

International Tax Forum: Selected Accounting Aspects of GloBE / QDMTT

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Agenda

1 Overview of ETR calculation mechanism

2 Zooming in on the denominator of the formula

3 Zooming in on the numerator of the formula

Recap: Effective Tax Rate (ETR) per Jurisdiction

$$\text{ETR} = \frac{\text{adjusted covered taxes}}{\text{adjusted GloBE income}}$$

Adjusted Covered Taxes per Jurisdiction

The lower the Covered Tax, the higher the chances of a Top-Up Tax.

The higher the Covered Tax, the lower the chances of a Top-Up Tax.

Adjusted GloBE Income per Jurisdiction

Taxes being fixed

The higher the GloBE income, the higher the chances of a Top Tax.

The lower the GloBE income, the lower the chances of a Top-Up Tax

Zooming in on the denominator:

**Focus on Article 3: Computation of GloBE Income /
Loss**

Article 3.1 – GloBE Income or Loss per jurisdiction – GloBE Tax Base

The relevant financial accounting standard for calculating the GloBE tax base is the financial accounting standard used by the parent in the preparation of its consolidated financial statements

The acceptable financial accounting standards include International Financial Reporting Standards (IFRS) and the generally accepted accounting principles of Australia, Brazil, Canada, MSs of the EU, MSs of the EEA, Hong Kong (China), Japan, Mexico, New Zealand, the People's Republic of China, the Republic of India, the Republic of Korea, Russia, Singapore, Switzerland, the UK, and the US.

GloBE/QDMTT Income / Loss

The Financial Accounting Net income or loss of the CE which has been prepared by the UPE when it does consolidation is the starting point for the calculations.

Certain adjustments are made, eg. items of income are removed and certain items of expense are added back to the net income or loss to arrive at the GloBE tax base per country

Note that CE statements prepared in accordance with local GAAP are not recognized for GloBE. However, QDMTT calculations may be based on local financial accounting standard, if the country wishes to exercise this option. Also, QDMTT needs to be paid in local currency

Chapter 3 – The Adjustment Landscape for GloBE purposes

Mandatory adjustments

- Article 3.2.1 – Some general adjustments
- Article 3.2.3 – Adjustments with respect to the Arm's Length Principle
- Article 3.2.4 – Dealing with qualified, transferable and non-qualified refundable tax credits
- Article 3.2.7 – Specific provision for countering planning through intra group financial arrangements
- Article 3.2.11 – Adjustments made in Chapter 6 and 7
- Article 3.4 – Special rules for Permanent Establishments
- Article 3.5 – Special rules for flow through entities

Taxpayer Elections

- Article 3.2.2 – Employee Stock Options
- Article 3.2.5 – Gains and losses using realisation principle
- Article 3.2.6 – Aggregate Asset gains
- Article 3.2.8 – The use of Tax Consolidation

Industry or case specific

- Article 3.2.9 – Insurance companies
- Article 3.2.10 – Banks
- Article 3.3 – Shipping sector

*** For QDMTT purposes countries can be stricter: eg. not allowing deductions for fines and penalties or when ESOP expenses are treated similarly for financial accounting and tax law purposes**

GloBE Income Adjustments – Case Study

State R

R Co

Case study facts:

- The UPE R Co in State R has Constituent Entities: S1 Co in State S1, S2 Co in State S2, and S3 Co in State S3.

Questions:

- What is the GloBE Income / Loss per entity / jurisdiction?
- What are the Covered Taxes per entity / jurisdiction?
- What is the GloBE ETR per entity / jurisdiction?

S1 Co

State S1

- Profit after taxes of \$100
- Income Taxes of \$ 20
- Fines and penalties of \$ 15
- Gains from stock disposition \$ 10

S2 Co

State S2

- Profit after taxes of \$ 35
- Income Taxes of \$ 4
- Foreign currency transitional loss in P&L of \$ 1

S3 Co

State S3

- Profit after taxes \$ 20
- Income Taxes of \$ 5
- Bribe cost of \$ 0,5
- Dividends received of \$ 2 from Sub Co (Not portfolio dividend)

Article 3.2.1 – Case Study – Solution

S1 Co

- Profit after taxes of \$100
- Income Taxes of \$ 20
- Fines and penalties of \$ 15
- Gains from stock disposition \$ 10

S2 Co

- Profit after taxes of \$ 35
- Income Taxes of \$ 4
- Foreign currency transitional loss in P&L of \$ 1

S3 Co

- Profit after taxes \$ 20
- Income Taxes of \$ 5
- Bribe cost of \$ 0,5
- Dividends received of \$ 2 from sub

	S1 Co	S2 Co	S3 Co
Profit after tax	100	35	20
GloBE Income adjustments (Article 3.2.1):			
Net Tax expense	+20	+4	+5
Excluded Dividends			-2
Excluded Equity Gain or Loss	-10		
Included Revaluation Method Gain or Loss			
Gain or loss from disposition of assets and liabilities as part of a GloBE Reorganization			
Asymmetric Foreign Currency Gains or Losses		+1	
Policy Disallowed Expenses	+15		+0,5
Prior Period Errors and Changes in Accounting Principles			
Accrued Pension Expense			
Total GloBE income adjustments	+25	+5	+3.5
Adjusted GloBE Income	125	40	23,5
Adjusted Covered Taxes	20	4	5
ETR	16.00%	10.00%	21.28%

Zooming in on the numerator:

Focus on Article 4: Covered Taxes

Definition of Income Taxes – IFRS (IAS 12.1 – 12.2)

Scope

- 1 This Standard shall be applied in accounting for income taxes.
- 2 For the purposes of this Standard, income taxes include all domestic and foreign taxes which are based on taxable profits. Income taxes also include taxes, such as withholding taxes, which are payable by a subsidiary, associate or joint arrangement on distributions to the reporting entity.

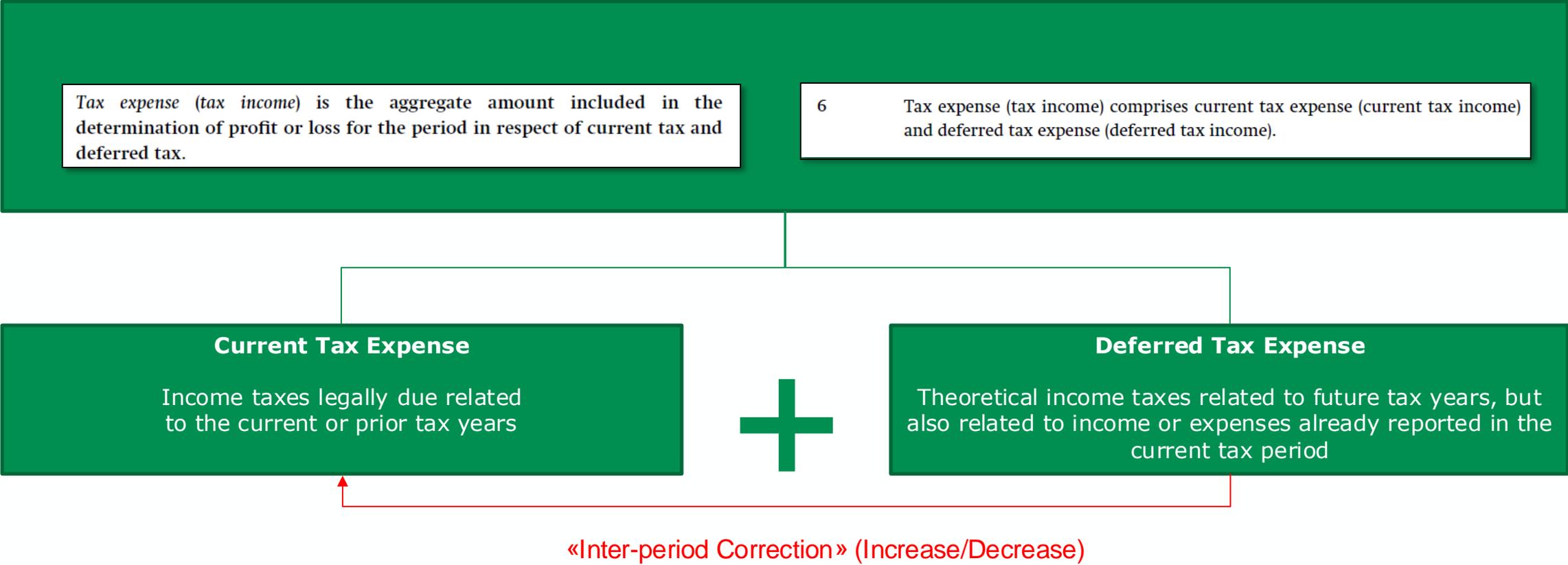
«All domestic and foreign taxes which are based on taxable profits»

«IAS 12 applies to income taxes, which are defined as taxes that are based on taxable profit, and that the term 'taxable profit' implies, in general, a notion of a net rather than a gross amount»

«Taxes, such as withholding taxes, which are payable by a subsidiary, associate or joint arrangement on distributions to the reporting entity»

- Intercompany dividend distributions from:
- Subsidiaries («control», simplified: > 50%);
 - Joint arrangement («common control», simplified: 50%);
 - Associate («significant influence», simplified: 20% to < 50%)

Income Tax Expense – IFRS (IAS 12.5)



Current Taxes – IFRS (IAS 12.5)

Current Taxes

Current tax is the amount of income taxes payable (recoverable) in respect of the taxable profit (tax loss) for a period.

Taxable Profit

Taxable profit (tax loss) is the profit (loss) for a period, determined in accordance with the rules established by the taxation authorities, upon which income taxes are payable (recoverable).

Deferred Taxes on Temporary Differences – IFRS (IAS 12.5)

Deferred Taxes

Deferred Tax Liabilities

Deferred tax liabilities are the amounts of income taxes payable in future periods in respect of **taxable temporary differences**.

Deferred Tax Assets

Deferred tax assets are the amounts of income taxes recoverable in future periods in respect of:

- (a) **deductible temporary differences**;
- (b) the carryforward of unused tax losses; and
- (c) the carryforward of unused tax credits.

Article 4.1 – Adjusted Covered Taxes

Step 1

Article 4.1.1 – The starting point is the current year tax expense booked in the financial accounts (**only covered taxes listed in Article 4.2 are taken into account**)

Step 2

Step 1 needs to be adjusted by:

- Additions and reductions pursuant to Article 4.1.2 and Article 4.1.3
 - The Total Deferred Tax
- Increases/ decreases in Covered Taxes recorded in equity or Other Comprehensive Income
- Special case of Article 4.1.5

Adjustment Amount as per Article 4.4

Adjusted Covered Taxes

Step 3

Article 4.3 – We would also need to know to which entity are these taxes allocated

Step 4

Article 4.6 – Post-filing adjustments need to be taken into account

Step 1: Article 4.2 – Identification of Covered Taxes

Covered taxes	Scope
taxes or surcharges imposed on the net income from specific activities	imposed on the net income from specific activities (banking activities, the exploration and production of oil and gas), irrespectively whether or not they apply in addition to a generally applicable income tax
taxes on net income imposed at state and local government level	even though they are deductible for the purposes of income taxes imposed at the national government level
Pillar One taxes	paid on net income allocated to jurisdiction under Pillar One
taxes imposed under an Eligible Distribution Tax System	taxes on distributed profits, deemed profit distributions, and non-business expenses imposed under an Eligible Distribution Tax System (a corporate tax that is only paid when profits are distributed to shareholders or spent on specific non-business costs, that it must meet or exceed a minimum rate and must have been in force by July 1, 2021, see Article 10.1 of MR).
taxes in lieu of a generally applicable income tax	any form of taxes imposed as a substitute for standard corporate taxes and operating as alternatives to them (for example, withholding taxes interest, rents, and royalties, which substitute for regular income taxes, taxes based on non-income factors such as the number of units produced, commercial surface area, or simplified methodologies for specific business categories, like tonnage taxes, also taxes under STTR)
taxes on retained earnings and corporate equity	which can be regarded as an ex-ante income tax on the company (for example capital tax in Switzerland)
taxes based on multiple components	under the condition that all the components of the tax base fall within the definition of income or profit covered by the Pillar Two rules, or predominately are taxes on an entity's income (for instance Zakat levied by the Kingdom of Saudi Arabia)
taxes paid under CFC rules	provided that they are imposed on the income of the CFC that is attributed to shareholders in the parent jurisdiction

Step 1: Article 4.2 – Identification of Covered Taxes

Non-covered taxes	Scope
consumption and sales taxes	sales taxes and value-added taxes (VATs)
excise taxes	excise and other taxes on inputs
digital services taxes	Which are designed to apply to the gross revenues from the provision of certain digital services and so would not be considered an income tax
stamp and other transfer taxes	stamp duty, ad valorem taxes and other taxes are they are imposed on a particular transaction are not taxes on income or taxes in lieu of an income tax
payroll taxes and social security contributions	payroll taxes and social security contributions as they are not imposed on the employer in respect of its income
property taxes	property taxes are based on the assessed value of the property instead of income, retained earnings, or corporate equity; neither are they taxes imposed in lieu of a generally applicable income tax

Step 2 – The Adjustment Landscape vis-à-vis Covered Taxes

Article 4.1.2 Four Mandatory Additions

- **Article 4.1.2 (a)** – amount of Covered Taxes accrued as an expense in the profit before taxation in the financial accounts; e.g. capital tax is booked as expense in profit and loss account. Thus, it is added back to GloBE income and added to covered tax
- Article 4.1.2 (c) – amount of Covered Taxes that is paid in the Fiscal Year and that relates to an uncertain tax position where that amount has been treated for a previous Fiscal Year as a Reduction to Covered Taxes under Article 4.1.3(d); e.g. the TP policy which could be disputed (e.g. mark up for an R&D center) is recorded as a UTP and which then actually leads to additional payment of taxes
- Article 4.1.2 (d) – amount of credit or refund in respect of a Qualified Refundable Tax Credit / MTTC that is recorded as a reduction to the current tax expense e.g. QRTC is reduced from covered taxes. In this case, it needs to be added back to covered taxes and to GloBE income
- Elective Adjustment which becomes Mandatory: Article 4.1.2 (b) – amount of GloBE Loss Deferred Tax Asset used under Article 4.5.3;

Article 4.1.3 Five Mandatory Reductions

- **Article 4.1.3 (a)** – the amount of current tax expense with respect to income excluded from the computation of GloBE Income or Loss under Chapter 3; e.g. dividends received by a substantial shareholder are excluded. Thus, any taxes linked to these dividends should also be excluded for the recipient
- Article 4.1.3 (b) – amount of credit or refund in respect of a NQRTC that is not recorded as a reduction to the current tax expense; e.g. NQRTC is treated as income. In this case, it is reduced from GloBE income and from covered taxes
- Article 4.1.3 (c) – amount of Covered Taxes refunded or credited, except for any QRTC, to a CE that was not treated as an adjustment to current tax expense in the financial accounts;
- **Article 4.1.3 (d)** – the amount of current tax expense which relates to an uncertain tax position; e.g. the TP policy which could be disputed which could lead to more payment of taxes in the future
- Article 4.1.3 (e) – amount of current tax expense that is not expected to be paid within 3 years of the last day of the Fiscal Year. E.g. taxpayer does not pay the taxes

Step 2 – The Adjustment Landscape for Deferred Taxes – Highly complex

Deferred tax expense must be recast to 15 % if the applicable tax rate is above 15 %

Art. 4.4.1 Exclude deferred tax expense related to:

- Items excluded from the computation of GloBE Income or Loss under Chapter 3;
- Disallowed Accruals and Unclaimed Accruals;
- Valuation adjustments and accounting recognition adjustments;
- Re-measurement in relation to a change in the applicable domestic tax rate;
- Generation & use of tax credits.

Art. 4.4.2 Adjusted for the following:

- **Increased:** By the amount of any payments made during the year in relation to Disallowed Accruals and Unclaimed Accruals;
- **Increased:** By the amount of any Recaptured Deferred Tax Liability determined in a previous year, that is paid in the current year;
- **Reduced:** By the amount of deferred tax assets for GloBE purposes, where in instances valuation allowance or accounting recognition adjustments prohibit the recording of the DTA during the year in which the loss relates.

Art. 4.4.3 / 4.4.4 / 4.4.5 Recast & Recapture

- **Recast:** DTAs if recorded below 15%, recast to 15% (loss case)
- **Recapture:** For DTLs that do meet the Recapture Exception Accrual criteria, and the DTL does not reverse in 5 years, then the remaining amount is treated as a reduction to covered taxes.

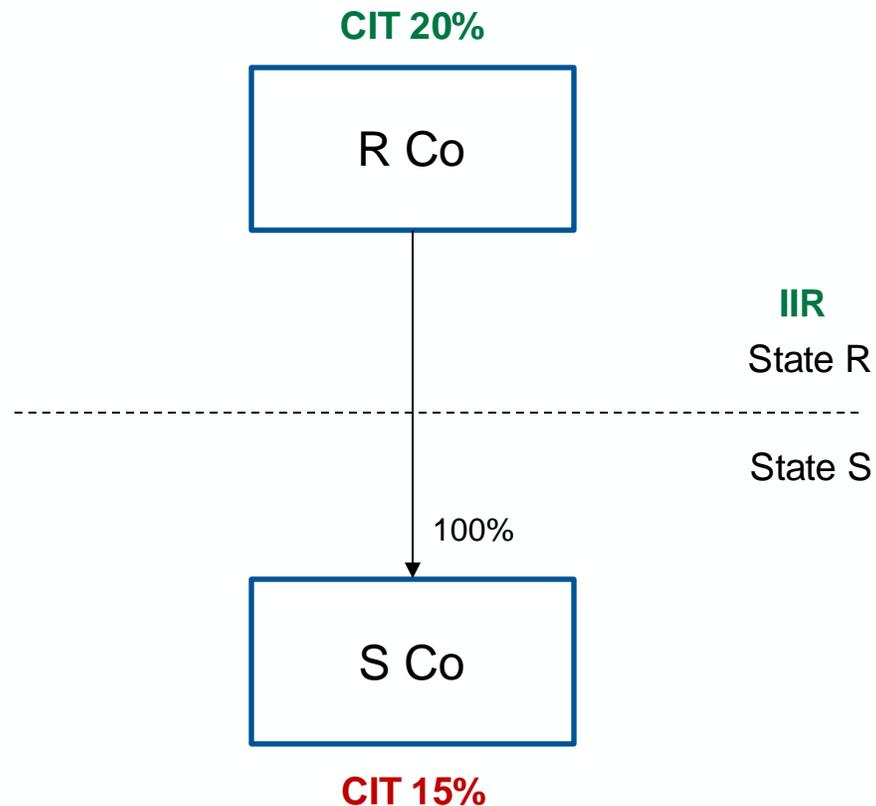
Specific Topics – Tax Losses

- Top-up taxes for loss-making entities;
- Loss-making Parent Entities of CFCs.

Art. 4.5 The GloBE Loss Election

- If applicable, consider using the GloBE Loss Election to waive the requirements under Article 4.4.

Case study: Recapture rules – Immediate expensing – intangible assets



Case study

- R Co is UPE of the MNE Group and it is resident in State R which has implemented IIR.
- It owns 100% of S Co resident in State S.
- State S offers an expenditure-based tax incentive which is immediate expensing of acquired trademarks for tax purposes, which under financial accounting rules are amortised over a period of 10 years.
- State R has implemented the IIR. The tax rate in State S is 15% and it has not implemented any domestic minimum tax, including QDMTT.

Solution – with recapture

	Taxable income accounts									
Year	1	2	3	4	5	6	7	8	9	10
Income	1000	1000	1000	1000	1000	1000	1000	1000	1000	1000
Expense	1000	0	0	0	0	0	0	0	0	0
Profit	0	100	100	100	100	100	100	100	100	100
Tax rate	15%	15%	15%	15%	15%	15%	15%	15%	15%	15%
Current Tax Expense (A)	0	150	150	150	150	150	150	150	150	150

With recapture	Financial and GloBE Accounts										
Year	1	1 adj.	2	3	4	5	6	7	8	9	10
Income	1000		1000	1000	1000	1000	1000	1000	1000	1000	1000
Expense	100		100	100	100	100	100	100	100	100	100
Profit	900		900	900	900	900	900	900	900	900	900
Current Tax Expense (A)	0		150	150	150	150	150	150	150	150	150
Deferred Tax Amount	900		-100	-100	-100	-100	-100	-100	-100	-100	-100
Deferred tax rate	15%		15%	15%	15%	15%	15%	15%	15%	15%	15%
Deferred Tax Expense (B)	135		-15	-15	-15	-15	-15	-15	-15	-15	-15
Covered Taxes (A+B)	135	135-75=60	135	135	135	135	135+15=150	135+15=150	135+15=150	135+15=150	135+15=150
Globe Income	900	900	900	900	900	900	900	900	900	900	900
ETR	15%	6.66%	15%	15%	15%	15%	15%	16.66%	16.66%	16.66%	16.66%
Top-up tax	0	75.96	0	0	0	0	75.96	0	0	0	0

How immediate expensing of intangibles impacts the ETR ?

Article 4.4.4 read with 4.4.5 (a):

If deferred tax liability is not reversed within the 5 subsequent Fiscal Years, the amount must be recaptured.

The Amount of the Recaptured Deferred Tax Liability determined for the current Fiscal Year shall be treated as a reduction to Covered Taxes in the 5th preceding Fiscal Year and the ETR and Top-up Tax of such Fiscal Year shall be recalculated

Leads to Additional Current Top Up Tax in Year 6

Step 3: Article 4.3 – Allocation of Covered Taxes under GloBE

General principle Article 4.4.1

- Covered Taxes are allocated to the CE that includes the corresponding income in the computation of its GloBE Income or Loss and which are taken into account in the ETR computation for the jurisdiction in which the CE is located

Withholding taxes on interest, royalties and service fees payments

- allocated to the receiving CE

Taxes with respect to Tax Transparent Entity Article 4.3.2 (b)

- are allocated to that CE owner

Withholding taxes on intra group dividends Article 4.3.2 (e)

- are allocated to the distributing CE

CFC taxes (as well as dividend taxes) Article 4.3.2 (c)

- are allocated to the CE whose income is subject to CFC tax and not to the CE-owner which pays the CFC taxes

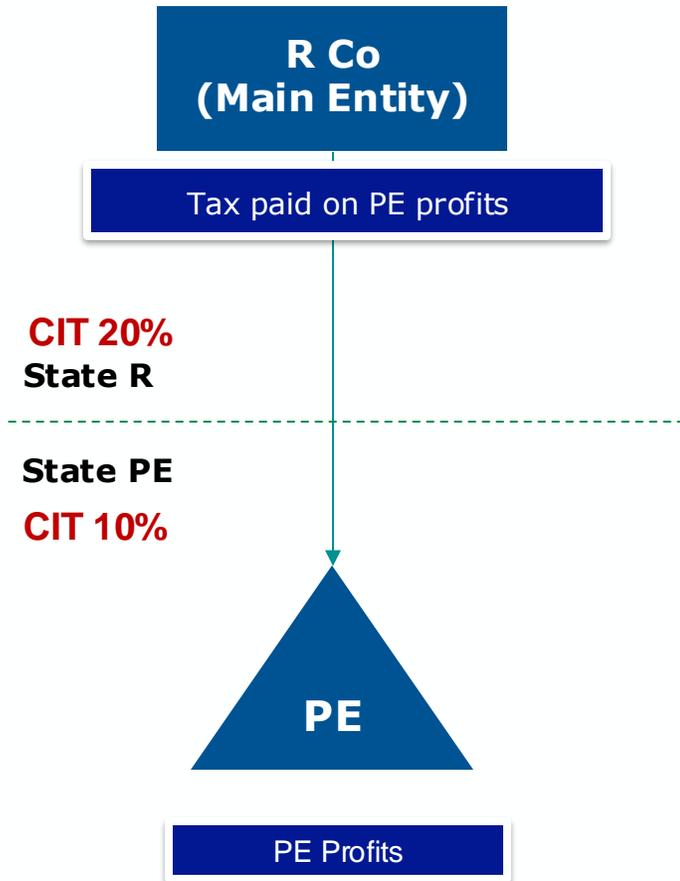
Taxes with respect to PE levied at the level of the Main Entity Article 4.3.2 (a)

- are allocated to PE

Taxes with respect to Hybrid Entity levied at the level of the owner Article 4.3.2 (d)

- are allocated to the Hybrid Entity

Taxes levied at the Main Entity Level – GloBE vs QDMTT

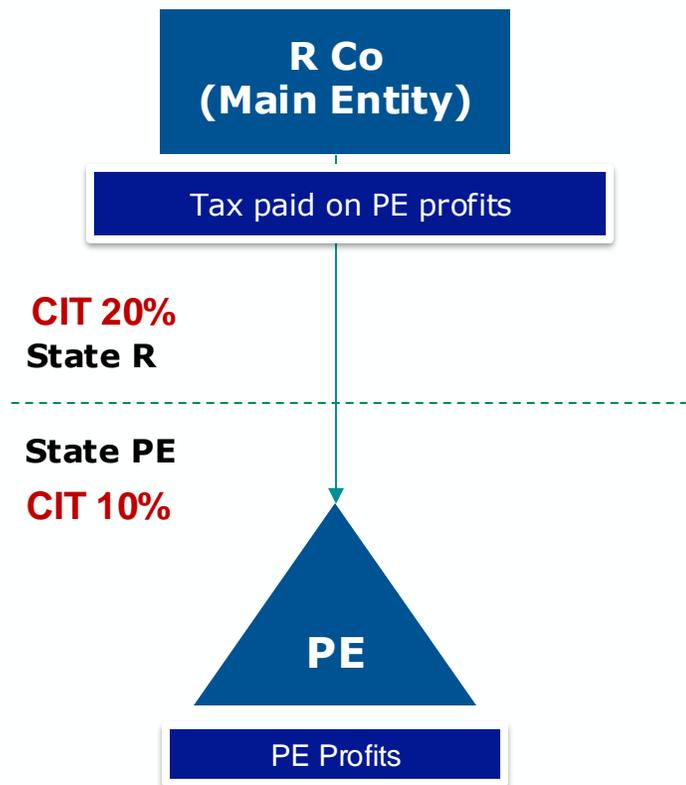


Facts

- R Co is a company resident in State R.
- It has a PE in State PE. State R tax rate is 20%.
- State PE tax rate is 10%.
- PE earns 100 of taxable profit and PE pays $100 \times 10\% = 10$ of tax to State PE.
- R Co pays $(100 \times 20\%) - 10 = 10$ of tax to State R.

How much of taxes should be allocated to PE under IIR and QDMTT?

Mandatory Variation: Case Study – PE and QDMTT



GloBE IIR

- The amount of any Covered Taxes included in the financial accounts of a CE with respect to GloBE Income or Loss of a PE is allocated to the PE (Article 4.3.2. (a)).
- Computation of Covered Taxes arising in the Main Entity in respect of the PE income:
 - Step 1: determine the amount of the PE income that is included in the Main Entity's local taxable income
 - Step 2: determine the Main Entity's tax liability arising from inclusion of the PE income
 - Step 3: determine the tax credit, if any, allowed in respect of Taxes paid by the PE
- The amount of taxes paid on PE income inclusions is the excess of the tax liability arising from the PE income inclusions over any credit allowed for the PE's taxes on its income, so in case presented is $20-10=10$
- **10 of taxes is excluded from R Co's Covered Taxes and allocated to the PE because that is the actual liability with respect to the PE income – Taxes paid at the main entity level are pushed down**

QDMTT

- OECD Administrative Guidance – Para 118.30: ***"A QDMTT shall exclude tax paid or incurred by... a Main Entity that is allocable under Article 4.3.2(a) to a Permanent Establishment located in the jurisdiction"***
- **10 of taxes is not pushed down when the QDMTT applies**