Briefing

International review for March

Speed read

In what might mark the start of divergence in international implementation of the global minimum tax, Singapore, Hong Kong and Thailand have announced the Pillar Two rules will be effective from 2025, rather than 2024. In the US, the FY 2024 Budget proposes significant tax increases for companies, investors and wealthy individuals, but divisions in Congress mean it is unlikely any of these proposals will become law, at least in the short term. Europe continues its efforts to keep pace with the US on green incentives, with temporary relaxation of state aid rules. The OECD has published a report on the latest developments in international tax reform. Brazil has issued further guidance on its new OECD-aligned transfer pricing regime. Finally, multinationals should note the latest changes to the EU list of non-cooperative jurisdictions and consider the broader implications for DAC 6 and EU public country by country reporting.

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Pillar Two national implementation update

On 14 February 2023, Singapore presented its 2023 Budget. One of the major announcements was the implementation of Pillar Two, including a domestic minimum top up tax (DMTT). Singapore had previously indicated it would implement the global minimum tax, and was widely anticipated do so from 2024 in line with other jurisdictions. However, in an unexpected development it has chosen to implement the rules from January 2025.

Hong Kong followed suit in its Budget announcement on 22 February 2023, confirming the global minimum tax and a DMTT would apply from 2025 onwards.

On 7 March 2023, the Thai Cabinet approved in principle measures to support the implementation of Pillar Two. The indicative timetable is for draft legislation to be published this year with the rules being effective from 2025 at the earliest.

These announcements could well mark the beginning of a 2025 implementation trend in the Asia Pacific region. Two 'waves' of Pillar Two adoption (2024 and 2025) would further complicate the landscape for multinational enterprises (MNEs) working hard to prepare for implementation of the global minimum tax.

US FY 2024 Budget

On 9 March 2023, the Biden administration transmitted its FY 2024 Budget recommendations to Congress. The Green Book publication outlines significant tax increases for US corporations, investors and wealthy individuals as part of a plan to reduce the Federal deficit by almost $3 trillion over the next decade. Key tax raising measures include:

- increasing the statutory corporate rate to 28%;
- increasing the excise tax rate on repurchase of corporate stock to 4%;
- treating certain corporate distributions to shareholders as dividend or dividend equivalents;
- increasing the top individual income tax rate from 37% to 39.6%;
- taxing long-term capital gains and qualified dividends at ordinary rates for taxpayers with adjusted gross income exceeding $1m (applicable to gains required to be recognised after the date of enactment); and
- imposing a 25% minimum tax on total income (generally inclusive of unrealised capital gains) for all taxpayers with wealth greater than $100m.

Measures designed to align the US tax system with the global minimum tax include:

- reducing to 25% the deduction for global intangible low-taxed income (GILTI), eliminating the qualified business asset investment (QBAI) exemption, and imposing a jurisdiction-by-jurisdiction calculation;
- repealing the deduction for foreign-derived intangible income (FDII); and
- replacing the base erosion anti-abuse tax (BEAT) with a new undertaxed profits rule that is consistent with the Pillar Two model rules.

Action on most of the tax proposals in the FY 2024 Budget is unlikely in the short term. With a divided Washington the prospects for enactment are narrow, and one might question the relevance of the Budget announcement. In the near term, the proposals are important in the context of the forthcoming US elections: the Biden administration has set forth its vision of what the tax system should be, and that will no doubt become a theme of the 2024 presidential and congressional elections.

Further away from home, countries seeking to implement Pillars One and Two will be paying close attention, and we are likely to see the international tax announcements as reassurance of the US's commitment to the BEPS 2.0 project.

In the longer term, the announcements are significant because budgetary proposals, once released, never truly disappear. These ideas have a long shelf life in the tax policy world and are likely to reappear in various formats in the years (perhaps decades) to come.

EU: temporary state aid rules to support green transition

The EU has continued to respond to the incentives provided in the US Inflation Reduction Act (IRA) with a significant relaxation of the otherwise strict EU state aid rules. On 9 March 2023 the new Temporary Crisis and Transition Framework (TCTF) was adopted as part of the broader Green Deal Industrial Plan covered in my February article.

Under the new framework, that applies until 31 December 2025, member states are allowed to implement schemes to support new investments and production facilities in defined, strategic net-zero sectors. Support can be structured as direct grants or as tax advantages (for example, tax credits) loans or guarantees. A cap applies, both in terms of nominal values (ranging from €150m to €350 m per company per member state) and a percentage of support over total investment costs.

In exceptional cases where there is a real risk of investment being diverted away from the EU, member states are allowed to provide higher support to individual companies, with the option to provide a matching aid (matching the amount of support the company could receive for an equivalent investment in that alternative location) or cover a funding gap (amount needed to incentivise the company to locate the investment in the EEA). Member states are required to select the lowest amount of these two options. Strict safeguards are also introduced, related to the location of the projects and the technology to be used from an environmental emissions perspective. Similar to the general schemes, the individual aid may not be provided to facilitate relocation of production activities between member states.

The US action on green incentives will continue to cause waves across the EU and further afield in the coming months, as territories try to stay competitive on green investment.

OECD update on international tax reform

On 24 February 2023, the OECD published the *Secretary-general tax report to the G20 finance ministers and central bank governors* providing updates on the latest developments in international tax reforms. Key updates include:

Pillar One: Following a year of consultation with stakeholders and the public, whilst some of the building blocks of Amount A are relatively stable, several aspects remain subject to ongoing negotiations. Inclusive Framework (IF) delegates are now working 'around the clock' to agree the text of a Pillar One Amount A Multilateral Convention (MLC) to be opened for signature by mid-2023.

The IF confirmed it is currently working through the responses it received to the December 2022 public consultation on the main design elements of Amount B, however no further information was provided on the expected timetable for further releases.

Pillar Two: As outlined in my February article, following the release of the Administrative Guidance in February 2023, the IF will continue to release further agreed administrative guidance on an ongoing basis to ensure the Pillar Two Rules continue to be implemented and applied in a coordinated manner. The IF recognises that the subject to tax rule (STTR) is an integral part of achieving consensus on Pillar Two for developing countries. The STTR is a treaty-based rule that allows source jurisdictions to impose taxes on certain related party payments not subject to an agreed minimum rate of 9%. Work on the STTR and its commentary is well advanced, and the IF is continuing its work to reach a compromise on the remaining outstanding issues to enable signature of the STTR multilateral instrument by mid-2023.

Capacity building: Developing countries account for around half of the membership of both the IF and its steering group: building tax capacity to implement international tax reform across all members of the IF therefore continues to be a priority.

Inclusive forum on carbon mitigation approaches (IFCMA): The IFCMA is designed to support individual countries' emissions reduction efforts through data and information sharing, evidence based mutual learning and inclusive multilateral dialogue. We can expect to hear more about the work of the IFCMA as we go through 2023.

Global forum on tax transparency and exchange of information on request (EOIR): International tax transparency efforts continue to yield sustained results, from the EOIR which raised almost €2.6bn in revenue for governments from 2019 to 2021, to the automatic exchange of financial account information (AEOI), which 120 jurisdictions have now committed to implement.

Brazil: guidance on OECD-aligned transfer pricing rules

Last April, I reported that, in something of a quantum leap, Brazil announced that it would align its unique transfer pricing regime to the OECD's transfer pricing paradigm. On 28 December 2022, the government issued Provisional Measure No. 1,152 (the 'provisional measure'), which, but for a few minor issues, incorporated all the proposed changes. Taxpayers must apply the new rules to their Brazilian intercompany transactions for taxable periods beginning on or after 1 January 2024, but have the irrevocable option to apply them early for their 2023 taxable period.

On 17 February 2023 the Brazilian tax authorities published a first 'normative instruction' providing further guidance on the new regime. MNEs already conducting impact assessments on the new rules should factor this latest development into their analysis. The normative instruction includes information for early adopters (who must make such an election in September 2023) and information on the criteria for carrying out transfer pricing adjustments throughout the year. It also gives further guidance on the deductibility of royalty payments, which have historically been subject to severe restrictions by Brazil.

Changes to the EU list of non-cooperative jurisdictions

On 14 February 2023, the Council of the European Union (EU) updated the list of non-cooperative jurisdictions. The Council agreed to add the Marshall Islands to Annex I (the 'blacklist') and move three jurisdictions from Annex II (the 'grey list') to Annex I: British Virgin Islands, Costa Rica and Russian Federation.

Following this latest revision, the EU blacklist now consists of the following 16 jurisdictions: American Samoa, Anguilla, the Bahamas, British Virgin Islands, Costa Rica, Fiji, Guam, Marshall Islands, Palau, Panama, Russian Federation, Samoa, Trinidad and Tobago, Turks and Caicos Islands, US Virgin Islands and Vanuatu.

In addition, Albania, Aruba and Curaçao were added to the grey list while four jurisdictions (Barbados, Jamaica, North Macedonia and Uruguay) were removed from the grey list as they had fulfilled their previous commitments. As a result, the grey list now includes the following 18 jurisdictions: Albania, Armenia, Aruba, Belize, Botswana, Curaçao, Dominica, Eswatini, Hong Kong, Israel, Jordan, Malaysia, Montserrat, Qatar, Seychelles, Thailand, Turkey and Vietnam.

It is more important than ever for taxpayers to monitor the evolution of the list in light of defensive measures that are being applied by EU member states against listed jurisdictions in the form of non-deductibility of costs, Controlled Foreign Company rules, increased withholding tax or limitation of participation exemption.

The list is also relevant for the purposes of the EU mandatory disclosure rules under DAC6, where recipients of cross-border payments are resident for tax purposes in a jurisdiction that is included in Annex I. Under Hallmark C1b (ii) of DAC 6, such payments may trigger a reporting obligation irrespective of whether the transaction is aimed at generating a tax benefit. Note that consensus has not formed among member states on the point in time at which the list should be tested (for example, the triggering date or the reporting date).

The list also has a direct impact on the EU public country by country reporting obligations that apply in relation to financial years starting on or after 22 June 2024. Under the rules, country by country information must be separately reported for each jurisdiction listed on Annex I or for each jurisdiction listed on Annex II for a minimum of two years (i.e. as opposed to the disclosure of aggregated amounts, which is the requirement for the rest of non-EU jurisdictions). ■

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- Pillar Two and the GloBE rules (J Burton, E Birkemeyer, N Lawton & M Fraser, 22.3.23)
- The Inflation Reduction Act 2022: less than promised? (D Korb & A Solomon, 6.10.22)