KPMG

# GloBE Updated Administrative Guidance

**February 2023**

The GloBE Administrative Guidance (AG) was released on 2 February 2023. It covers 26 items in 111 pages and sets out to clarify, and in some instances also simplify, the application of the GloBE rules. Each item of the AG refers to a particular section of the Commentary, and a revised version of the latter (originally released on 14 March 2022) incorporating the AG should be released later in 2023. The AG is not open to public comment. The released AG is noted to be an initial tranche, to be followed by further items of guidance in future. The rules and guidance released so far already exceed 450 pages.

The AG covers items in the categories of Scope (Article 1 of the GloBE rules), Income & Taxes (largely Articles 3 and 4), Application of GloBE Rules to Insurance Companies (various articles), Transition (Article 9) and Qualified Domestic Minimum Top-up Taxes (Article 10). Brief descriptions of each of the items are set out in the table below, with items of particularly substantive importance highlighted up front. The table is followed by KPMG observations on the road ahead.

## General observations

Several general observations might be made on the AG content.

***Helpful clarifications:*** Many of the AG items are directed at 'helping' taxpayers. These clarify the application and interpretation of the GloBE rules in such a way as to avoid distortive outcomes that could otherwise arise. Examples include the AG items 'softening' the application of Article 4.1.5, the various insurance-relevant rule clarifications, clarifications on the excluded entity definitions, the treatment of hedges of investments in foreign operations and clarifications of various transitional rules.

***GloBE and accounting:*** A number of the AG items might be viewed as 'patches' to deal with quirky interactions of the GloBE rules with accounting treatments. Conceivably, some of these outcomes were not foreseen when the GloBE rules and Commentary were initially drafted. Examples include the AG item on the application of the rules where historic cost is used for intragroup asset transfers, and where there is an asymmetric accounting treatment of preference shares at holder and issuer levels.

***Spill-over effects:*** Some of the AG items are directed at resolving specific issues but could conceivably have significant spill-over effects. An example is the list of 'events' treated as a transfer of assets for the purposes of the Article 9.1.3 transitional period rules, e.g., licenses, change of tax residence. Do these clarifications also have implications for the 'in-regime' rules? Another example is the assertion that the Arm's Length Principle-related Article 3.2.3 applies to adjust the price of intragroup asset transferred at carrying value, rather than fair value. The Commentary limited the application of Article 3.2.3 to instances where there had been a transfer pricing adjustment, which is not the case for the new AG item. What are now the new 'limits' on the application of Article 3.2.3?

***Dynamic vs static interpretation:*** The GloBE rules provide, at Article 8.3.1, that jurisdictions must apply the GloBE rules in accordance with the AG. Furthermore, it is clear from the AG document that in order for the IIR, UTPR or minimum tax of a jurisdiction to be 'qualified', it is necessary for it to follow the AG. This may raise issues where countries vary on whether the AG should be applied on a dynamic or static basis.

In addition, there could conceivably be instances in which the courts in a jurisdiction determine that the AG interpretation of a GloBE rules provision is not supported by the wording of the rule, as incorporated into domestic law. It was notable that in the draft UK GloBE legislation, released in July 2022, elements of the Commentary were integrated into the UK legislation, alongside the GloBE rules. It may well be that some countries will choose to take similar action, bringing elements of the Commentary and AG, perhaps also including safe harbor provisions, into domestic law. How this will sit alongside future AG tranches remains to be seen.

***Qualified domestic minimum top-up tax (QDMTT) design flexibility:*** As detailed further below, the AG provides jurisdictions with a degree of flexibility on how their QDMTTs are designed, with the option to modify or omit certain GloBE rule provisions in so far as these variations do not produce outcomes that are inconsistent with the GloBE rules. Whether a minimum tax is to be treated as a QDMTT will be determined under a multilateral review process (Peer Review) guided by the AG. Once a jurisdiction has designed a QDMTT that they consider should pass Peer Review, there may well be a 'queue' of other countries, seeking sign off, ahead of them. There is also the possibility that a jurisdiction might need to amend its minimum tax following review. As such, there appears to be a 'journey' ahead for countries in relation to their QDMTTs.

## Notable AG items

The most notable AG items, of general relevance to many MNEs, include the following.

***QDMTT (AG item 26):*** The AG reiterates that in order for a jurisdiction's minimum tax to qualify as a QDMTT it must provide for outcomes consistent with the GloBE rules, which generally requires that any variations not produce a lower liability than would be expected under the GloBE Rules. As well, the AG identifies certain elements of a QDMTT, as designed by a jurisdiction, that would need to be identical with the GloBE rules, and certain other elements that may vary. For example, variations from the GloBE rules may be permissible where particular GloBE provisions would be 'redundant' in light of the jurisdiction's tax system.

For instance, where a country's Corporate Income Tax (CIT) rules do not provide a tax deferral for reorganizations, the corresponding Chapter 6 GloBE rules can be omitted from that jurisdiction's QDMTT. In addition, certain variances from the GloBE rules which would systematically increase the tax liability under the QDMTT can be acceptable, e.g., lowering or dropping the Substance-based Income Exclusion (SBIE) provided for under the GloBE Rules. The Peer Review process will undertake a detailed ('case by case') evaluation of the QDMTT rules proposed by a jurisdiction, considering such alongside the domestic CIT rules, to see if omission/adaptation of any GloBE provisions is acceptable.

There are also some notable clarifications on the overall operation of the QDMTT:

- The AG reinforces that under the Model Rules and Commentary a QDMTT can be based on an accounting standard that differs from the one used in the consolidated financial statements of the Ultimate Parent Entity (UPE), assuming the accounting standard is of an "Acceptable" or "Authorised" (adjusted to prevent material distortions) nature.

- The AG clarifies that the QDMTT ETR numerator for the relevant jurisdiction would not include taxes paid by a shareholder of an entity located in such jurisdiction under a CFC regime that would otherwise be allocable to such subsidiary under the GloBE Rules. (Such rule would also apply in respect of any taxes paid by an owner of a permanent establishment located in such jurisdiction). Instead, the relevant CFC regime may give a credit for a QDMTT imposed on the CFC. As such, this would give the QDMTT imposing jurisdiction priority taxing rights over all others. Where CFC rule applying jurisdictions land in practice on this crediting point will be an area of intense interest going forward.

- The QDMTT developed by a jurisdiction needs to include the safe harbors developed by the OECD. Otherwise, an MNE would be forced to perform complex calculations for purposes of calculating liability under the QDMTT, which they are excused from if the IIR/UTPR applied. This might require adaptation of the temporary safe harbors released in December 2022.

- To be qualified, a QDMTT must be imposed on 100% of the TUT calculated for local CEs. It cannot be limited to the UPE's ownership percentage in those CEs. As such, QDMTT could lead to more TUT than if the IIR at the UPE level applied in such jurisdiction.

- Elections under the GloBE rules generally need to be provided for under a QDMTT. Some need not be provided where they are irrelevant in the context of the local CIT law, e.g., the stock compensation election where the deduction under the CIT is limited to the amount applied under the local accounting standard. An MNE group would need to make the same elections for QDMTT and IIR/UTPR purposes.

- Finally, a QDMTT must apply the same transition rules provided for under the GloBE Rules or otherwise the QDMTT will not reliably provide for outcomes consistent with the GloBE Rules. For example, if the same transition rule did not apply in respect of deferred taxes, the covered taxes taken into account in computing the ETR under a QDMTT and IIR would be inconsistent.

The IF members have not yet agreed on a QDMTT safe harbor and the AG notes that work will continue on its development. In its absence, QDMTT reduces the amount of top-up tax that arises under the GloBE rules (i.e., a credit mechanism) while a safe harbor would switch this to an exemption mechanism. Practically, in the absence of a QDMTT safe harbor, MNEs may be required to compute the ETR for a given jurisdiction twice: first for purposes of the QDMTT (potentially using the local accounting standard) and again for purposes of the IIR/UTPR (using the consolidated financial accounting standard of the UPE). The final design features of the QDMTT safe harbor will be highly anticipated, such as whether tax compliance over it would fall solely within the purview of the jurisdiction applying the QDMTT, or whether other jurisdictions could also have involvement. Another point might be the extent to which QDMTT filing information is shared with other jurisdictions, when the QDMTT safe harbor is in point.

***CFC Tax Allocation (AG item 15):*** The AG sets out a simplified approach for allocating CFC tax imposed under Blended CFC Tax Regimes that can be applied for a limited time. The latter are regimes that aggregate income and taxes of CFCs in different jurisdictions. Notably, the AG states explicitly that U.S. GILTI is such a Blended CFC Tax Regime. By contrast, where CFC tax is clearly imposed in respect of a given jurisdiction, then this may be directly 'traced' to that jurisdiction and the formulaic approach is not used.

The allocation formula described below considers both (i) the quantum of income in a jurisdiction within the scope of the relevant CFC Tax Regime, and (ii) the degree to which the GloBE ETR in the jurisdiction falls beneath the reference rate (i.e., the rate of foreign tax which would offset tax due under the CFC regime under the applicable credit method) for the relevant Blended CFC Tax Regime.

The **"Blended CFC Tax Allocated to an Entity**" is determined using the following formula.

$$\frac{\textit{Blended CFC Allocation Key}}{\textit{Sum of all Blended CFC Allocation Keys}} \times \textit{Allocable Blended CFC Tax}$$

The **"Blended CFC Allocation Entity"** is determined using the following formula.

$$\textit{Attributable Income of Entity} \times \textit{(Applicable Rate – GloBE Jurisdictional ETR)}$$

For the above formula:

- "Allocable Blended CFC Tax" is the amount of tax incurred by the CE-owner under that regime. The AG notes that, in the case of GILTI, the Allocable Blended CFC Tax can be determined from the U.S. federal income tax return and in the absence of a domestic loss is equal to the amount of GILTI (reduced by the GILTI deduction) multiplied by 21%, less the foreign tax credit allowed in the GILTI basket.

- "Attributable Income of Entity" is defined as the owner's proportionate share of the amount of the income of the CFC (or relevant part thereof where the CFC is composed of more than one CE) in the jurisdiction in which the CE is located as determined under the Blended CFC Tax Regime. As relevant to GILTI, the Attributable Income of the Entity can be determined from the US federal income tax return and is equal to the US shareholder's share of the tested income (without reduction for foreign income taxes) of the CE (which may be a CFC or tested unit thereof).

- "Applicable Rate" is defined as the "threshold for low taxation under the Blended CFC Tax Regime". This is explained to be the rate at which foreign taxes on CFC income generally fully offset the CFC charge through the tax credit mechanism applicable to the CFC Tax Regime. For GILTI, the Applicable Rate is noted to currently be 13.125%.

- "GloBE Jurisdictional ETR" means the ETR as computed under the GloBE Rules but without regard to any taxes allocated under a CFC Tax Regime. If this rate exceeds the Applicable Rate, the Blended CFC Allocation Key for the CE is zero.

The methodology includes a provision which ensures that, where income of non-CEs is subject to the Blended CFC Tax Regime, an appropriate amount of the Allocable Blended CFC Tax amount is not allocated within the group. While the approach seems reasonable, certain technical questions are left open and require further consideration.

The outlined allocation approach is applicable for fiscal years beginning on or before 31 December 2025, indicating that the approach outlined above may be amended at this time.

***Equity Gain/Loss Inclusion Election and Flow-Through Tax Benefits (AG item 13):*** In some jurisdictions that offer tax credits, the commercial arrangements used to access the credits may take the form of investment partnerships, or other tax transparent entity types. The investment returns may be accounted for by the MNE using the equity method of accounting. Under the GloBE rules, equity method accounted income and losses are removed from the ETR denominator and current tax expense on income accounted for under the equity method is removed from the ETR numerator.

However, the GloBE Rules do not explicitly provide for the removal of any current tax benefit arising from losses accounted for under the equity method. At the time of the March 2022 Commentary, open questions remained as to the proper treatment of tax credits related to the investment partnership in respect of the ETR calculation, as well as the treatment of current tax benefits arising from equity method losses.

The AG provides an election to remedy the distortive effects of a loss that is accounted for under the equity method of accounting and therefore removed from the denominator of the ETR calculation but nevertheless reduce Adjusted Covered Taxes because such loss is deductible for local tax purposes. More specifically, MNEs can make a 5-year election to include in GloBE income gains, profits and losses earned via equity method accounted investments (and other Ownership Interests) subject to certain exclusions for items not subject to tax.

Where this election is made all associated current and deferred tax expense and benefits are included in Adjusted Covered Taxes. Absent an MNE making this election, no adjustment is allowed where losses arising under the equity method investments distort the owner's ETR because such losses reduce taxable income in the owner's jurisdiction but not its GloBE income.

Where the election described above has been made, the AG provides for certain limited circumstances in which tax credits (other than Qualified Refundable Tax Credits (QRTCs)) that flow through transparent entities accounted for under the equity method will not cause a reduction in the ETR numerator. This applies only where a project would be uneconomic in the absence of the grant of the credit – that is, where the total amount invested by a holder is expected to exceed total distributions, QRTCs and tax benefits arising from allocated losses that are to be received by the holder.

In such instance, the equity method investment is not subject to the mechanics of the election described above, but instead the holder is allowed a positive adjustment for the amount of any credits or tax benefits arising from losses to the extent such credits or tax benefits otherwise reduced the holder's Adjusted Covered Taxes.

Importantly, these positive adjustments are only allowed to the extent such credits or tax benefits constitute a return of the holder's investment in the transparent entity (and not a return on investment), i.e., only to the extent such credits and other tax benefits (such as those arising from losses) do not exceed the holder's investment. Once the holder's investment has been returned, excess credits and benefits will reduce the holder's Adjusted Covered Taxes.

The AG notes that further guidance will be developed to clarify which credits would be covered by this provision and thus 'protected' from GloBE tax, clarification of how the election would work in connection with different GAAPs, and anti-avoidance rules for artificial structuring in connection with the election.

***Excess Negative Tax Carry-forward guidance (AG item 14):*** The GloBE rules contain a provision, in Article 4.1.5, which could lead to the imposition of GloBE tax in a year in which a GloBE loss arises. The intention of the provision is understood to forestall potential GloBE tax planning, whereby an MNE might 'time' the booking of permanent benefits (e.g., bonus depreciation) to occur in a GloBE loss year. In the absence of Article 4.1.5 the permanent benefit would not impact on the ETR and top up tax calculation.

However, many commentators considered it less than ideal that a global minimum tax on profits should have application in years of loss. The AG now adapts the application of Article 4.1.5. Rather than imposing top up tax in a GloBE loss year, an Excess Negative Tax Expense amount is calculated and carried forward. This would then reduce the ETR of a subsequent profitable year, potentially leading to the payment of further top up tax at that time.

The same mechanism is used to avoid the possibility of top up tax rates higher than 15%, modifying the application of Article 5.2.1. In a year where the GloBE ETR is determined to be negative in a jurisdiction, an Excess Negative Tax amount is calculated and carried forward. This would reduce the ETR in a later year.

***Deemed Consolidation Test (AG item 2):*** The GloBE rules do not just apply to groups which have prepared consolidated financial statements (CFS) with revenue exceeding EUR750m. The rules also apply to collections of entities (related through ownership or control), which would have clocked up revenue exceeding EUR750m if they had been treated as a group and required to prepare a set of CFS. A question of particular concern to the investment fund industry is whether investment funds, their investees and investment managers would be caught by this rule, given the nature of their control relationships, and treated as a composite group for GloBE purposes.

The AG now clarifies that this will not be the case; the consolidation exemptions for investment funds in accounting standards, such as IFRS 10, will be respected. However, at the same time the AG makes clear that the unconsolidated investment arrangements used by, say, wealthy families to invest in various businesses could well be caught by the deemed consolidation rule. These clarifications help bring clarity to the intended targets of the GloBE rules

Beyond these items, there are several technical clarifications on the operation of the transition rules.

## List of AG items with brief summaries

| Nr | Topic | Article | Description |
|---|---|---|---|
| **Scope** | | | |
| 1 | Currency Conversion | 1.1, 1.2, 3.1.3, 4.6.1, 4.6.4, 5.5.1, 6.1.1, 9.3.2, 10.1 | The GloBE rules include various monetary thresholds expressed in euro. In addition to the group revenue scope threshold (EUR750m), further examples are the de minimis jurisdiction rule (EUR10m revenue and EUR1m profit/loss), and the material competitive distortion between certain accounting standards and IFRS (EUR75m).<br>The AG provides for an annual rebasing of thresholds in non-euro currencies using the average foreign exchange rate in the month of December. |
| 2 | Deemed Consolidation Test | 1.2.2, 10.1 | As noted above, the AG clarifies that the deemed consolidated test will not require the preparation of CFS in a case where the Authorized Financial Accounting Standard explicitly permits non-consolidation. For example, IFRS10 permits qualifying investment entities to reflect investments at fair value in their financial statements, rather than consolidating them. Illustrative examples set out the case where the investment entity is covered by IFRS 10 and the deemed consolidation rule does not apply. Also set out is the case where a privately held investment holding company is not covered by IFRS10, and the deemed consolidation rule applies. |
| 3 | Consolidated Deferred Taxes Amounts | 4.1.1 | The AG clarifies that deferred tax expense with respect to a CE should be included in the Deferred Tax Adjustment Amount, even when the expenses are recorded in the MNE Group's consolidated financial accounts, rather than the financial accounts of individual CEs. |
| 4 | Sovereign Wealth Funds (SWFs) and the UPE definition | 1.4.1, 10.1 | The AG confirms that SWFs are not to be treated as the UPE of an MNE Group. This covers the case where the SWF cannot avail of the IFRS 10 investment entity consolidation exclusion, e.g., where there is no defined exit strategy for the SWF investments. |

| Nr | Topic | Article | Description |
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| 5 | Clarifying the definition of Excluded Entities definition | 1.5.2 | The GloBE rules provide for an extended definition of excluded entity. The definition also includes an entity, 95% held by an excluded entity, which holds assets (or invests funds) for the excluded entity; or which carries out functions ancillary to those of the excluded entity.<br><br>An example might be an investment holding SPV held by an (excluded) investment fund. The AG confirms that the 95% held entity can qualify as excluded where it both holds assets (invests funds) and performs the ancillary functions. Commentators had wondered whether the SPV was required to do one or the other, but not both. |
| 6 | Application of Revenue Threshold to Non-Profit Organizations (NPOs) | 1.5.2 | An excluded entity will not have its income subject to GloBE top up tax, but it can still be a member (including UPE) of a MNE group for GloBE purposes. The revenues of an excluded entity will be considered, as part of the group CFS revenue number, when determining whether the group exceeds the EUR750m threshold. This could leave the trading subsidiaries of (excluded) NPOs such as universities or international aid organisations exposed to GloBE tax.<br><br>To address this the AG calls for an assessment of whether the revenue of the trading subsidiaries falls under a certain threshold. If it does then the subsidiary will be regarded as conducting 'ancillary' activities, and can itself be considered as an excluded entity for the purposes of the GloBE rules under Article 1.5.2(a)(ii). The revenue threshold for the trading subs is the lower of EUR750m or 25% of the revenue of the MNE group. |
| **Income and taxes** | | | |
| 7 | Intra-group transactions accounted at cost | 6.3.1 | The design of the GloBE rules assumed that the accounting treatment of intra-group transfers of assets would reflect fair market value. This would generally be the case for accounts prepared under IFRS but under other accounting standards transfers can be booked at historic cost.<br><br>To address the distortions that might otherwise occur, the AG provides that an arm's length price must be used to determine the GloBE income/loss of the disposer, where the transaction occurs cross-border. This is stated to be pursuant to the arm's length principle rule in Article 3.2.3. The AG also notes that further guidance may be developed in relation to the acquirer to avoid double tax outcomes arising.<br><br>This AG item might be viewed as constituting some expansion in the application of Article 3.2.3. The March 2022 Commentary indicated that for Article 3.2.3 to be triggered there would need to be a transfer pricing adjustment. |

| Nr | Topic | Article | Description |
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| 8 | Excluded Equity Gain or Loss and hedges of investments in foreign operations | 3.2.1 | The GloBE rules provide that gains/losses on the disposal of (non-portfolio) equity interests will be excluded from GloBE income. The exclusion also extends to fair value gains/losses on such equity interests, and profit/loss from ownership interests which are subject to equity method accounting. To the extent that such equity interests are denominated in a currency different from the functional currency of the holding entity, the MNE may choose to use hedging instruments. The AG provides an election to treat gains/losses on the hedging instruments themselves as also being excluded gains/losses. |
| 9 | Excluded Dividends – Asymmetric treatment of preference shares | 3.2.1 | The AG places a limitation on the GloBE income exclusion for dividends from (non-portfolio) equity interests. This is intended to deal with 'accounting mismatches' in relation to intra-group financing. For example, take the case where Co A holds preference shares issued by related party Co B. Co A accounts for this as equity, while Co B accounts for this as debt financing (though for local tax purposes Co B may still treat it as equity).<br><br>The Co B accounting treatment of dividend payments as interest, which would be followed by the GloBE income computation, would reduce the ETR denominator and raise the ETR – this is seen to be prone to GloBE tax planning. In consequence, the AG clarifies that Co A must be treated as receiving interest for GloBE purposes (i.e., conform recipient treatment to the accounting treatment of issuer Co B). This thereby limits the use of the GloBE dividends exclusion.<br><br>To the extent that other forms of financing instrument are bifurcated by Co B into debt and equity elements there would be a proportional decrease in the amount treated as excluded dividends by Co A. |
| 10 | Covered Taxes on deemed distributions | 4.3.2(e) | The GloBE rules allocate taxes paid in respect of distributions to the CE that made the distribution. The AG clarifies that this also applies to taxes imposed on deemed distributions. |
| 11 | Treatment of debt releases | 3.2.1 | The AG excludes debt release-related income, booked to the accounts, from GloBE income. Conditions apply, including that the income must be exempt from domestic tax and the debt release must occur in the context of a corporate rescue. |

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| 12 | Accrued Pension Expenses | 3.2.1 | The GloBE rules, at Article 3.2.1(i), allow pension liabilities as expenses in the computation of GloBE income. These are allowed to the extent of the contributions to a pension fund during the fiscal year. This treatment is intended to better align GloBE income with local tax base calculations and neutralize differences between accounting standards that book pension fund income via OCI or via the income statement. The AG makes several clarifications.<br><br>Firstly, if a company actually pays pensions to its retired employees, rather than paying them to a fund, then Article 3.2.1(i) has no application. These direct pension payments are taken into account as accrued in the accounts. Secondly, GloBE income adjustments may be made in the case where pension fund earnings exceed the pension expense for the current year, and the surplus is brought to the income statement. This depends on whether the surplus is being retained by the pension fund or returned to the MNE. |
| 13 | Equity Gain/Loss Inclusion Election and Flow-Through Tax Benefits | 4.1.3(a) | As noted above, the AG provides clarifications on the treatment of tax credits accessed via tax transparent entities, accounted for using the equity method. It also provides a new election in relation to equity gains/losses. |
| 14 | Excess Negative Tax Carry-forward guidance | 4.1.5 and 5.2.1 | As noted above, the AG 'softens' the effect of Article 4.1.5. It provides for the elective calculation of an Excess Negative Tax amount, where the original Article 4.1.5 approach would have imposed GloBE top up tax. This is then carried forward and can reduce the ETR of a subsequent profitable year, potentially leading to the payment of further top up tax at that time.<br><br>The same mechanism is used to avoid the possibility of top up tax rates higher than 15%, modifying the application of Article 5.2.1. In a year where the GloBE ETR is determined to be negative in a jurisdiction, an Excess Negative Tax amount is calculated and carried forward. This would reduce the ETR in a later year. |
| 15 | CFC Tax Allocation | 4.3 | As noted above, the AG sets out how CFC tax is to be attributed over jurisdictions. The attribution mechanism uses a 'tracing approach' in some instances and an allocation approach in other instances. The latter is used for allocating Blended CFC Tax Regimes that aggregate income and taxes of CFCs in different jurisdictions. |

| Nr | Topic | Article | Description |
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| 16 | Loss-making Parent Entities of CFCs | 4.4.1(e) | The GloBE rules, in Article Art 4.4.1(e), provide that DTAs recognised in respect of tax credits will be disregarded for GloBE purposes. The AG provides an exception to this for foreign tax credit DTAs in certain circumstances. The exception is applicable where a Parent Co is in a loss position in a year in which its CFC rules apply to the profits of Sub Co.<br><br>In this case the CFC tax on Sub Co profits may be offset by Parent Co's tax losses, and the FTC for Sub Co tax is carried forward. In this case the AG allows for Art 4.4.1(e) to be set aside, and the DTA for the FTC is recognised for GloBE purposes. |
| **Application of GloBE Rules to Insurance Companies** | | | |
| 17 | Application of Article 7.6 to Insurance Investment Entities | 7.6 | The GloBE rules, in Article 7.4, require that ETR and top up tax calculations are done on a separate entity basis for investment entities and insurance investment entities. This being said, Articles 7.5 and 7.6 can attribute the income of these investment entities to the entities that own them for GloBE purposes.<br><br>An Article 7.5 election can be made when the owner is subject to a mark-to-market tax regime in respect of fair value changes in the investment entity. An Article 7.6 election can be made to the extent that the investment entity makes distributions to the owner within a 4 year period.<br><br>The initially drafted GloBE rules provided that Article 7.5 could cover insurance investment entities as well as investment entities, but Article 7.6 did not. The AG now provides for this. |
| 18 | Intermediate Parent Entity (IPE) - Exclusion of insurance investment entities | 3.1.3 | The AG clarifies that the definition of IPE, which excludes investment entities, also excludes insurance investment entities. |
| 19 | Restricted Tier One Capital | 3.2.10 | The GloBE rules, in Article 3.2.10, treat the Additional Tier One Capital for banks in the same way as debt instruments. While these instruments may be treated as equity for accounting purposes, the GloBE rules treat payments on them as deductible in the same manner as interest. The AG now provides for the same treatment for Restricted Tier One Capital issued by insurance companies. |

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| 20 | Liabilities related to Excluded Dividends and Excluded Equity Gain or Loss from securities held on behalf of policyholders | 3.2.1 | The GloBE rules provide GloBE income exclusions for gains/losses on the disposal of (non-portfolio) equity interests and for dividend income from equity interests (other than short-term portfolio holdings). For simplicity the GloBE rules do not disallow expenses relating to these excluded income amounts. However, the AG now introduces an exception to this where insurance companies hold equity investments on behalf of policyholders, e.g., unit-linked insurance.<br><br>Under such arrangements the insurance company must pay all investment earnings to policyholders, less an investment management fee. To avoid the situation where the company will have excluded income, but still get a deduction for the liability recognized to policyholders (giving rise to a GloBE loss), this movement in insurance reserves will now be treated as non-deductible. |
| 21 | Simplification for Short-term Portfolio Shareholdings | 3.2.1 | The GloBE rules provide a GloBE income exclusion for dividend income from equity interests, other than short-term portfolio holdings. This then places a burden on in-scope MNEs to prove equity holding periods. As a simplification, the AG now provides for a 5-year election to include all dividends in GloBE income. It is expected that this election will largely be used by insurance companies but it is open to all groups. |
| 22 | Application of Article 7.5 to Mutual Insurance Companies | 7.5 | Mutual insurance companies are owned exclusively by their policyholders. As all investment returns are due as liabilities to policyholders, the mutual insurance company has no profit from an accounting perspective. However, where the mutual insurance company controls an investment entity (a separate CE for GloBE purposes) it may be that the investment income is at investment entity level but the offsetting liability to policyholders is at the mutual insurance company level.<br><br>An Article 7.5 election, which would attribute the investment entity income to the mutual insurance company (and allow for income-liability offset), requires that the mutual insurance company be taxed under a mark-to-market tax regime (which is typically not the case). The AG relaxes this requirement in the case of mutual insurance companies, allowing the Article 7.5 election to be used. |
| **Transition** | | | |
| 23 | Deferred tax assets with respect to tax credits under transition rules | 9.1.1 | As noted above the GloBE rules, in Article Art 4.4.1(e), provide that DTAs recognised in respect of tax credits will be disregarded for GloBE purposes both in the year the credit is generated and used. |

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| 23 | Deferred tax assets with respect to tax credits under transition rules | 9.1.1 | However, the GloBE Commentary was initially not clear on how this would interact with the transition year rules. Article 9.1.1 provides that an MNE is permitted to take into account "all" of the DTAs and DTLs reflected or disclosed in the accounts for the transition year. The AG confirms that this means that 4.4.1(e) does not apply to transition DTAs. At the same time the AG provides a simplified approach to recasting the DTAs for tax credits where they are booked at rates higher than the 15% minimum rate.<br><br>The AG also sets out special provisions dealing with refundable tax credits that accrued prior to the beginning of the transition year. For context, the GloBE rules differentiate between qualified refundable tax credits (QRTCs) and non-qualified refundable tax credits (NQRTCs).<br>The AG deals with the specific case where NQRTCs, which accrued prior to the beginning of the transition year (and which are carried forward for use in later years), were booked as an increment to income for accounting purposes. Due to such accounting treatment, there will be no transition DTA recognised. By contrast, had the NQRTC been booked in the accounts as relating to a future reduction to income tax expense (in line with its GloBE treatment) then a DTA would have been recognized. In a later year (in-regime), when the NQRTC is settled, the income tax expense will be reduced. Under the GloBE rules this will lower Covered Taxes and the ETR numerator for that year.<br><br>To preserve the overall neutrality of the GloBE rules, the AG provides that Covered Taxes will not be reduced in the year of settlement of the NQRTC, i.e., the Covered Taxes number will be 'artificially' held up in that year. |
| 24 | Asset carrying value & deferred taxes under transition rules | 9.1.3 | The GloBE rules, in Article 9.1.3, provide for special treatment of intra-group asset transfers after 30 November 2021 and before the start of the MNE group's transition year. The intent of the provision is to limit the ability of MNEs to enter into inter-group transactions during the pre-GloBE period that increase asset carrying values and thereby reduce GloBE income, e.g., through elevated depreciation and amortization expense, without the corresponding gain be included within GloBE Income. Specifically, Article 9.1.3 provides that, for the acquiring CE, its basis in the transferred assets will be based on the disposing CE's carrying value of the assets upon disposition. |

| Nr | Topic | Article | Description |
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| 24 | Asset carrying value & deferred taxes under transition rules | 9.1.3 | The acquiring CE's DTAs and DTLs for GloBE purpose will be determined on this basis. The AG provides additional clarity on how Article 9.1.3 is meant to be applied.<br><br>The AG deals with both the case where an intra-group transfer is booked at cost at the level of the acquiring CE, and with the case where it is booked at fair value.<br><br>Starting with the case where the transfer is booked at cost, it is noted that a DTA could be recognised at the level of the acquiring CE. This could be because the acquiring CE's local jurisdiction recognises a higher base cost for tax purposes, for example where the transfer consideration was higher than the historic cost at which the transfer was booked. The AG provides that recognition of this DTA for GloBE purposes is dependent on tax being paid, by the disposing CE, on the gain on transfer. To the extent that the gain is taxed at 15% (or above) the acquiring CE can recognize the DTA at 15%; lower levels of tax on the gain will lead to proportionate reduction in the quantum of DTA that can be recognized. Where no tax is imposed on the transfer gain then no DTA can be recognised for GloBE purposes. Where tax losses at the level of the disposing CE mitigate the tax actually paid on the gain, a DTA may still be recognizable at the level of the acquiring CE.<br><br>In the alternative case where intra-group transfer is booked at fair value at the level of the acquiring CE, the same considerations are in play. Regard is had to the tax applied to the gain at the level of the disposing CE. Treatment at the level of the acquiring CE is 'equalized' with the treatment that would have applied to a transfer booked at cost. The GloBE carrying value at acquiring CE is reduced to cost and (assuming tax is paid on the disposal gain) a DTA is recognised at the level of the acquiring CE. |
| 25 | Applicability of Article 9.1.3 to transactions similar to asset transfers | 9.1.3 | The AG details a series of transaction types, similar to asset transfers, which are to be covered by the Article 9.1.3 provisions. In addition to asset sales this covers certain capital leases, licenses and prepayments of royalties/rents, transfers of assets through sale of a controlling interest, and total return swaps transferring an underlying asset to the accounts of an acquiree. It also covers entity tax residence migration leading to tax or accounting basis step up, and asset value adjustments arising from fair value accounting. The latter two transactions are regarded as deemed transfers happening 'within the same entity'. |

| Nr | Topic | Article | Description |
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| 26 | QDMTT | 10.1 | As noted above, the AG identifies which elements of a QDMTT, as designed by a jurisdiction, would need to be identical between QDMTT and the GloBE rules, and which elements are allowed to vary. |

## KPMG Observations – Looking ahead

As noted above, this is a first tranche of AG. More will follow in due course, though it is not yet clear what items are on the 'priority list' and when and in what order they will be dealt with. The AG tranche just released raises, in many instances, as many new issues for clarification as it addresses. The mechanism through which the business community can raise these issues and have input on their prioritization is of high importance and is a key focus of recent KPMG public consultation submissions.

Highlighted below are the areas for which the AG document highlights that further guidance is at least under consideration:

- Treatment of acquirer for intra-group asset transfers
- Treatment of creditor for debt releases
- Fuller guidance on equity investment inclusion election
- Further guidance on the operation of QDMTT, including:
    - Design features including threshold for material competitive distortions, PE income allocation, jurisdictional blending, treatment of investment entities and transparent entities
    - Allocation of QDMTT liability amongst entities in a jurisdiction
    - Identification of 'benefits' to taxpayer which would invalidate 'qualified' status
    - Information collection/exchange arrangements
    - QDMTT safe harbor

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