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25 February 2022

HIGHLIGHTS

- **Review of draft model rules on tax base determinations for Amount A in Pillar One: released for public comments**
- **Continuation of detailed review of GloBE model rules**
    - **Today: computation of Adjusted Covered Taxes (Part 3)**

HAPPY FRIDAY!

Happy Friday (or is it?)

Putin wasn't bluffing …

Meanwhile, in the tax world …

Domestic minimum top-up taxes are fashionable; **GloBE** disconnects; **Malaysia** provides incentives for future vaccines; the **EU** shows a yellow card to 10 tax jurisdictions (including **Russia!**); and **Canada's DST** is creating noisy neighbours!

But at the end of a dramatic week in eastern Europe, **we should all #StandWithUkraine**

Have a great weekend!
Steve

THIS WEEK'S PODCAST

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

1. Pillar One
2. GloBE model rules
3. Other global developments
4. Asia Pacific
    - Hong Kong, Malaysia, Singapore
5. Europe
    - EU, Italy, Russia
6. Africa
    - South Africa
7. Americas
    - Canada

ITB series on Pillars One & Two

- **GloBE model rules: Computation of Adjusted Covered Taxes (Part 3) (ITB, 25 February 2022)**
- **GloBE model rules: Computation of Adjusted Covered Taxes (Part 2) (ITB, 18 February 2022)**
- **GloBE model rules: Computation of Adjusted Covered Taxes (Part 1) (ITB, 11 February 2022)**
- **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)**
- **Draft model rules for Amount A in Pillar One: Tax base determinations (ITB, 25 February 2022)**
- **Draft model rules for Amount A in Pillar One: Nexus and revenue sourcing (ITB, 11 February 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

Wolfgang Schön
"The Role of 'Commercial Reason' and 'Economic Reality' in the 'Principle Purpose Test' under Art. 29(9) OECD Model Tax Convention 2017"
9 February 2022 (freely available at www.ssrn.com)

Erik Christenson, Matt Jenner, John Barlow, and Young-Eun Choi
"Final FTC Regulations Cause Double Taxation – Burden(s) Falls on Taxpayers, Parts 1 to 3"
Tax Management International Journal, Bloomberg BNA, 4 February 2022 (subscription service)

INTERNATIONAL TAX QUIZ

THIS WEEK'S NEW QUIZ

UPE, a company resident in R, is the ultimate parent of an MNE group. The corporate income tax rate in R is 25%.

UPE owns 100% of the shares in ACo, a company resident in A.

ACo owns 100% of the shares in BCo, a company resident in B.

During the current Fiscal Year:

- ACo pays to UPE a royalty of 200, from which is deducts A royalty withholding tax of 20
- ACo also pays to UPE a dividend of 600, from which it deducts A dividend withholding tax of 30
- UPE pays to BCo interest of 400, from which it deducts R interest withholding tax of 40
- BCo pays to ACo a dividend of 250, from which it deducts B dividend withholding tax of 25
- UPE includes in its income tax expense: R tax of 250 in respect of BCo's income of 1,000 allocated to UPE under the R CFC rules. Of that 1,000, 600 is "Passive Income" (as defined in Art. 10.1.1). Before taking into account the R tax of 250, the Top-up Tax Percentage for jurisdiction B is 5%.

Based on these numbers, what are the amounts of Covered Taxes for UPE, ACo and BCo?

Answer in next ITB email alert!

LAST WEEK'S QUESTION

ACo, a Constituent Entity resident in A, has these financial items for a Fiscal Year:

1. Current tax expense: 25,000
2. Country B royalty withholding tax (recorded as debit to royalty income): 100
3. Country C digital services tax (recorded as debit to sales revenue): 500
4. Current tax expense in regard to uncertain tax positions:
    a. Accrued during current year: 1,000
    b. Paid during current year (accrued in prior year): 1,500
    c. Reversed during current year (accrued in prior year): 800
5. Income tax credit (refundable in cash for 3 years): credited to current tax expense: 300
6. Current tax expense in regard to "Excluded Dividends": 1,200

Based on these numbers, what is ACo's Adjusted Covered Taxes for the Fiscal Year?

LAST WEEK'S ANSWER

1. Start with current tax expense: 25,000 (Art. 4.1.1).
2. Country B royalty withholding tax (recorded as debit to royalty income): addition (Art. 4.1.2(a)).
   Thus, add 100.
3. Country C digital services tax (recorded as debit to sales revenue) – If the DST is levied on gross revenue, if it's a final tax, and if it is not in substitution for corporate income tax on net income (e.g., corporate income tax does not apply to the relevant gross revenue, possibly because of source rules), then (according to the October 2020 blueprint report – we don't have the Commentary yet!), the "in lieu of" test in Art. 4.2.1(c) is not satisfied. In that situation, the DST is not a Covered Tax. For the purpose of the calculation, I will assume (for the above reasons) that the Country C DST is not a Covered Tax.
   Thus, ignore.
4. Current tax expense in regard to uncertain tax positions.
    a. Accrued during current year (1,000): reduction (Art. 4.1.3(d).
    b. Paid during current year (accrued in prior year) (1,500): addition (Art. 4.1.2(c)).
    c. Reversed during current year (accrued in prior year) (800): ignore – because the "paid" condition in Art. 4.1.2(c) is not satisfied (but see my question below).
       Thus, add 500 (i.e., add 1,500 and deduct 1,000).
5. Income tax credit (refundable in cash for 3 years): credited to current tax expense (300): addition (Art. 4.1.2(d)).
   Thus, add 300.
6. Current tax expense in regard to "Excluded Dividends" (1,200): reduction (Art. 4.1.3(a)).
   Thus, deduct 1,200..

Thus, ACo's Adjusted Covered Taxes = 25,000 + 100 + 500 + 300 – 1,200 = 24,700

Do you agree with ignoring the reversal in the current tax expense in regard to uncertain tax positions?

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