Council adopts EU Minimum Tax Directive

ECOFIN Council – BEPS 2.0 – GloBE Model Rules – Minimum Tax – EU Directive – Compromise Text – Unanimity

On December 15, 2022, the Council of the EU reached unanimous agreement to implement the EU Minimum Tax Directive.

The agreed compromise text (November 25, 2022) requires Member States to transpose the rules into domestic law by December 31, 2023 and to start applying the Income Inclusion Rule (IIR) for fiscal years beginning on or after December 31, 2023. The Undertaxed Profits Rule (UTPR) will be applied for fiscal years beginning on or after December 31, 2024.

In addition, the agreed compromise text provides the option for Member States to implement a qualified domestic top-up tax (QDMTT) and to defer the application of the IIR and the UTPR up to December 31, 2029, where a maximum number of 12 UPEs are based in that EU Member State.

Background

The European Commission published the initial Minimum Tax Directive proposal on December 22, 2021 after the OECD had published its Model Rules for the Global Anti-Base Erosion Rules (GloBE Rules) two days before, on December 20, 2021 (for more details, please refer to Euro Tax Flash Issue 463).

Following technical discussions in the Council working groups, a number of compromise texts were published in the course of 2022 and provided for several amendments, including to make reference to the ongoing work of the OECD, rectify areas of discrepancy between the Model Rules and the initial text and provide for a deferral option of up to six years for Member States where a maximum number of twelve UPEs are based in that Member State.

Amendments were also made to address reservations raised by Poland regarding the adoption of the EU Minimum Tax Directive independent of Pillar One. In this context, a specific provision was added to the compromise text requiring the Commission to submit a progress report to the Council on the implementation of Pillar One by June 30, 2023. Furthermore, the Commission committed to submit a legislative EU proposal in the absence of the implementation of the Pillar One solution at international level. In light of the amendments to the compromise text and the commitments provided by the European Commission, Poland advised that it could lift its reservations at the ECOFIN meeting in June 2022. However, in an unexpected development, the Hungarian delegation was no longer able to support the proposal, citing concerns regarding the economic consequences of introducing the Minimum Tax Directive, noting the need for further work on substantial and procedural questions related to the new rules and highlighting the expected delay in the Pillar One implementation timeline (for more details, please refer to Euro Tax Flash Issue 470). The file was therefore in deadlock between June and December 2022.

Following checks by linguists and lawyers, a new compromise version of the draft Directive was released on November 25, 2022. Although a vote on the new text was initially included on the agenda of the December 6 ECOFIN meeting, it was removed just prior to the meeting. The approval of the compromise text was therefore not discussed in the public session.

Approval of the EU Minimum Tax Directive

On December 12, 2022, the Council of the EU announced that Member States reached political agreement to implement the EU Minimum Tax Directive. The Czech Presidency noted that it was able to secure the required unanimous support of all Member States at a December 11, 2022 meeting of the Committee of Permanent Representatives (COREPER). According to subsequent statements, the Directive was discussed as part of the so-called "Hungarian package", together with the instruments allowing the EU to provide financial aid for Ukraine and Hungary's national recovery and resilience plan.

It was decided by the COREPER that the package would be formally adopted through a written procedure. The initial deadline set by the Council – December 14, 2022 – could, however, not be met due to ongoing reservations expressed by the Polish delegation. These were eventually resolved during the European Council summit on December 15, 2022.

A statement was attached to the Council conclusions recalling the European Union's determination to have both Pillar 1 and Pillar 2 implemented as agreed in October 2021. The note also calls on the Commission to put forward, if appropriate, a proposal by the end of 2023 if agreement at international level on a Pillar 1 solution is not reached.

On December 16, 2022, the Council issued a press release as well as the written procedure communication confirming the adoption of the EU Minimum Tax Directive (all delegations voted in favour of, except for Hungary that abstained) and the approval of the Council conclusion relating to Pillar 1 (all delegations voted in favour).

The Directive will enter into force on the day after its publication in the Official Journal of the EU, which is expected shortly.

November 25 compromise text

The agreed compromise text mainly includes linguistic and structural changes compared to the June 2022 version and remains closely aligned with the OECD GloBE Model Rules.

To achieve consistency with EU law, particularly with the freedom of establishment, the EU implementation of Pillar Two differs from the OECD Model Rules as follows:

- it is not limited to cross-border situations but also applies to domestic groups, and
- it requires the application of the IIR at the level of an EU parent entity located in a low-taxed jurisdiction not only with respect to its low-taxed foreign subsidiaries (as per the Model Rules) but

also with respect to all low-taxed constituent entities resident in the same Member State of that parent.

The November 2022 compromise text also clarifies the power of the European Commission to adopt delegated acts to supplement certain non-essential elements of the directive. Such acts would be used when determining the jurisdictions with a domestic legal framework which can be considered to be equivalent to a qualified IIR. This assessment would be performed by the EC, after appropriate consultations, including with experts appointed by member states.

For a more detailed comparison of the Directive and the OECD GloBE Model Rules, please refer to the following table:

	Model Rules	Agreed EU Minimum Tax Directive
General approach	- Common approach	- Compromise text generally mirrors the OECD Model Rules. - Reference to the OECD Commentary and GloBE Implementation Framework - Main exceptions due to alignment of the rules with EU law.
Scope	- Scope limited to MNE groups that meet the revenue threshold test of EUR 750 million.	- Scope extended to large-scale domestic groups that meet the revenue threshold test of EUR 750 million.
IIR	- IIR limited to cross-border situations - Option provided by the Commentary to extent the application of IIR to domestic situations.	- IIR extended to domestic situations
Domestic (Minimum) Top-up tax	- Option to apply a qualified domestic (minimum) top-up tax to Constituent Entities (CEs) located in their territory.	- Optional qualified domestic top-up tax (QDTT) - Safe harbor rule in respect of QDTT - QDTT must be imposed within four years
Safe Harbor	- Elective to-be-developed Safe Harbor which applies on a jurisdictional basis, and, assuming the MNE is eligible, has the effect of reducing the top-up tax for the relevant jurisdiction to zero in the eligible year.	- Jurisdictional top-up tax will be zero where the effective level of taxation of the CE located in that jurisdiction fulfils the conditions of the agreed GloBE Implementation Framework.
Penalties	- Application of national laws with respect to penalties, sanctions and the confidentiality of returns and return information	- Penalties to be applied for infringement of national provisions in an effective, proportionate and dissuasive manner in order to ensure that CEs in their territory comply with their obligations to file and pay their share of top-up tax or to have an additional cash tax expense.
Transposition timeline	- Model Rules to be brought into law in 2022 to be effective in 2023 with	- Transposition deadline of December 31, 2023,

	the UTPR coming into effect in 2024.	- IIR to apply for fiscal years beginning on or after December 31, 2023; and - UTPR to apply for fiscal years beginning on or after December 31, 2024.
Optional deferral	- Not available	- Optional deferral up to December 31, 2029 of the application of IIR and UTPR, where no more than 12 UPEs of in-scope MNE groups are located in a Member State - Application of UTPR by those Member States that do not opt for the deferral, where the Member State that makes use of the deferral election is low-taxed.

ETC Comment

With the EU Directive now in place, all eyes now turn to the OECD Inclusive Framework and the completion of the work on the GloBE Implementation Framework, including the eagerly anticipated transitional and permanent safe harbor provisions. At this stage, it seems that some elements of the Implementation Framework are still work in progress and a release can be expected shortly. It remains to be seen which elements of the package the Inclusive Framework were able to be approved or finalized for public consultation.

Given the reference to the Implementation Framework in the agreed EU text, it remains to be seen how Member States will incorporate those additional provisions and administrative clarifications in their national implementation. Generally, the Directive requires Member States to transpose the rules into national law by December 31, 2023. In this context, the Netherlands already conducted a public consultation on a legislative proposal to implement the GloBE Rules in line with the EU June 2022 compromise text (for more information, please refer to E-News Issue 164). In addition, the French and German Ministries of Finance announced their intention to publish a first implementation draft law for discussion in early 2023. Now that the Directive has been adopted, other Member States will have to follow suit.

Another question is whether any of the Member States that qualify for the deferral option (i.e. those with no more than 12 UPEs) will eventually make use of that option and decide to apply the IIR and UTPR at a later stage (December 31, 2029 at the latest).

Should you have any queries, please do not hesitate to contact KPMG's EU Tax Centre, or, as appropriate, your local KPMG tax advisor.

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