

- Australian Implementation of the GloBE Model Rules

**17.** Do you have any comments on how Australia should implement the GloBE Model Rules into domestic law?

Answer: The treatment of refundable Tax Credits is an important issue as under Pillar Two, minimum tax is imposed on MNE's income earned through subsidiaries or PEs to the extent that the foreign country's ETR is less than 15 percent. When tax credits reduce the ETR below the 15 percent benchmark, the country of the parent MNE may be entitled to impose IIR top-up tax, therefore, undermining the purpose of the tax credit as the offsetting minimum tax is collected by another country through IIR or UTPR. If the tax credit is limited to income qualified as "substance-based income exclusion," this will reduce the "excess profit"<sup>1</sup> subject to the minimum tax. The exclusion allows Australia, to provide tax credits to reduce the fixed amount of income from business activities from tangible assets and employees without resulting to minimum tax. Relief measures are the "qualified refundable tax credits" (QRTC) and "non-qualified refundable tax credits" or "other refundable tax credits" (ORTCs).<sup>2</sup> Under Article 3.2.4 of the Model Rules, QRTSs are included in the net GloBE income and ORTCs are not. Any refund of covered taxes reduces the amount of covered taxes and if the reduction is made in respect of QRTC, it is added back under Article 4.1.2 (d). QRTCs are treated as government grants, do not reduce covered taxes and do not reduce the ETR. Where a refund of ORTC does not reduce the amount of covered taxes in the financial accounts, Article 4.1.3 (b) requires the refund to reduce covered taxes and therefore, reduce the country's ETR. The legislation must clearly define what is a QRTC and domestic legislation to identify the conditions to qualify for QRTC and provide a credit in order to avoid disputes. A dispute resolution mechanism will need to be included as more likely disputes will arise.

- Interaction with Integrity Provisions

**32.** Are there any issues which you think may arise in allocating taxes imposed under Australia's CFC Tax Regime?

Answer: The minimum tax does not replace a country's CFC rules so Australia can apply CFC Rules and implement the Pillar Two minimum Tax. There are significant differences between CFC rules and the Pillar Two minimum Tax regarding the tax base, the tax rate and the country that collects the tax. The exclusion of the IIR top-up tax from the definition of a CFC tax makes sense.<sup>3</sup> The provisions of the Model Rules dealing with CFC rules will operate independently of Australia's CFC Rules. So, the first step is to determine if Australia's CFC rules are within the definition of "CFC Tax Regime" in article 10.1.1 of the Model Rules. Once it is determined that Australia's CFC rules are under a "CFC tax

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<sup>1</sup> OECD, 2021, *Tax Challenges Arising from the Digitalisation of the Economy-Global Anti- Base Erosion Model Rules (Pillar Two): Inclusive Framework on BEPS*, OECD, Paris, Article 5.2.2, (hereinafter, Model Rules), viewed at: <https://www.oecd.org/tax/beps/tax-challenges-arising-from-the-digitalisation-of-the-economy-global-anti-base-erosion-model-rules-pillar-two.htm>

<sup>2</sup> Arnold, 2022, *Pillar Two: The Treatment of Refundable Tax Credits*, The Arnold Report, Issue 239, Canadian Tax Foundation.

<sup>3</sup> For a detailed analysis on the interaction of CFC Rules and the Pillar Two Model Rules refer to Arnold, B., 2022, OECD/ International- *An Investigation into the Interaction of CFC Rules and the OECD Pillar two Global Minimum Tax*, *Bulleting for International Taxation*, Vol 76, No.6, Chapter 5, (hereinafter Arnold, 2022, CFC and Pillar Two).

Regime,” the Pillar Two Model Rules will apply to CFC taxes under a CFC tax regime without regard to the domestic CFC rules.<sup>4</sup>

Under Article 4.3.2(a) of the Model Rules, covered taxes with regard to the GloBE income or loss of a PE are allocated to a PE. There is no limit on the amount allocated to a PE with regard to the passive income of the PE as there is with regard to the passive income of a CFC under Article 4.3.3 of the Model Rules. Subject to the Rule in Article 4.3.4 of the Model Rules, taxes ‘arising in the location of the PE as taxes of the Main Entity’, such taxes are not pushed down to the country in which the PE is located as this special rule is to offset the impact of the PE losses deductible against the income of the main entity in a prior year.<sup>5</sup>

- Corporate Restructuring under GloBE

**33.** Do you have any comments on how the GloBE Model Rules in relation to corporate restructurings and holding structures may interact with Australia’s tax laws on mergers and acquisitions, including tax consolidation? Do you also have any comments on how the GloBE Model Rules could be implemented so that interactions with our domestic rules, including tax consolidation, do not lead to outcomes inconsistent with the GloBE Model Rules?

Answer: Australian Legislation regarding Corporate Restructuring under GloBE may consider the key points in Chapter 8, Paragraphs 69 – 72 of the UK Draft Multinational Legislation dealing with restructuring of groups, specifically, paragraph 69 (2)-69 (11) (c) provide for detailed adjustments when a member joining or leaving a multinational group. When the transfer of controlling interest treated as transfer of acquisition of assets and liabilities, paragraph 69 does not apply. When a member of a multinational group transfers assets or liabilities to another entity in the course of a qualifying reorganisation, any gains or loss on the transfer is to be excluded from the adjusted profits of the member.<sup>6</sup> If a transfer of assets and liabilities take place as a result of a merger, de-merger, liquidation or a change in form of an entity, or a similar event, the transfer is made in the course of a qualifying reorganisation.<sup>7</sup>

- Domestic Minimum Tax

**35.** Do you have any comments on whether or not Australia should adopt a Domestic Minimum Tax in conjunction with the implementation of the GloBE Model Rules?

Answer: HM Treasury published the ‘OECD Pillar 2 Consultation on implementation: Summary of Responses’<sup>8</sup> and many respondents thought a DMT could help reduce compliance costs and removing the need to perform UTPR calculations. Also, the DMT could provide additional certainty for MNEs by protecting them from the application of other jurisdictions’ GloBE Rules, in particular the UTPR. The savings will materialise if there was a Safe Harbour from the IIR and UTPR when a jurisdiction introduces a DMT. In the absence of this, a DMT could increase complexity and incremental taxation, where there are

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<sup>4</sup> Id., Chapters 5-6.

<sup>5</sup> Model Rules, [4.3.2]- [4.3.3].

<sup>6</sup> UK Draft Multinational Legislation [71]

<sup>7</sup> Id., [72]

<sup>8</sup> HM Treasury, 2022, *OECD Pillar 2 Consultation on implementation: Summary of Responses*, [12.1]-[12.6] (hereinafter UK GloBE Responses) viewed at: <https://www.gov.uk/government/consultations/oecd-pillar-2-consultation-on-implementation#>

differences between the DMT and another jurisdiction's GloBE Rules. These are valid reasons for Australia to adopt a DMT in conjunction with the implementation of the GloBE Model Rules.

**36.** Do you agree that a Domestic Minimum Tax in Australia should only apply to multinationals in the scope of Pillar Two (for example, not applying to businesses that only operate in Australia)?

Answer: To ensure a level playing field, a DMT should apply to both domestic and foreign headed groups. This will align with other countries, example EU draft directive. There is an area of risk for US companies for GILTI purposes and may impose additional top-up taxes.

**37.** If Australia were to adopt a Domestic Minimum Tax, do you have any views on its design as a Qualified Domestic Minimum Tax (that is, on the Domestic Minimum Tax being consistent with the outcomes under the GloBE Model Rules)?

Answer: The scope of the DMT should be aligned with the scope of the GloBE Rules. It may be necessary to extend the rules to wholly domestic groups to ensure the rules are compatible with Double Tax Treaties and as they would be in scope of the DMT but not the GloBE, a simplified computation will be required for these entities.<sup>9</sup> The timing should be aligned with the implementation date of the UTPR internationally without being exposed to incremental taxation. The calculation of tax should closely adhere to the Model Rules, it is important the tax to be treated as a qualified DMT and a close alignment with the Model Rules is best to ensure this.

There can be an election to compute DMT using the UPE accounting standards used to compute the ETR under the GloBE Rule or MNE's could choose the accounting standards of the ultimate parent entity or engage in GAAP shopping.<sup>10</sup> So calculating the ETR under AASB standards is of a limited benefit even thus it is listed as acceptable under Pillar Two,<sup>11</sup> it may lead to material competitive distortions<sup>12</sup> as the figures from AASB are subject to adjustments in accordance with IFRS requirements. Material Competitive distortion exists when the application of the domestic accounting principles result in an aggregate variation of more than € 75m.<sup>13</sup> In the European Union (EU) a proposal for a Council Directive provides

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<sup>9</sup> See UK GloBE Responses [12.12]- [12.14].

<sup>10</sup> Devereux, M., Bares, F., Clifford, S., Freedman, J., Guceri, I., McCarthy, M., Simmler, M., Vella, J., 2020, *The OECD Global Anti- Base Erosion ("GloBE") Proposal*, Oxford University for Business Taxation, pp.15-18, viewed at: <https://oxfordtax.sbs.ox.ac.uk/globe>

<sup>11</sup> Model Rules 10.1.1.

<sup>12</sup> OECD, 2022, *Tax Challenges Arising from the Digitalisation of the Economy- Commentary to the Global Anti- Base Erosion Model Rules (Pillar Two)*, OECD /G20 Base Erosion and Profit Shifting Project, Inclusive Framework on BEPS, [10.59], (hereinafter OECD, 2022, Commentary to Pillar Two Rules), viewed at: <https://www.oecd.org/tax/beps/tax-challenges-arising-from-the-digitalisation-of-the-economy-global-anti-base-erosion-model-rules-pillar-two.htm>; *Tax Challenges Arising from the Digitalisation of the Economy- Global Anti-Base Erosion Model Rules (Pillar Two) Examples*, 2022, OECD /G20 Base Erosion and Profit Shifting Project, Inclusive Framework on BEPS, OECD, Paris, viewed at: <https://www.oecd.org/tax/beps/tax-challenges-arising-from-the-digitalisation-of-the-economy-global-anti-base-erosion-model-rules-pillar-two.htm#examples>

<sup>13</sup> Id., [10.60].

for a variation of more than 10% of revenue as an alternative criterion.<sup>14</sup> The use of an alternative accounting standard is limited by three conditions:

- i. A constituent Entity may not use an accounting standard under Article 3.1.3 other than the one used in its financial accounts;<sup>15</sup>
- ii. Information in the financial accounts are reliable;<sup>16</sup>
- iii. Permanent differences in excess of € 1m to items of income or expenses are conformed to the treatment under the accounting standards used in the consolidated statements.<sup>17</sup>

There should be priority ordering for the charge, with wholly owned entities in a group, allocated the top up before entities with minority investors. The administration should be aligned with GloBE reporting and the detailed calculations of the DMT should be reported on the GloBE Information Return and avoid the introduction of a separate complex return specifically for the DMT. Also, the QDMTT alters the rule order of Pillar 2, it moves the “source” country to the head of the chain to collect the top- up tax generated by Pillar 2. If a MNE is taxed below the minimum tax rate in a particular country, the missing revenue will be collected through the QDMTT, the IIR or the UTPR, in that order.<sup>18</sup>

**38.** If a Domestic Minimum Tax were to be implemented, do you have any views as to whether there should be a separate return (that is, in addition to the GloBE Information Return and any potential local GloBE Tax Return), and do you have any additional feedback on this return? Would there be any particular issues if a Domestic Minimum Tax Return were to be due earlier than the GloBE Information Return?

Answer: The DMT should be reported on the GloBE information Return and not a separate return.

**39.** If a Domestic Minimum Tax is implemented, how should the relevant liability be allocated amongst Australian Constituent Entities? Should the liability be joint and several amongst Australian Constituent Entities?

Answer: The liability should be joint and several amongst Australian Constituent entities.

**40.** Do you have any views on whether tax paid in Australia under a Domestic Minimum Tax should give rise to franking credits?

Answer: No Franking credits should give rise to tax paid in Australia under DMT as the design will be a Qualified Domestic Minimum Tax (QDMT) and consistent with the GloBE Model Rules.<sup>19</sup>

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<sup>14</sup> European Union, Document 52021PC0823, *Proposal for a Council Directive on ensuring a global minimum level of taxation for multinational groups in the Union*, COM/2021/823, Article 14.3, (hereinafter Council Directive 2022), viewed at: <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52021PC0823>

<sup>15</sup> OECD, 2021, Pillar Two Rules, Article 3.1.3, [14].

<sup>16</sup> Id., [15].

<sup>17</sup> Id., [16].

<sup>18</sup> Devereux, M., Vella, J., Wardell-Burrus, H., 2022, *Pillar 2: Rule Order, Incentives and Tax Competition*, Oxford University Centre for Business Taxation Policy Brief 2022, [2.1], viewed at:

[https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=4009002](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4009002)

<sup>19</sup> Commentary to Pillar Two Rules, Article 10.1, [124]