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International Tax Bytes by Steve Towers

"International tax news, explained"

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5 August 2022

HIGHLIGHTS

- **Pillar Two**
  - **Mauritius and Malaysia take steps to implement GloBE rules**
- **BlackRock case from UK**
  - **Deductions for interest on intragroup debt**
- **Continuation of detailed review of GloBE model rules**
  - **Today: Deferred tax liability recapture rules in Arts. 4.4.4 and 4.4.5**

HAPPY FRIDAY!

Batgirl is cancelled; and **Nancy** almost starts a war!

Meanwhile, in the tax world...

Mauritius and **Malaysia** start moving the globe; **BlackRock** loses interest; the **UN** takes aim at energy companies; **John Wiley's LLP** wins the issue, without an issue; **Barcelona** wants to tax **Amazon** for causing traffic jams; and **Uruguay** becomes less territorial!

But at the end of the week, the most important question is this: **"Do you think that Nancy Pelosi's visit to Taiwan was a good idea?"**

Have a great weekend!
Steve

THIS WEEK'S PODCAST

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

1. Pillars One & Two
2. BlackRock case
3. Other global developments
4. GloBE model rules: detailed review
5. Asia Pacific
   - Australia, Hong Kong, India, Malaysia, New Zealand, Singapore
6. Europe
   - Germany, Spain
7. Americas
   - Puerto Rico, US, Uruguay

ITB series on Pillars One & Two

- **GloBE model rules:**
  - **Deferred tax liability recapture rules in Arts. 4.4.4 and 4.4.5 (ITB: 5 August 2022)**
  - **Art. 4.4: mechanism to address temporary differences (ITB: 29 July 2022)**
  - **Scope: Art. 1.5 (definition of "Excluded Entity") (ITB: 1 July 2022)**
  - **Scope: Arts. 1.1 to 1.4 (ITB: 24 June 2022)**
  - **Charging Provisions (parts 1 to 5) (ITB: 6, 13 & 20 May; 10 & 17 June 2022)**
  - **Computation of Effective Tax Rate and Top-up Tax (Parts 1 to 6) (ITB, 18 & 25 March; 1, 8, 22 & 29 April 2022)**
  - **Flow-through Entities and Hybrid Entities (ITB, 4 March 2022)**
  - **Computation of Adjusted Covered Taxes (Parts 1 to 3) (ITB, 11, 18 & 25 February 2022)**
  - **Computation of GloBE Income or Loss (Parts 1 to 4) (ITB, 7, 14, 21 & 28 January 2022)**
- **Progress Report on Amount A in Pillar One (ITB, 22 July 2022)**
- **Draft model rules for Amount A in Pillar One:**
  - **Tax certainty (ITB, 10 June 2022)**
  - **Regulated Financial Services exclusion from scope (ITB, 13 May 2022)**
  - **Extractives exclusion (ITB, 22 April 2022)**
  - **Scope (ITB, 8 April 2022)**
  - **Tax base determination (ITB, 25 February 2022)**
  - **Nexus and revenue sourcing (ITB, 11 February 2022)**
- **Inclusive Framework's final agreement on Pillars One & Two (ITB, 15 October 2021)**

WORTH READING

Valentin Bendlinger and Georg Kofler
"Computation of the Effective Tax Rate and the 'Top-up Tax'"
freely available on SSRN (posted 30 July 2022).

Jonathan Culver
"Pillar Two – Challenges in the Coordination of Domestic Minimum Taxing Rights"
Asia-Pacific Journal of Taxation, Taxation Institute of Hong Kong / School of Accounting and Finance of The Hong Kong Polytechnic University, 2022 (Vol. 26), Issue No. 1 (subscription service) (posted by the author on LinkedIn).

Lily Zechner
"Understanding VAT in Three-Party, Platform-Based Business Models: Which Party Is Supplying Which Service?"
EC Tax Review, Kluwer, 2022, Issue No. 4 (subscription service).

INTERNATIONAL TAX QUIZ

THIS WEEK'S NEW QUIZ

ACo, a company located in jurisdiction A, is a Constituent Entity in a "within scope" MNE Group.

ACo is a special purpose company which has been formed to undertake a large construction project in jurisdiction A.

The project is expected to produce total pretax accounting profits and taxable income of 10,000 over its 10 years duration (i.e., Years 1 to 10).

For financial accounting purposes, ACo recognizes profit on a "percentage of completion" (POC) basis. Under the POC basis, ACo expects to recognize 1,000 of pretax profit in each of Years 1 to 10.

For jurisdiction A corporate income tax purposes, profit on long-term projects is recognized on a "completed contract" (CC) basis. Under the CC basis, ACo expects to recognize no taxable income in each of Years 1 to 9, but it will recognize 10,000 of taxable income in Year 10.

The jurisdiction A corporate income tax rate is 15%.

In each year, ACo's GloBE Income is equal to its financial accounting pretax profit.

Q1: What amounts of Top-up Tax (if any) will be triggered in each of Years 1 to 10?
Q2: Would your answer to Q1 be different if the MNE Group made an election under Article 4.4.7 for each of Years 1 to 5?

Answer in next ITB email alert!

LAST WEEK'S QUESTION

XCo is a Constituent Entity in an MNE Group, which is "within scope" of the GloBE rules.

XCo is located in jurisdiction X, which levies a corporate income tax.

In Year 1:

- XCo purchases (at the start of Year 1) a fixed asset for 100, which it depreciates for financial accounting purposes at 50% per annum, and which it claims as a 100% deduction for income tax purposes in Year 1
- XCo has GloBE Income of 500, after expensing 50 of depreciation for the fixed asset
- XCo has taxable income (for the purposes of X corporate income tax) of 470, after deducting 100 for the fixed asset
- XCo has no other temporary differences between its financial accounting pretax profit and taxable income
- The X corporate income tax has a nominal rate of 25%

In Year 2:

- XCo has GloBE Income of 620, after expensing 50 of depreciation for the fixed asset
- XCo has taxable income of 580
- XCo has no other temporary differences between its financial accounting pretax profit and taxable income
- Jurisdiction X increases its corporate income tax nominal rate to 30% (effective in Year 2)

Based on these facts, what are XCo's Adjusted Covered Taxes and ETR in Years 1 and 2?

Note: I made some changes to last week's question - sorry!

LAST WEEK'S ANSWER

Year 1:

- Current tax expense: 470 x 25% = 117.5
- Deferred tax expense (financial accounting): 50 x 25% = 12.5
- Total Deferred Tax Adjustment Amount (Art. 4.4.1): 50 x 15% = 7.5 (i.e., recast at 15%, no adjustments and no exclusions are relevant)
- Adjusted Covered Taxes: 117.5 + 7.5 = 125
- ETR: 125 / 500 = 25%

Year 2:

- Current tax expense: 580 x 30% = 174
- Total Deferred Tax Adjustment Amount (Art. 4.4.1): (7.5) (i.e., change in X tax rate is ignored: Art. 4.4.1(d))
- Adjusted Covered Taxes: 174 + (7.5) = 166.5
- ETR: 166.5 / 620 = 26.85%

Do you agree?

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