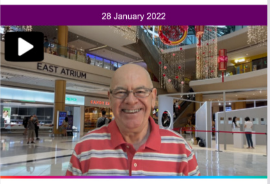
ITB International Tax Bytes *by Steve Towers*

"International tax news, explained"

28 January 2022



HIGHLIGHTS

- **Continuation of detailed review of GloBE model rules**
  - **Today, computation of GloBE Income or Loss (Part 4)**
- **Top international tax cases in 2021**
  - **Today, countdown of top 5**

HAPPY FRIDAY!

Inflation causes a **stock market rollercoaster**; **Amy Schneider** shows pearls of wisdom; but **Neil Young** can't find a heart of gold on **Spotify!**

Meanwhile, in the tax world…

Spain confiscates foreign assets; **Lithuania** follows **Estonia**; the **US** goes piecemeal; and **Alta Energy** wins the case and the prize!

But at the end of the week, the most important question is this: **"Should GloBE be a Wordle?"**

Have a great weekend!
Steve

THIS WEEK'S PODCAST

(For ITB video subscribers, please log in to access the video and documents/reports)

1. GloBE model rules
2. Top 10 international tax cases in 2021
3. Other global developments
4. Europe
   - ECJ, EU, Germany, Lithuania
5. Americas
   - US

ITB series on Pillars One & Two

- **GloBE model rules: Computation of GloBE Income or Loss (Part 4) (ITB, 28 January 2022)**
- **GloBE model rules: Computation of GloBE Income or Loss (Part 3) (ITB, 21 January 2022)**
- **GloBE model rules: Computation of GloBE Income or Loss (Part 2) (ITB, 14 January 2022)**
- **GloBE model rules: Computation of GloBE Income or Loss (Part 1) (ITB, 7 January 2022)**
- **Inclusive Framework's final agreement on Pillars One & Two (ITB, 15 October 2021)**

Pillar One

- **Scope (Parts 1, 2 & 3) – ITB (22, 29 Jan & 5 Feb 2021)**
- **Nexus – ITB (19 Feb 2021)**
- **Revenue sourcing rules (Parts 1 & 2) – ITB (26 Feb & 5 Mar 2021)**
- **Tax base determinations (Parts 1 & 2) – ITB (12 & 19 Mar 2021)**
- **Profit allocation (Parts 1 & 2) – ITB (26 Mar & 9 Apr 2021)**
- **Elimination of double taxation (Parts 1 & 2) – ITB (16 & 23 Apr 2021)**
- **Amount B (Parts 1 & 2) – ITB (30 Apr & 7 May 2021)**
- **Tax Certainty (Parts 1 to 4) – ITB (21, 28 May & 4, 11 Jun 2021)**
- **Implementation and administration – ITB (18 Jun 2021)**

Pillar Two

- **GloBE rules**
  - **Scope – ITB (9 Oct 2020)**
  - **Calculating the ETR (Parts 1 & 2) – ITB (16 & 23 Oct 2020)**
  - **Carry-forwards – ITB (30 Oct 2020)**
  - **Carve-out, and computation of the ETR and top-up tax – ITB (6 Nov 2020)**
  - **Income Inclusion Rule – ITB (13 Nov 2020)**
  - **Switch-Over Rule, and Undertaxed Payments Rule (Parts 1 & 2) – ITB (20 & 27 Nov 2020)**
  - **Associates, joint ventures and orphan entities; and Simplification options – ITB (4 Dec 2020)**
- **Other topics**
  - **Subject to Tax Rule – ITB (2 Oct 2020)**
  - **Implementation and Rule Co-ordination – ITB (11 Dec 2020)**
  - **Unresolved issues, GILTI & hub jurisdictions – ITB (18 Dec 2020)**

WORTH READING

Jinyan Li
"Finding the Purpose of Tax Treaty Provisions Under GAAR: Lessons from *Alta Energy*"
Tax Notes Today International, Tax Analysts, 27 January 2022 (subscription service)

Luc De Broe and Mélanie Massant
"The General Court's Judgment in Engie: The Non-application of a National GAAR Confers State Aid"
EC Tax Review, Kluwer, 2022 (Vol. 31), Issue 1 (subscription service)

INTERNATIONAL TAX QUIZ

THIS WEEK'S NEW QUIZ

ACo 1, a company resident in A, is a Constituent Entity within an MNE Group, for the purposes of the GloBE rules.

ACo 1 has the following financial information for the current fiscal year:

1. Profit or loss: negative **EUR 20 million**
2. Income tax expense: **EUR 7 million**
3. Profit on sale of 8% shareholding in XCo, an unrelated company: **EUR 3 million**
   a. The shares were sold to ACo 2 (another Constituent Entity resident in A)
   b. ACo 1 and ACo 2 are members of a tax consolidation group in A
   c. MNE Group's UPE makes an election under Art. 3.2.8 to apply its consolidated accounting treatment to all Constituent Entities resident in A
4. Charter fee revenue: **EUR 4 million**
   a. The revenue is from the lease of a ship for 2 years, on a bare boat charter basis, to BCo (unrelated shipping company resident in B)
   b. BCo uses the ship to transport passengers in international traffic
   c. ACo 1 incurs **EUR 1.5 million** of costs directly or indirectly attributable to this revenue
   d. ACo 1 has no other shipping activities
   e. ACo 2 has **EUR 6 million** of charter fee revenue from leasing a ship (to be used to transport cargo in international traffic) on charter fully equipped, crewed and supplied; ACo 2 incurs **EUR 2 million** of costs directly or indirectly attributable to this revenue
5. ACo 1 has a sales agent in C
   a. The sales agent causes ACo 1 to have a "contract-concluding agency" PE in C, under the A/C double tax treaty (which is identical to the 2017 UN model treaty)
   b. ACo 1 does not prepare separate financial accounts for the PE in C
   c. However, if ACo 1 did prepare separate financial accounts for the PE in C on a standalone basis in accordance with the accounting standard used in the preparation of the UPE's consolidated financial accounts, those separate financial accounts would show a profit of **EUR 0.5 million**. That profit of **EUR 0.5 million** is equal to the profit attributable to the PE, under Art. 7 of the A/C treaty
   d. **EUR 0.2 million** of ACo 1's income tax expense relates to the C income tax for the PE

Based on those numbers, what is the GloBE Income or Loss of ACo 1 (Main Entity) and the C PE, respectively?

Answer in next ITB email alert on 11 February 2022!

LAST WEEK'S QUESTION

XCo, a company resident in X, is a Constituent Entity within an MNE Group, for the purposes of the GloBE rules.

XCo has the following financial information for the current fiscal year:

1. Profit or loss: **negative EUR 5 million**
2. Income tax expense (in regard to Covered Taxes): **EUR 2 million**
3. Excise duty credit: **EUR 4 million**
   a. The credit can be used to offset future excise duty liabilities for the next 3 years – to the extent it is not used during that period, it will lapse
   b. Reported as credit to indirect tax expense in profit or loss
4. Loss of **EUR 8 million** under impairment accounting (included in profit or loss)
   a. XCo has not disposed of relevant asset
   b. Filing Constituent Entity makes election under Art. 3.2.5 to determine loss under realisation principle
5. Dividends of **EUR 2.5 million** paid on redeemable preference shares issued to YCo (Constituent Entity resident in Y)
   a. MNE Group has jurisdictional ETR of 14.95% in Y in current fiscal year. However, that jurisdictional ETR would be 15.1% if the dividends of EUR 2.5 million on the redeemable preference shares were excluded.
   b. Dividends are non-deductible / tax-exempt (including no withholding tax) in the 2 jurisdictions
   c. Dividends treated as interest expense in computing XCo's profit or loss
6. Prior period error of **EUR 3 million** (after tax benefit of **EUR 0.8 million**)
   a. Error was understatement of expenses in prior fiscal year
   b. Error correction is reported as a decrease in the opening equity at the start of the current fiscal year

Based on those numbers, what is XCo's GloBE Income or Loss for the current fiscal year?

LAST WEEK'S ANSWER

Computation of ACo 1's GloBE Income or Loss:

1. Start with loss (in P&L) (Art. 3.1): **negative EUR 5 million**
2. Income tax expense (Covered Taxes): add EUR 2 million (Art. 3.1.1(a))
   Thus, EUR 2m is added
3. Excise duty credit:
   a. Excise duty credit can be used only to offset future excise duty liabilities for next 3 years – IMHO: not "refundable". [Note that it is possible to take the view that the excise duty credit is "refundable" (and is therefore a "Qualified Refundable Tax Credit"), based on a statement in the October 2020 blueprint report (Art. 10.1.1 definition). In this question, it should not have any effect on the answer: in both situations, the excise duty credit is not excluded from GloBE Income or Loss (Art. 3.2.4).]
   b. Therefore, the GloBE rules do not require it to be either included or excluded.

   Thus, no adjustment.

4. Loss of EUR 8 million under impairment accounting (included in profit or loss): due to the election to determine loss under realisation principle, loss should be added (Art. 3.2.5).
   Thus, EUR 8 million is added.
5. Dividends of EUR 2.5 million paid on redeemable preference shares (RPS) issued to YCo:
   a. If YCo is a "High-Tax Counterparty", then the RPS would likely be an "Intragroup Financing Arrangement" (Art. 10.1.1 definitions).
   b. YCo is a "High-Tax Counterparty", as (according to the question) Y's jurisdictional ETR would be 15.1%, if the dividends on the RPS were excluded. Note that, for this situation to occur, the dividends are presumably not "Excluded Dividends" (Art. 10.1.1 definition), because, if they were, they would already be excluded in computing Y's jurisdictional ETR (Art. 3.2.1(b)). This would mean that the dividends fall within either of the 2 exceptions in the Art. 10.1.1 definition of "Excluded Dividends".
   c. EUR 2.5 million should be added (Art. 3.2.7).

   Thus, EUR 2.5 million added.

6. Prior period error of EUR 3 million (after tax benefit of EUR 0.8 million) – qualifies as "Prior Period Error and Changes in Accounting Principles" (Art. 3.2.1(h) & definition in Art. 10.1.1). Note that the exception in para. (a) of definition does not apply, because the "error correction" resulted in a decrease in Covered Taxes of less than EUR 1 million. As the amount reported as a decrease in opening equity is after the tax benefit, that "after tax" amount should, I think, be the amount which is adjusted.
   Thus, EUR 3 million is deducted.

Based on the above, XCo's GloBE Income or Loss = (5m) + 2m + 8m + 2.5m – 3m = EUR 4.5m.