

Want to learn more about ITB? Sign up for a free trial by emailing us

Free Trial

Check out our suite of subscription plans: individual (standard), student, university faculty, young professional, and enterprise

Subscribe

14 July 2023



### HIGHLIGHTS

- **Outcome Statement on Pillars One & Two**
  - More work is required on Amounts A & B
  - But final STTR documentation will be released next week
- **Germany removes "royalty barrier" rule**
- **Korea is expected to defer UTPR to 2025**
- **Continuation of detailed review of Administrative Guidance on GloBE rules**
  - Today: Asset carrying value and deferred taxes under Art. 9.1.3

### HAPPY FRIDAY!

**Biden clusters with Ukraine; Italians object to a 10-second rule; and folks throw stones at Musk's glass house!**

Meanwhile, in the tax world...

IF releases an **Outcome Statement** (or should that be "Outlook Statement"?); **ATAP's** glass is half-full and half-empty; **Germany** dismantles and builds barriers; **Korea** shows deference; **Turkey's** inflation applies to tax rates; and be careful of merging in **Peru!**

But at the end of the week, the most important question is this: "Will Hollywood actors really go on strike - or are they just acting?"

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: Outcome Statement
2. GloBE rules
3. Other global developments
4. Administrative Guidance on GloBE rules: Transition (part 3)
5. Europe
  - EU, Turkey
6. Africa
  - South Africa
7. Americas
  - Brazil, Colombia, Peru, US
8. 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, 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 from scope (ITB, 22 April 2022)
  - Scope (ITB, 6 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: Transition (Parts 1 to 3) (ITB, 16 & 23 June; 14 July 2023)
  - Administrative Guidance on GloBE rules: Income & taxes (Parts 1 to 8) (ITB, 31 March; 14, 21 & 29 April; 5, 12 May; 2 & 9 June 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, 10 & 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 & 21 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 9) (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

Mindy Herzfeld

"Limiting the Fallout from Moore"

Tax Notes Today International, Tax Analysts, 10 July 2023 (subscription service).

Niels Winther-Sorensen

"The Danish Supreme Court's Decisions on Withholding Tax on Dividends and Interest"

European Taxation, IBFD, 2023 (Vol. 63), No. 7 (subscription service).

Guy Sanschagrin and Doug Schwerdt

"The Profit-Split Method: A Commentary on the Nulon Example"

Tax Notes Today International, Tax Analysts, 5 July 2023 (subscription service).

### INTERNATIONAL TAX QUIZ

#### THIS WEEK'S NEW QUIZ

XCo (a company located in jurisdiction X) and YCo (a company located in jurisdiction Y) are both Constituent Entities in an MNE Group which is "within scope" of the GloBE rules. XCo and YCo have been members of the MNE Group for over 10 years.

For the MNE Group, the Transition Year for both jurisdiction X and jurisdiction Y is the 2024 fiscal year (31 December year-end).

Jurisdiction X imposes a 20% corporate income tax, and jurisdiction Y imposes a 25% corporate income tax.

XCo was the owner of IP. The IP had a carrying value in XCo's balance sheet of EUR 5m. However, its fair market value was EUR 150m.

XCo's tax basis in the IP was zero, and XCo had a deferred tax liability of EUR 1m in respect of the IP, due to accelerated tax depreciation.

On 1 January 2022, XCo sold the IP to YCo for a price of EUR 150m.

Under the accounting standard used to prepare the MNE Group's consolidated financial statements: (1) At the purchase date, YCo has an accounting carrying value in the IP equal to XCo's accounting carrying value at disposition (i.e., EUR 5m); and (2) YCo amortises the IP at the rate of 10% per annum (reducing balance method).

For jurisdiction Y corporate income tax purposes: (1) At the purchase date, YCo has a tax basis of EUR 150m in the IP; and (2) YCo amortises the IP at the rate of 20% per annum (reducing balance method).

At the start of the 2024 fiscal year, what will be YCo's treatment under Art. 9.1.3 in respect of the IP?

Answer in next ITB email alert on 28 July 2023!

### LAST WEEK'S QUESTION

XCo, a company located in jurisdiction X, is a Constituent Entity in an MNE Group which is "within scope" of the GloBE rules. The jurisdiction X corporate income tax rate is 20%. XCo is the only Constituent Entity located in jurisdiction X.

XCo owns 100% of the shares in YCo, a company located in jurisdiction Y. The jurisdiction Y corporate income tax rate is 10%. YCo is treated as a resident company for jurisdiction Y tax purposes; however, it is treated as tax transparent (a "disregarded entity") for jurisdiction X tax purposes. YCo is the only Constituent Entity located in jurisdiction Y.

Anti-hybrid mismatch rules are not included in the corporate income tax law of either jurisdiction X or Y. However, both jurisdictions have implemented the GloBE rules, including a QDMTT (in effectively the same form as the GloBE model rules).

For a fiscal year, YCo's GloBE income is 100. Its taxable income (for jurisdiction Y corporate income tax purposes) is also 100. In computing the 100, these items are taken into account:

1. Interest expense of 30 (on a loan from XCo) is deducted.
2. Interest income of 10 (on a loan to a third party bank) is included.
3. Fee income of 15 (for provision of know-how to third parties) is included.

For jurisdiction X purposes, YCo's before-tax profit is included in XCo's taxable income. The amount of profit so included is 130, after "adding back" the disregarded interest expense of 30. XCo is entitled to a foreign tax credit for the jurisdiction Y corporate income tax paid by YCo on that profit. In calculating the foreign tax credit, please assume that no expenses or losses are deducted from the foreign source income.

Based on this information, what is YCo's Adjusted Covered Taxes for that fiscal year?

### LAST WEEK'S ANSWER

YCo's Adjusted Covered Taxes:

1. YCo's current tax expense: 10% x 100 = 10.
2. YCo's deferred tax expense: 0.
3. XCo's Covered Tax allocated to YCo under Art. 4.3.2(d) [see Note A below]: 14.9.
4. Adjusted Covered Taxes: 10 + 14.9 = 24.9. [See Note B below]

Note A:

- a. YCo is a "Hybrid Entity" (defined in Art. 10.2.5).
- b. YCo's Covered Tax on YCo's profit (after foreign tax credit 10): (20% x 130) - 10 = 16.
- c. Art. 4.3.3 limitation must be determined ...
- d. YCo's "Passive Income" (defined in Art. 10.1.1): know-how fee income is probably not a "royalty" (not defined), and therefore not "Passive Income". However, YCo's interest income of 10 would be Passive Income. The question does, however, provide full information on YCo's expenses, although the interest expense incurred to XCo is mentioned. The Comm does not discuss whether Passive Income is determined before or after deducting related expenses. Based on the wording of the definition in Art. 10.1.1, my preferred view is that related expenses are not deducted, if this is correct, YCo's Passive Income is 10.
- e. Art. 4.3.3, para. (a) should be: 16 x (10 / 100) = 1.6
- f. Art. 4.3.3, para. (b) should be: 5% x 10 = 0.5.
- g. Thus, Art. 4.3.3 limitation is 0.5.
- h. XCo's Covered Tax on YCo's profit (excluding YCo's Passive Income): 16 x (90 / 100) = 14.4.
- i. XCo's Covered Tax allocated to YCo under Art. 4.3.2(d) (after applying Art. 4.3.3 limitation): 14.4 + 0.5 = 14.9.

Note B: In discussing QDMTTs, AG (section 5.1.3) addresses the allocation of CFC tax under Art. 4.3.2(c) and "Main Entity" tax under Art. 4.3.2(a), but it does not address the allocation of "Hybrid Entity" tax under Art. 4.3.2(d). Accordingly, I have assumed that Art. 4.3.2(d) applies for the purposes of a QDMTT.

Do you agree?



Tax Quiz Archives



Email Alert Archives



Ask Steve



Referral Program



What is ITB?

If you have a friend or colleague who you think might find this email alert interesting, please forward it to them.

Watch ITB video podcasts anytime, anywhere with our App!

