ITB International Tax Bytes by Steve Towers

"International tax news, explained"

28 July 2023

HIGHLIGHTS

- **GloBE rules**
  - **New Administrative Guidance**
  - **GloBE Information Return**
- **Subject to Tax Rule:**
  - **Draft treaty article**
  - **Commentary**
- **Major corporate tax reform bill released in Germany**
- **US Treasury & IRS provide temporary relief from 2022 final regulations on foreign tax credits**

HAPPY FRIDAY!

Earth reaches boiling point; **China's** foreign ministry goes back to the future; and the son rises in **Cambodia**!

Meanwhile, in the tax world…

Michael Plowgian is grilled; **Vietnam** joins the party; the **UK** gets in front of the OECD; **BIAC** wants to be relevant; **Germany** is at a loss; and the **IRS** relaxes temporarily!

But at the end of the week, the most interesting question is this: **"Is it possible to register 'X' as a trademark?"**

Have a great weekend!
Steve

THIS WEEK'S PODCAST

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

1. July 2023 Administrative Guidance on GloBE rules: Overview
2. GloBE Information Return
3. Other GloBE developments
4. Subject to Tax Rule (STTR): Overview
5. Amount B
6. Amount A
7. Europe
   - Germany
8. Americas
   - US
9. Treaty news

ITB series on Pillar One

- **Consultation document on Amount B in Pillar One (ITB, 28 July 2023)**
- **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, 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:**
  - **GloBE Information Return (ITB, 28 July 2023)**
  - **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:**
  - **July 2023 Administrative Guidance on GloBE rules: overview (ITB, 28 July 2023)**
  - **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 & 28 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)**
- **Subject to Tax Rule (STTR):**
  - **Subject to Tax Rule (STTR): overview (ITB, 28 July 2023)**

WORTH READING

Robert Goulder
"SCOTUS Crystal Ball: Predicting Moore's Future"
Tax Notes Today International, Tax Analysts, 25 July 2023 (subscription service).

Mees Vergouwen
"The subordination clause in the new tax treaty between the Netherlands and Belgium that grants primacy to the Pillar 2 Directive"
Kluwer International Tax Blog, 13 July 2023 (freely available).

Brian Platt, Enda Curran, and Gabrielle Coppola
"Subsidy Wars Heat Up With US Allies Forced to Pay Up or Lose Out"
Daily Tax Report: International, Bloomberg, 26 July 2023 (subscription service).

INTERNATIONAL TAX QUIZ

THIS WEEK'S NEW QUIZ

ACo (a company located in jurisdiction A) and BCo (a company located in jurisdiction B) are both Constituent Entities in an MNE Group which will be "within scope" of the GloBE rules, when the rules commence (on 1 January 2024). ACo and BCo are the only Constituent Entities located in their respective jurisdictions. Jurisdiction U (in which the UPE is located) has enacted the IIR, but it does not have any CFC rules.

Jurisdiction A has no corporate income tax. Jurisdiction B has a corporate income tax with a 20% tax rate. Neither jurisdiction A or jurisdiction B has a QDMTT.

For many years, ACo has been the owner of IP, which it licenses to group companies in return for arm's length royalties (totalling EUR 40m annually). No foreign withholding tax is imposed on the royalties. ACo's accounting carrying value in the IP is zero. ACo has a zero tax basis in the IP, and there are no deferred taxes relating to the IP.

The MNE Group is concerned about the IIR Top-up Tax which will be triggered in respect of jurisdiction A, when the GloBE rules commence.

The MNE Group has suggested this "solution": Before the GloBE rules commence, ACo will sell the IP (together with the licences) to BCo for fair market value (which is EUR 400m). This will mean that, when the GloBE rules commence, BCo will derive the EUR 40m of annual royalties, not ACo.

The MNE Group has estimated that, in the first year of operation of the GloBE rules (2024), BCo's GloBE position (before considering the impact of its purchase of the IP) would be this:

1. GloBE Income: EUR 200m
2. Adjusted Covered Taxes: EUR 40m
3. Substance-based Income Exclusion: EUR 20m

Under the applicable accounting standard, BCo will have an accounting carrying value in the IP of zero.

For jurisdiction B corporate income tax purposes, BCo's tax basis in the IP will be EUR 400m.

For tax purposes, BCo will amortise the IP at a rate of 25% per annum, straight line.

Based on this information, will the MNE Group's Top-up Tax be lower if the above-mentioned "solution" is implemented, or if the status quo (i.e., ACo retains the IP) is maintained?

Please (1) assume that the sale transaction would be undertaken on 31 December 2023; and (2) ignore any possible safe harbours.

Answer in next ITB email alert!

LAST WEEK'S QUESTION

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. XCo derived a taxable gain of EUR 150m on the sale.

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?

LAST WEEK'S ANSWER

(1) YCo's GloBE carrying value in IP:

As at the purchase date (1 January 2022), YCo's GloBE carrying value in the IP is EUR 5m (i.e., XCo's accounting carrying value on that date).

To determine the GloBE carrying value at 1 January 2024 (the start of the Transition Year), we must deduct 2 years of amortisation, using the accounting amortisation rate and method, and applied to the GloBE carrying value (and not YCo's accounting carrying value).

The amortisation in 2022 is: EUR 5m x 10% = EUR 0.5m (giving a carrying value at 31 December 2022 of EUR 4.5m).

The amortisation in 2023 is: EUR 4.5m x 10% = EUR 0.45m.

Thus, YCo's GloBE carrying value at 1 January 2024 is EUR 4.05m.

[See para. 10.1 of Comm to Art. 9.1.3 (added by Feb23 AG, section 4.3.3)].

(2) YCo's deferred taxes relating to IP:

In accordance with para. 10.9 of Comm to Art. 9.1.3 (added by Feb23 AG, section 4.3.3) ...

As at the purchase date, YCo's prima facie deferred tax asset relating to the IP would be: [EUR 150m x 20%] + [EUR (1m)] = EUR 29m.

However, "[a] deferred tax asset created under this rule shall not exceed the Minimum Rate multiplied by the difference in the local tax basis in the asset and the GloBE carrying value of the asset ...". This limitation is: [EUR 150m – EUR 5m] x 15% = EUR 21.75m.

Thus, as at the purchase date, YCo would have (for GloBE purposes) a deferred tax asset of EUR 21.75m relating to the IP.

Para. 10.9 says: "This deferred tax asset is adjusted annually in proportion to any decrease in the carrying value of the asset for the year, for example due to depreciation, amortization, or impairment."

The meaning of this sentence is not totally clear – however, my "best guess" is this: Over the 2022 and 2023 years, the GloBE carrying value of the IP is reduced by an aggregate of 19% (i.e., 10% per annum reducing balance) – the deferred tax asset should also be reduced by 19%.

If this is correct, then YCo's deferred tax asset (for GloBE purposes) in the IP as at 1 January 2024 would be: EUR 21.75m x 81% = EUR 17.62m.

(3) Final answer:

GloBE carrying value: EUR 4.05m.
Deferred tax asset (for GloBE purposes): EUR 17.62m.

Do you agree?