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31 March 2023

HIGHLIGHTS

- **Latest developments on Pillars One & Two**
 - **US is estimated to collect 56% of Pillar One (Amount A) global tax revenue**
 - **Japan, Canada, and Liechtenstein move forward with GloBE rules**
- **Significant investment tax credits introduced**
 - **Canada (for "clean energy" investments)**
 - **Korea (for semiconductor investments)**
- **Detailed review of Administrative Guidance on GloBE rules**
 - **Intra-group transactions accounted at cost**
 - **Excluded Equity Gains and Losses, and hedges of investments in foreign operations**

HAPPY FRIDAY!

Bragg creates a Storm; Taiwan's president transits; and Charles shows off his German – but I wonder how good his Welsh is!

Meanwhile, in the tax world...

Kenya changes course; Korea credits chips; Hong Kong draws a bright line; Delivero's contract fails to deliver; Russia imposes a "voluntary" tax (they promise to say "thank you"); the UK wants to stop leaks; Canada comes clean; and Japan is still the US's number 1 partner!

But the most amazing news this week is this: **There's water on the Moon!**

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. Other global developments
3. Administrative Guidance on GloBE rules: Income & taxes (part 1)
4. Asia Pacific
 - Australia, China, Hong Kong, Korea, India, Singapore
5. Europe
 - Montenegro, Netherlands, Russia, UK
6. Africa
 - Malawi, Namibia
7. Middle East & Central Asia
 - UAE
8. Americas
 - Canada, US
9. Treaty news

ITB series on Pillar One

- **Draft MLC provisions for commitments on DSTs and other relevant similar measures (ITB, 6 January 2023)**
- **Consultation document on Amount B in Pillar One (ITB, 16 December 2022)**
- **Progress Report on Amount A in Pillar One (ITB, 23 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 from scope (ITB, 22 April 2022)**
 - **Scope (ITB, 8 April 2022)**
 - **Tax base determinations (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)**

ITB series on Pillar Two

- **GloBE Implementation Framework:**
 - **Tax Certainty for the GloBE rules (ITB, 13 January 2023)**
 - **GloBE Information Return (ITB, 13 January 2023)**
 - **Guidance on Safe Harbours and Penalty Relief (ITB, 6 January 2023)**
- **GloBE model rules:**
 - **Administrative Guidance on GloBE rules: Income & taxes (part 1) (ITB, 31 March 2023)**
 - **Administrative Guidance on GloBE rules: Scope (Parts 1 to 3) (ITB, 10, 17 & 24 March 2023)**
 - **Administrative Guidance on GloBE rules: Allocation of taxes arising under Blended CFC Tax Regimes (ITB, 3 March 2023)**
 - **Administrative Guidance on GloBE rules: QDMTTs (Parts 1 & 2) (ITB, 16 & 24 February 2023)**
 - **Art. 7.4 on ETR computation for Investment Entities (ITB, 2 December 2022)**
 - **Corporate Restructurings and Holding Structures (Parts 1 to 7) (ITB, 23 & 30 September; 7, 14 & 31 October; 11 & 18 November 2022)**
 - **Scope (Parts 1 & 2) (ITB, 24 June; 1 July 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 8) (ITB, 11, 18 & 25 February; 29 July; 5, 12, 19 & 26 August; 16 September 2022)**
 - **Computation of GloBE Income or Loss (Parts 1 to 4) (ITB, 7, 14, 21 & 28 January 2022)**

WORTH READING

Leonard Wagenaar

"Do Bilateral Tax Treaties Distort, Rather than Support, International Trade?"

Talking Points, IBFD, 2023, No. 27 (subscription service).

Rouven Avi-Yonah

"Why 15%? Justifying the Global Corporate Minimum Tax"

18 March 2023 (freely available on www.ssrn.com; and posted by Steve Towers on LinkedIn).

Saud M. Alholiby

"Saudi Arabia's Tax Treaties: What Does Zakat Have to Do with Them?"

Bulletin for International Taxation, IBFD, 2023 (Vol. 77), No. 3 (subscription service).

INTERNATIONAL TAX QUIZ
THIS WEEK'S NEW QUIZ

ACo, a company located in jurisdiction A, is a Constituent Entity in an MNE Group which is "within scope" of the GloBE rules.

The UPE has a 60% Ownership Interest in ACo, with the balance of 40% owned by minority shareholders.

ACo has the following financial income for a fiscal year (determined in accordance with the Acceptable Accounting Standard used by the UPE in preparing its Consolidated Financial Statements):

1. Profit (i.e., net income) (in P&L): 30,000
2. Income included in Profit under equity accounting method: 5,000
3. Other comprehensive income (relating to changes in liabilities under ACo's pension plan): 4,500 (after deducting tax of 1,500)
4. Immaterial deviations from the Acceptable Accounting Standard: (800)
5. Income tax expense: 10,000 (includes 1,000 referable to income included in Profit under equity accounting method)
6. Withholding tax deducted from outbound royalties: 1,500 – this tax is economically borne by ACo under a "gross-up" condition in the licence agreement

Based on this information, what is ACo's GloBE Income or Loss for the fiscal year?

Answer in next ITB email alert on 14 April 2023!

LAST WEEK'S QUESTION

ACo is a company located in jurisdiction A. ACo runs the public hospital system in jurisdiction A. It is incorporated as a company by Act of parliament, it is required to provide comprehensive hospital services and not pursue profits, and it is exempt from jurisdiction A corporate income tax.

ACo has several subsidiaries (with ACo's shareholding percentage indicated):

1. Sub Co 1 (100%), which is located in jurisdiction B, but with a PE in jurisdiction F. Sub Co 1 carries out administrative activities which are ancillary to ACo's hospital activities in jurisdiction A. Sub Co 1 also invests funds for the benefit of ACo. Both of these activities are performed in the Main Entity and the PE.
2. Sub Co 2 (97%), which is located in jurisdiction C. The other 3% shareholding is owned by senior management in Sub Co 2. Sub Co 2 has been funded by equity from ACo and has borrowed from third parties. It has used the funding to acquire a broad range of debt and equity investments.
3. Sub Co 3 (100%), which is located in jurisdiction D. Sub Co 3 has also been funded by equity from ACo and has borrowed from third parties. It has used the funding to acquire shares, from which Sub Co 3 derives only Excluded Dividends and Excluded Equity Gains and Losses.
4. Sub Co 4 (100%), which is located in jurisdiction E. Sub Co 4 operates several private hospitals in jurisdiction E, using IP and services provided by ACo.

ACo prepares consolidated financial statements in accordance with the applicable financial accounting standard in jurisdiction A, and as required by jurisdiction A law. For the latest fiscal year, those consolidated financial statements report revenue of EUR 3 billion.

Also for that latest fiscal year, the "separate entity" revenue for the 5 companies in the group is:

- ACo: EUR 2.5b
- Sub Co 1: EUR 200m (comprising: (i) Main Entity: EUR 180m; and (ii) PE: EUR 20m)
- Sub Co 2: EUR 150m
- Sub Co 3: EUR 100m
- Sub Co 4: EUR 200m

All of the 6 jurisdictions (A to F) have implemented the GloBE rules (IR and UTPR) and a QDMTT (which is effectively identical to the GloBE rules).

Based on this information, ACo's tax director has told you that it is not possible for any of those 5 companies to have an IR, UTPR or QDMTT tax liability for that fiscal year. Do you agree?

LAST WEEK'S ANSWER

Introductory point:

If any of the 5 companies is not a "Constituent Entity", then these taxes (in its location jurisdiction) will not apply to it: IR (Art. 2.1), UTPR (Art. 2.4.1), and QDMTT (because there would be no Top-up Tax in that jurisdiction: Arts. 5.1 & 5.2).

ACo:

ACo is a "Non-Profit Organisation" (Art. 10.1.1 definition), and thus it is an "Excluded Entity" (Art. 1.5.1(c)).

ACo is therefore not a "Constituent Entity" (Art. 1.3.3).

Sub Co 1:

Is Sub Co 1 an "Excluded Entity" under Art. 1.5.2(a)?

The fact that Sub Co 1 performs 2 activities (i.e., administrative activities which are ancillary to ACo's hospital activities, and investing funds for the benefit of ACo) does not disqualify it from "Excluded Entity" status (para. 54.1 in new Commentary to Art. 1.5.2, added by AG).

Also, in assessing its compliance with Art. 1.5.2, the activities of the whole of the Entity (i.e., Main Entity and PE) are considered together – and, if the definition is satisfied, the whole of the Entity is an "Excluded Entity": para. 43.1 in new Commentary to Art. 1.5.2, added by AG.

Thus, Sub Co 1 (Main Entity and PE) is an "Excluded Entity" (Art. 1.5.2(a)), and it is thus not a "Constituent Entity" (Art. 1.3.3).

Sub Co 2:

The fact that Sub Co 2 has borrowed from third parties does not disqualify it from "Excluded Entity" status under Art. 1.5.2(a) (para. 63 in new Commentary to Art. 1.5.2, added by AG) – subject to one qualification: the new Commentary provides an example of a "wholly owned subsidiary" (cf. Sub Co 2, which is 97% owned by ACo). Does that make a difference?

BMH: That should not make a difference, having regard to the fact that para. (a) in Art. 1.5.2 requires only "at least 50%" ownership. Also, note that, even with the 3% "leakage", Sub Co 2 does "almost exclusively" hold assets or invest funds for the benefit of ACo.

Thus, **BMH:** Sub Co 2 should be an "Excluded Entity" (Art. 1.5.2(a)), and thus it is not a "Constituent Entity".

Sub Co 3:

Apart from the third party borrowing, Sub Co 3 would clearly satisfy Art. 1.5.2(b).

There is nothing in Art. 1.5.2(b), the Commentary, or the AG to indicate that the third party borrowing would make a difference.

Thus, Sub Co 3 is an "Excluded Entity" (Art. 1.5.2(b)), and thus it is not a "Constituent Entity".

Sub Co 4:

Based on the text in the GloBE rules, Sub Co 4 does not satisfy either para. (a) or (b) of Art. 1.5.2.

However, the AG has introduced a "bright-line test" which can deem "ancillary activities" status under Art. 1.5.2(a)(i).

Application of test: Is Sub Co 4's revenue (EUR 200m) less than (1) EUR 750m, or (2) 25% of "revenue of MNE Group" (i.e., 25% x EUR 3b = EUR 750m) (whichever is lower)? Yes!

Therefore, Sub Co 4 is deemed to satisfy Art. 1.5.2(a)(i). Thus, Sub Co 4 is an "Excluded Entity" (Art. 1.5.2(a)), and it is thus not a "Constituent Entity".

Final answer:

ACo's tax director is correct.

Do you agree?



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