative would introduce a common EU-wide system for withholding tax on dividend and interest payments, as well as a system for tax authorities to exchange information and cooperate.

A range of policy options are being considered and could include one or more of the following:

- implementing measures to simplify and streamline withholding tax refund procedures, for example through digitalisation of current paper-based processes and common standardised EU forms and procedures for refund claims;
- establishment of a 'fully-fledged common EU relief at source system' where the withholding tax rate provided for in the applicable double tax treaty is applied at the time of payment to the non-resident investor thereby not incurring double taxation; and
- enhancing the existing administrative cooperation framework to verify entitlement to double tax treaty benefits to provide reassurance to the country of residence and the source country that the correct level of taxation has been applied to the non-resident investor.

Building a new EU-wide system offers the opportunity to do away with complex paper-based forms seen across the EU and digitalise the process, making things more efficient and cost-effective for investors in the process.

It should also provide the EU with a way to better monitor withholding tax claims and help reduce the risk of tax abuse.

It will be interesting see what form the new system will take and how effective it will be in breaking down current barriers to investment. If all goes to plan, the new system could be adopted by the Commission in the fourth quarter of 2022.

Austrian tax reform

Finally, on 3 October 2021 the Austrian government presented its plans for tax reform. Based on the announcements, the corporate tax rate will be reduced from 25% to 24% from 2023 and then to 23% from 2024.

Whilst lowering the corporate tax rate might seem surprising in light of pillar two and the effects of covid-19 on economies worldwide, the tax cut will be funded by new taxes on carbon emissions. Other jurisdictions, including Germany and France, already impose their own taxes on carbon emissions. But is the current unilateral approach working, or could this be the next candidate for a global solution? ■

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- The two-pillar framework: what does the October statement tell us? (P Greenfield, C O'Hara & G Maffini, 14.10.21)
- BEPS 2.0: the two-pillar approach (I Zeider & L Hodgson, 16.9.21)