

Briefing

International review for September

Speed read

Despite an initial lull during the early weeks of summer, there were still a few key developments in the tax world. Firstly, a shocking announcement that agreement had been reached between Senate Majority Leader Chuck Schumer (D-NY) and Senator Joe Manchin (D-WV) on tax, climate change, energy and health care provisions which formed part of the Inflation Reduction Act of 2022, which has now been passed into law. In light of the challenges the European Union is facing in implementing Pillar Two, a number of member states have indicated that, even if unanimity cannot be reached at EU level, they remain committed to implementing Pillar Two in their jurisdictions. Other jurisdictions are also making strides in implementing Pillar Two, with Hong Kong, Mauritius and Switzerland seeing developments. Lastly, some EU member states have indicated their commitment to completing work on Amount A under Pillar One.



Tim Sarson
KPMG

Tim Sarson is a tax partner at KPMG and the UK head of tax policy. He has worked in the international tax and transfer pricing field since 1998, in both practice and industry. Email: tim.sarson@kpmg.co.uk; tel: 020 7694 4831.

US: Inflation Reduction Act

On 16 August 2022, President Biden signed into law what is commonly referred to as the 'Inflation Reduction Act of 2022'. The Bill was passed by the Senate on 7 August, followed by the House of Representatives on 12 August. The legislation moved through Congress through a budget reconciliation process, which allows some legislation to move through the Senate by only a majority vote.

The legislation includes significant changes related to tax, climate change, energy and health care. Despite this being a significant breakthrough for Democrats, the new law is smaller in scope and spending and includes fewer revenue-raising provisions than what was included in the Build Back Better Initiative (BBBA).

The tax measures include:

- an alternative minimum tax of 15% on certain large corporations
- an excise tax of 1% in corporate stock buy-backs;
- energy-related tax credits; and
- additional funding for the IRS for taxpayer services and enforcement.

Corporate alternative minimum tax

The new law introduces a 15% corporate alternative minimum tax (corporate AMT) on the 'adjusted financial statement income' (AFSI) of certain large corporations (corporations reporting at least \$1 billion average adjusted pre-tax net income on their consolidated financial statements) for tax years beginning after 31 December 2022. It is estimated that this would raise approximately \$222.25 billion over the ten-year budget window.

Under the corporate AMT, corporations could owe

corporate AMT whenever they have significant permanent or temporary book-tax differences that cause financial statement income to exceed taxable income in a given year.

It is important to note that the new law provides significant regulatory authority with respect to certain aspects of the corporate AMT. There are more than 15 specific directions for the Treasury to fill gaps in the legislation. Therefore, in many respects the operation of the corporate AMT would depend on Treasury's decisions in implementing the regime, which is a particularly onerous task given that this provision is effective in a few months.

It is important to note that this domestic minimum tax is distinct from the global minimum tax plan embodied by Pillar Two. Furthermore, the new law does not include a substantial number of international tax changes that were in the BBBA initiative. The BBBA would have modified GILTI, the interest limitations and a number of other international provisions. Many of those changes would have aligned the US tax system more closely with those proposed in the ongoing OECD BEPS 2.0 project. By excluding those changes, it is not clear where the new law leaves the US system relative to the changes being contemplated outside the US with regard to Pillar Two.

The corporate AMT might be viewed as part of an effort by lawmakers to insulate income earned in the US from another country's undertaxed profits rule (UTPR), which could apply to US-parented multinational groups with €750m or more of revenue. However, it seems unlikely to fully achieve this given that, under the Pillar Two model rules, avoiding the application of a UTPR would require establishing that the ETR of the US entities in an MNE group is at least 15%, as measured based on the Pillar Two rules.

Nevertheless, the corporate AMT shares some similarities with the Pillar Two ETR calculation, in that both use financial statement income as the starting point for the tax base and apply 15% as the minimum rate of tax. The scope and technical design of the new corporate AMT, however, deviates from the Pillar Two framework in material ways. Pillar Two uses a much lower threshold in respect of scope, so a large population of taxpayers would be outside the scope of the corporate AMT and within the scope of Pillar Two. Further differences include:

- how Pillar Two and the corporate AMT compute tax liability;
- Pillar Two generally follows deferred tax accounting for purposes of determining the taxes included in the numerator of the Pillar Two ETR calculation, whereas the corporate AMT generally compares the tentative minimum tax to current taxes without any reference to book deferred tax accounts; and
- foreign taxes attributable to foreign branch operations of a US resident would be allowed to reduce the Corporate AMT owed with respect to income that is earned from activities conducted entirely within the US, which is contrary to the country-by-country approach of Pillar Two.

As a result of these and other deviations, corporate AMT taxpayers could still have an ETR that is lower than 15% for Pillar Two purposes and be exposed to the UTPR. Given the differences, the corporate AMT may not be considered a qualified domestic minimum top-up tax (QDMTT) under the Pillar Two framework.

So, is Pillar Two no longer on the table for the US? Treasury Secretary Janet Yellen has indicated that she will look for every opportunity to enact Pillar Two, but with the razor thin Democratic majorities, and a lack of support among Republicans and Senator Joe Manchin it is currently unclear whether and when this could be achieved. The US political landscape could look very different after the mid-term elections in November and tax advisors and businesses will be watching closely.

BEPS 2.0 Pillar Two

After a lull in the summer months, there has been some movement in respect of BEPS 2.0 Pillar Two.

European Union

The European Union has faced a challenging few months in reaching political agreement on the revised compromise text of the EU Directive to implement Pillar Two (the Directive). First, Poland raised objections, followed by Hungary which withdrew its previous agreement. On 3 September 2022, the German government announced its intention to start with the implementation of global minimum effective taxation rules. This was shortly followed on 9 September by a joint statement issued by the governments of France, Germany, Italy, Spain and the Netherlands, which expressed their full commitment to implementing Pillar Two. The release states that the five EU member states are fully determined to introduce rules on global minimum effective taxation in 2023, by any possible legal means. Although they have indicated that their primary goal remains to reach consensus by all EU member states, it is currently unclear how countries intend to achieve implementation. As I have discussed previously, the option of the 'enhanced cooperation' procedure is a possible solution, whereby a minimum of nine EU member states can choose to move ahead. Alternatively, the EU member states may look to proceed unilaterally.

The next ECOFIN meeting will be held on 4 October 2022, and we will have to see whether Hungary will continue to veto the initiative and if so, what steps will be taken next.

Hong Kong

On 15 August, the secretary for Financial Services and the Treasury issued an open letter that provided an update on the implementation of Pillar Two in Hong Kong and indicated that the implementation has now been deferred from 2023 to 2024 at the earliest. The deferral of implementation will provide more time for both the government and in-scope groups in Hong Kong to better prepare for the significant challenges presented by Pillar Two implementation.

The key messages of the letter are as follows:

- The implementation of the income inclusion rule (IIR) has been deferred from 2023 to 2024 at the earliest. The government plans to introduce the necessary legislative proposals to the Legislative Council in 2023.
- The government will monitor the implementation status of the undertaxed payment rule (UTPR) in other jurisdictions and review Hong Kong's own implementation plan.
- The government originally announced in the 2022/23 budget delivered in February 2022 that it would consider introducing a domestic minimum top-up tax in Hong Kong starting from year of assessment 2024/25 (i.e. 1 April 2024). This will now also be subject to the implementation status of other jurisdictions.
- In the coming months, the government will continue to closely monitor the OECD's latest timetable on the implementation of BEPS 2.0 and the implementation plans of other jurisdictions, and keep stakeholders closely informed of the implementation progress of Hong Kong.
- The government plans to launch a consultation towards the end of 2022 to collect views on the translation of the Pillar Two rules into domestic legislation and the relevant requirements.

Mauritius

On 29 July, the Finance (Miscellaneous Provisions) Bill 2022 has been released for consultation, and the draft legislation includes measures announced in the budget speech on

7 June 2022. Once the legislation is approved by parliament and signed by the president, the measures would be enacted. The bill includes proposed measures to align with the OECD's BEPS 2.0 recommendations, including a domestic top-up tax for companies part of an international group with a consolidated turnover of €750m or more.

Switzerland

On 17 August 2022, the Swiss Federal Council launched a public consultation on the draft ordinance to implement the OECD's Pillar Two model rules providing for a global minimum tax. The ordinance would temporarily enable the minimum tax rules to come into force before being replaced by a formal legislative amendment that requires more time due to the legislative process in Switzerland. However, this is subject to a pending constitutional amendment that would empower the government to release such ordinance. Furthermore, the release notes that the Federal Council will examine how far implementation of the OECD's Pillar Two solution has progressed in other countries when deciding to bring the regulations into force. The regulations are currently scheduled to become effective from 1 January 2024.

BEPS 2.0 Pillar One

The joint statement issued by France, Germany, Italy, Spain and the Netherlands notes that the five countries are also fully committed to completing the work on Amount A of Pillar One, with the objective of signing a multilateral convention by mid-2023. Pillar One remains significantly behind Pillar Two and considerable work needs to be undertaken over the next few months. It will be interesting to see whether this endorsement will prove enough to put Pillar One on more secure footing.

OECD tax director retires

On 6 September, the Organisation for Economic Cooperation and Development (OECD) released a statement announcing that Pascal Saint-Amans will retire from the organisation at the end of October 2022. Mr Saint-Amans has been at the OECD for 15 years, ten of which as the Director of the Centre for Tax Policy and Administration (CTP) and has been involved in significant developments at the OECD during his time there.

In 2012, he launched the BEPS Project, delivering the 15-point action plan of BEPS measures to tackle tax avoidance within a record two-year period, including a new type of multilateral instrument that has since been signed onto by 99 jurisdictions. As part of the BEPS Project, he brokered last year's landmark agreement among 137 countries and jurisdictions on the Two Pillar solution to the tax challenges arising from the digitalisation and the globalisation of the economy.

Grace Perez-Navarro, who has served as deputy director of the Centre for Tax Policy and Administration since 2007, will assume the role of director from 1 November 2022 until 31 March 2023, while David Bradbury, who has served as the head of the tax policy and statistics division since 2014, and Achim Pross, who has been the head of the international co-operation and tax administration division since 2011, will serve as acting deputy directors of the centre for tax policy and administration. ■

 For related reading visit www.taxjournal.com

► UK implementation of Pillar Two: where are we now? (L Hodgson, E Rowlands & J Kemp, 1.9.22)

► Pillar Two and the future of tax incentives (B Salehy, 6.7.22)