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Tax Newsflash

Global minimum tax payable by large groups of companies enters into force

Law 431/2023 on ensuring a global minimum level of taxation of large multinational and national enterprise groups ("Law 431") was published in the Official Journal of Romania No. 8/2024 and entered into force on 8 January 2024. The legislation transposes into national law the provisions of Directive 2523/2022 on ensuring a minimum level of taxation ("Directive 2523"), which incorporates the guidelines of the second pillar of the "Global Anti-Base Erosion Model Rules" (hereafter referred to as the "GloBE Rules") issued by the OECD/G20 Inclusive Framework on BEPS, as well as the Administrative Guidelines on the GloBE Rules.

Background

In an ongoing effort to address aggressive tax treatments applied by multinational groups of companies that may result from the non-taxation of profits where value is created, since 2015 the OECD has developed a series of 15 actions aimed at discouraging such aggressive tax treatments (BEPS Actions). These have led to the adoption of tangible measures in international taxation in subsequent periods, such as the amendments to the EU Directive 16/2011 on administrative cooperation (the Directive that introduced CRS rules, reporting under DAC6, DAC7, etc.).

As a further step, in 2021 the OECD published an agreement to address aggressive tax planning - the Inclusive Framework, which is based on two pillars:

- *Pillar One* - includes provisions to allocate taxing rights to those jurisdictions where companies earn profits. Discussions are currently underway on the multilateral convention that will apply under this pillar.
- *Pillar Two* – establishes a minimum effective tax rate of 15% across all jurisdictions that are part of the Inclusive Framework.

At EU level, the Pillar Two provisions were transposed by Directive 2523, which was unanimously approved by all Member States at the end of 2022. Achieving the necessary consensus for a unanimous vote required considerable negotiation given the contentious nature of the issue, and consequently we would not now expect to see significant changes.

KPMG Observations

- In Romania, the provisions that will regulate the taxation rules under Pillar Two were introduced in a special law (Law 431/2023) and were not implemented as an amendment to the Fiscal Code (Law 227/2015).
- The new provisions introduced by Law 431 are very complex. The calculations for any top-up tax that might result from applying the new rules are different from the traditional methods of calculating corporate income tax. The general rule in this case would be to calculate the Pillar Two amounts based on indicators included in the groups' consolidated financial statements.
- Although the nominal statutory corporate tax rate in Romania is 16%, the rules introduced by Pillar Two involve the calculation of a top-up tax based on an effective tax rate of 15%. There may be situations (e.g. where certain tax incentives are applied) which may lead to an effective tax rate below 15%, in which case an additional top-up tax would need to be calculated at jurisdiction level.

- Another new element in the new rules means calculating the 15% effective tax rate for each financial year at **jurisdiction level and not at entity level**. In other words, if a group of companies has three entitites in Romania, the indicators at the level of all Romanian companies will be cumulated to determine the effective tax rate in Romania.
- Article 5 of Law 431 clearly mentions that the provisions of Law 431 will be applied together with the Administrative Guidelines published by the OECD. The OECD is continuously working on issuing new administrative guidelines (three such publications were issued in 2023). This brings additional complexity to the application of this law as any additional legislation/guidelines published in the future by the OECD on the applicability of the Pillar Two rules will also need to be taken into account. The Administrative Guidelines, as well as other material issued by the OECD, are published on the OECD website.

General aspects

Groups of companies subject to the Pillar Two rules

The Pillar Two rules apply to large groups of companies, both national and multinational, with a consolidated turnover (at group level) of at least 750 million euros in at least two of the four years preceding the reference year. For example, consolidated turnover for 2020, 2021, 2022 and 2023 needs to be determined in order to conclude whether the rules are applicable for 2024 at group level.

If the group of companies reaches the minimum turnover under the scope of the Pillar Two rules, the following steps should be taken to determine whether there is a potential top-up tax due under the new rules.

1. Identification of in-scope entitites

If the group meets the minimum turnover requirements, the first step would be to identify the types of entity in the group, specifically which are the constituent entities (i.e. those to which the rules will apply) and whether there are any excluded entities within the group.

The Pillar Two legislation lists a number of entities which are excluded from the requirement to pay the top-up tax: government entities, international organisations, non-profit organisations, pension funds, investment funds and real estate investment vehicles that are ultimate parent entities (UPE) of the group. Furthermore, certain categories of entity may qualify as excluded entities as long as they are owned by an excluded entity (ownership of at least 85%) and carry out certain activities.

Although excluded entities are not subject to the GloBE rules (they will not be included in the calculation of the effective tax rate or other specific indicators), their turnover is taken into account when determining the minimum 750 million euro threshold.

2. Calculation of the effective tax rate (ETR)

As mentioned above, this effective tax rate is calculated at jurisdiction level (and not at entity level). The ETR formula includes in the numerator the adjusted covered taxes ("covered taxes") of the constituent entities in a jurisdiction and the qualified net income ("GloBE income") of the constituent entities in that jurisdiction as the denominator.

Adjusted covered taxes and *qualified net income* are calculated based on the amounts included in the group's consolidated financial statements, to which certain fiscal adjustments need to be applied. The purpose of these adjustments is to align the tax base which is calculated at global level under Pillar Two rules with the applicable local tax adjustments and allocation of profits between jurisdictions, if the case.

If the effective tax rate exceeds 15%, no top-up tax for that jurisdiction is due under the Pillar Two rules in that financial year.

KPMG Observations

The fiscal adjustments to calculate the ETR are complex and many types of adjustment listed by the legislation are not applicable under Romanian tax law. The ETR calculation at jurisdiction level involves reviewing all the adjustments included in the legislation and identifying those adjustments that are applicable under local law to a group of companies which is present in Romania.

3. Top-up tax calculation

If the effective tax rate at jurisdiction level is below 15%, top-up tax needs to be calculated (at jurisdiction level as well) using the formula:

Top-up tax = top-up tax percentage x excess profit

The top-up tax percentage is the difference between the minimum rate of 15 percent and the ETR of the jurisdiction.

The excess profit is the positive difference, if any, between the GloBE income and losses of all constituent entities in the jurisdiction over a substance – based income carve out (SBIE). The formula for SBIE calculation takes into account the number of employees and the intangible assets in a certain jurisdiction.

4. Imposition and allocation of top-up tax

The top-up tax can be allocated to a certain jurisdiction under the three rules which need to be applied in the following order:

1) *Qualified Domestic Minimum Top Up Tax (QDMTT).*

The QDMTT is an option that some countries, including Romania, have implemented in their national legislation, whereby the top-up tax is calculated and paid in the jurisdiction in which the low taxed entities are located (where the effective tax rate is less than 15%). The system for calculating the top-up tax closely follows the principles of the GloBE rules and applies to group entities located in the jurisdiction applying the QDMTT.

Romania has chosen to implement this system (according to Article 17 of Law 431), i.e. any top-up tax for Romanian constituent entities will be calculated under QDMTT rules and paid to the Romanian tax authorities.

The top-up tax is calculated at jurisdiction level and will be allocated to the Romanian constituent entities based on a formula that takes into account the proportion of the qualifying profit of the constituent entity to the aggregate qualifying profit of all Romanian constituent entities.

The QDMTT applies in Romania from 1 January 2024.

2) *Top-up tax under the Income Inclusion Rule (IIR)*

Under this rule, the top-up tax is calculated and paid in the jurisdiction of the ultimate parent entity (UPE) for the jurisdiction in which the low taxed entities are located. The IIR applies as long as a jurisdiction does not have the QDMTT system in place, so that the taxing rights of the low-taxed jurisdiction are attributed to the UPE.

The IIR applies in Romania from 1 January 2024.

3) *Top-up tax under the Undertaxed Profits Rule (UTPR)*

The UTPR serves as a backstop to the QDMTT and IIR for calculating and collecting the top-up tax, if it has not been collected by the above mentioned methods. The UTPR applies where a jurisdiction has not implemented the QDMTT, the ultimate parent entity is resident for tax purposes in a jurisdiction that does not apply a qualified IIR or where the ultimate parent entity is an excluded entity.The top-up tax for a low taxed jurisdiction will be allocated through the UTPR to all jurisdictions applying the GloBE rules based on an allocation key that takes into account the number of employees and the value of fixed assets in a jurisdiction proportional to the total number of employees and total fixed assets in all jurisdictions applying the GloBE rules.

In Romania, the top-up tax will be payable as an additional tax in the amount of the top-up tax allocated under UTPR to the Romanian constituent entities.

The UTPR will apply in Romania from 1 January 2025.

KPMG Observations

- Romania implemented the QDMTT from 1 January 2024, which in practical terms means that the top-up tax at the level of Romanian constituent entities that are low taxed is calculated according to the QDMTT rules (Article 17 of Law 431) and will be collected, declared and paid to the Romanian tax authorities.
- A very important point is that Romania has also implemented the QDMTT safe harbour regime, which means that, in principle, no additional top-up tax will be calculated at the level of the ultimate parent entity under the IIR and the UTPR. The top-up tax calculated according to the QDMTT and paid in Romania would be final.

5. Administration and filing obligations

Reporting of the top-up tax

Any EU-based constituent entity is required to file an informative return on the top-up tax calculated at group level (GIR - Global Income Return). A reporting relief is available if the GIR is filed either by the ultimate parent entity or by another designated entity within the group, as long as there is an exchange of information agreement between the jurisdiction of the filing entity and the jurisdiction of the constituent entity.

The GIR must to be filed within 15 months of the end of the financial year, except for the first year of application, for which the deadline is 18 months after the end of the financial year.

Reporting of the top-up tax calculated under QDMTT

Similarly to the above, the top-up tax calculated under the QDMTT rules needs to be declared and paid by Romanian-based constituent entities within 15 months of the end of the financial year (18 months for the first financial year). The model and format of the local return is not yet available. This will be published by ANAF within 12 months of the entry into force of Law 431/2023.

KPMG Observation

- The GIR template was published in July 2023. This is a complex return (the blank return contains 28 pages) that will need to include a large amount of information such as ETR calculations, top-up tax calculations, safe harbour application, etc.

Safe harbours

The safe harbours adopted by the OECD represent certain simplification measures, as it is universally agreed that the Pillar Two rules are very complex and in some cases would create excessive administrative burdens for certain groups of companies or low tax risk jurisdictions. Some simplification measures are transitional (i.e. they may apply for a limited period) and some will be permanently available. See below a brief presentation of the safe harbours adopted so far in Romania.

Transitional safe harbours

Country by Country (CbyCR) transitional safe harbour rules

- These apply to large multinational and national groups that prepare CbyCR reports based on qualified financial statements.
- The top-up tax is zero at jurisdiction level if at least one of three tests (de minimis test, simplified ETR test, routine profits test) is met.
- The calculations for the tests previously mentioned are based on certain indicators included in the CbyCR reports.
- The CbyCR safe harbour will apply for financial years beginning on or before 31 December 2026 but these must not end later than 30 June 2028 (for groups of companies where the financial year is the calendar year, the option will be available for 2024, 2025 and 2026).

UTPR safe harbour

- The top-up tax is deemed to be zero for the Ultimate Parent Entity (UPE)'s jurisdiction where that jurisdiction's nominal corporate tax rate is at least 20%.
- It will apply for financial years beginning on or before 31 December 2025 and end before 31 December 2026 (i.e., 2024 and 2025 for calendar year taxpayers).

Permanent safe harbour

QDMTT safe harbour

- The top-up tax calculated under the IIR and UTPR is zero as long as the top-up tax under Domestic Minimum Top Up Tax is **qualified** and certain conditions are met.
- The qualified status of the top-up tax is determined based on an OECD peer review.

The „de minimis" exclusion

- The top-up tax for a financial year is deemed to be zero in a jurisdiction as long as certain conditions are met. (The average qualifying revenue of all Romanian constituent entities must be less than 10 million euros and the average qualifying income or loss must be less than 1 million euros).

KPMG Observations

- The option to apply one of the safe harbours must be included in the Global Income Return (GIR) on an annual basis.
- The application of a safe harbour regime does not remove the requirement to submit an annual GIR.
- Certain simplification measures must be applied from the first year in which the group of entities would qualify to apply them, or they will not be available in subsequent periods (the "once out, always out" approach). Thus, we recommend that the analysis of whether a particular safe harbour regime applies should be carried out as early as possible.
- Although the deadline for reporting and paying the top-up tax under the GloBE rules may currently seem permissive, we recommend that such a complex exercise should be managed in a timely manner by groups of companies to ensure that they will be able to implement all the measures introduced by the new rules. Also, certain accounting disclosures may be required prior to the first reporting deadline (e.g. in 2026).

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