ITB International Tax Bytes by Steve Towers

"International tax news, explained"

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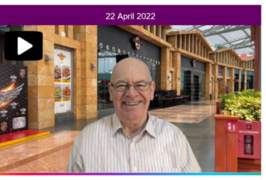

INTERNATIONAL TAX CASES BY STEVE TOWERS (ITC)

Newly launched! ITC video podcasts review recent international tax court and tribunal cases, which consider interesting international tax topics involving double tax treaties, transfer pricing, VAT and significant domestic tax issues.

First episode: Top 10 international tax cases in 2021
These cases cover an array of interesting international tax topics, including double tax treaty issues (such as PE status, residence, MFN clauses, application of domestic law anti-avoidance rules, and foreign tax credits), transfer pricing, and domestic law residence definitions.

*The first episode is **free**! To access the first episode, visit the ITC website: www.itkstevetowers.com and click on the "View product" button to see the details of the episode, and then click on "Buy now" (yes, it's free!) to access the video.*

HIGHLIGHTS

- **Review of draft model rules on Extractives exclusion from scope for Amount A in Pillar One**
  - **Released for public comment**
- **Continuation of detailed review of GloBE model rules**
  - **Today: De minimis exclusion in Art. 5.5**

HAPPY FRIDAY!

China books a **South Pacific** holiday; **Netflix** falls to Earth; and **Twitter's poison pill** causes **Marty Lipton** to trend!

Meanwhile, in the tax world ...

Infosys loses on the Indian connection; **OVID** doesn't copy; **Argentina** looks for a windfall; **Brazil** becomes comparable; **Canada** targets the banks; **Kenya** doesn't standstill; while the **Inclusive Framework** digs a hole in Step 3!

But at the end of the week, the best advice I can give you is this: **"Better Call Saul!"**

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. Pillar Two
3. 2021 UN model double tax treaty
4. Other global developments
5. GloBE model rules: detailed review
6. Asia Pacific
   - India, Indonesia, Thailand
7. Europe
   - Ireland, Netherlands
8. Africa
   - Kenya
9. Americas
   - Argentina, Brazil, Canada
10. Treaty news

ITB series on Pillars One & Two

- **GloBE model rules: Art. 5.5: De minimis exclusion (ITB, 22 April 2022)**
- **GloBE model rules: Art. 5.4.1: Additional Current Top-up Tax (ITB, 8 April 2022)**
- **GloBE model rules: Substance-based Income Exclusion – Tangible asset carve-out (ITB, 1 April 2022)**
- **GloBE model rules: Substance-based Income Exclusion – Payroll carve-out (ITB, 25 March 2022)**
- **GloBE model rules: Computation of Effective Tax Rate and Top-up Tax (ITB, 18 March 2022)**
- **GloBE model rules: Flow-through Entities and Hybrid Entities (ITB, 4 March 2022)**
- **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: Extractives exclusion (ITB, 22 April 2022)**
- **Draft model rules for Amount A in Pillar One: Scope (ITB, 8 April 2022)**
- **Draft model rules for Amount A in Pillar One: Tax base determination (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)**

WORTH READING

Zach Pouga Tinhaga
"Pillar 2: Not Your Traditional PE"
Tax Notes Today International, Tax Analysts, 13 April 2022 (subscription service)

Rodrigo Ruberti
"Applying the AOA to a PE That Performs Services: A Case Study on the Balance Sheet and the Profit and Loss Account of the Branch"
International Transfer Pricing Journal, 2022 (Vol. 29), No. 3, IBFD (subscription service)

Angelo Nikolakakis
"Bait and Switch – A Reply to Casey Plunket"
Letter to the Editor, Tax Notes Today International, 11 April 2022 (subscription service)

INTERNATIONAL TAX QUIZ

THIS WEEK'S NEW QUIZ

An MNE Group has 2 Constituent Entities (ACo and BCo) located in jurisdiction X.

ACo has these financial numbers for Years 1 to 3:

- Year 1:
  - GloBE Revenue: EUR 5 million
  - GloBE Income: EUR 0.8 million
- Year 2:
  - GloBE Revenue: EUR 7 million
  - GloBE Income: EUR 0.7 million
- Year 3:
  - GloBE Revenue: EUR 12 million
  - GloBE Loss: EUR 0.1 million

BCo has these financial numbers for Years 1 to 3:

- Year 1 (BCo was dormant in Year 1):
  - GloBE Revenue: EUR 0
  - GloBE Income or Loss: EUR 0
- Year 2:
  - GloBE Revenue: EUR 4 million (including EUR 3 million from services provided to ACo)
  - GloBE Income: EUR 0.2 million
- Year 3:
  - GloBE Revenue: EUR 3 million (including EUR 2 million from services provided to ACo)
  - GloBE Income: EUR 0.3 million

Is the MNE Group entitled to make a "de minimis exclusion" election for Year 3?

Answer in next ITB email alert!

LAST WEEK'S QUESTION

An MNE Group has one Constituent Entity (ACo) located in jurisdiction A.

For Year 1, the Group reported for jurisdiction A:

- Adjusted Covered Taxes: EUR 5 million
- Net GloBE Income: EUR 100 million
- ETR: 5%
- Substance-based Income Exclusion: nil
- Additional Current Top-up Tax: nil
- Qualified Domestic Minimum Top-up Tax: nil
- Thus, Top-up Tax = (10% x EUR 100 million) + 0 + 0 = EUR 10 million

For the current Fiscal Year (Year 3), the Group plans to report for jurisdiction A:

- Adjusted Covered Taxes: EUR 20 million
- Net GloBE Income: EUR 100 million
- ETR: 20%
- Substance-based Income Exclusion: nil
- Additional Current Top-up Tax: nil
- Qualified Domestic Minimum Top-up Tax: nil
- Thus, Top-up Tax = (0% x EUR 100 million) + 0 + 0 = 0

However, the Group now identifies a major jurisdiction A corporate income tax error in regard to Year 1. That error has caused an underpayment of EUR 2 million of tax for Year 1. However, the correction of the error will not cause any change to the GloBE Income for Year 1.

Q1: What are the adjusted amounts of Top-up Tax for Years 1 and 3?

Q2: Assume the same facts as above, except that the error in Year 1 has caused an overpayment of EUR 2 million of jurisdiction A corporate income tax for Year 1. Again, the correction of the error will not cause any change to the GloBE Income for Year 1. What are the adjusted amounts of Top-up Tax for Years 1 and 3?

LAST WEEK'S ANSWER

Q1

The correction of the jurisdiction A tax underpayment will cause an increase in Covered Taxes of EUR 2 million.

Art. 4.6.1 requires an increase in Covered Taxes for a prior Fiscal Year to be treated as relating to the current Fiscal Year (Year 3). There would thus be no adjustment to the Top-up Tax (i.e., EUR 10 million) for Year 1.

In Year 3, the Adjusted Covered Taxes are increased to EUR 22 million – therefore, the ETR becomes 22%. As there was no Top-up Tax in Year 3 prior to the correction, the correction will not cause any adjustment to the Top-up Tax (i.e., nil) for Year 3.

Therefore, the increase in the jurisdiction A tax will not any adjustment to Top-up Tax, in either Year 1 or Year 3.

Q2:

The correction of the jurisdiction A tax overpayment will cause a decrease in Covered Taxes of EUR 2 million.

Art. 4.6.1 requires a decrease in Covered Taxes for a prior Fiscal Year (Year 1) to be reflected in a recalculation of the ETR and Top-up Tax for Year 1, unless an election is available and is made (in this case, the election is not available, as the decrease amount exceeds EUR 1 million).

For Year 1:

i. the Adjusted Covered Taxes will now be EUR 3 million,
ii. the ETR will be 3%, and
iii. the Top-up Tax will be: (12% x EUR 100 million) + 0 + 0 = EUR 12 million.

Which means that there will be incremental Top-up Tax of EUR 2 million.

In accordance with Art. 4.6.1 and Art. 5.4.1, the incremental Top-up Tax:

i. is treated as Additional Current Top-up Tax in Year 3,
ii. the Year 3 Top-up Tax will be: (0% x EUR 100 million) + EUR 2 million + 0 = EUR 2 million, and
iii. there will be no adjustments to the assessments for Year 1.

Do you agree?