Tax Neutrality Regimes & GloBE

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The Problem

The GloBE rules establishes a top-up tax when the minimum level of taxation is not satisfied.

However, what if the UPE is not a taxable entity?

- Shall the minimum taxation threshold of 15% be determined at the level of the “holder” (owner)?
- Is the jurisdiction of this type of UPE still GloBE compliant?
- What happens if the holder is taxed at least at a 15%?

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- The ETR of the UPE will be zero or close to zero.
- Other rules contemplated in the Model Rules will not apply in case the holders are not group entities.
The OECD Model Rules (solution)

Article 7.1 resolves this issue for certain situations

The principle underlying the rules in Article 7.1:

“To the extent that the tax neutrality regime imposes tax on the UPE’s owners (e.g., partners, beneficiaries or shareholders) at or above the Minimum Rate on the UPE’s income contemporaneously or within a short time, the UPE’s exposure to Top-up Tax will likewise be reduced”.

- In simple terms, the amount of GloBE income that is attributed to the holders and subject to tax in their hands (according to their % of participation) will be reduced from the UPE’s GloBE income = this reduces the risk of a top-up tax.
The OECD Model Rules (solution)

Article 7.1.1— it allows the UPE to reduce its GloBE income for a fiscal year in three situations:

- **Paragraph (a) = general rule**
- **Paragraph (b) = safe harbour (small ownership-natural persons)**
- **Paragraph (c) = holder is a gov entity; int org; non-profit or pension fund**

The UPE will reduce its GloBE income by the amount of GloBE income attributable to each Ownership Interest that meets a criterion in paragraphs (a) to (c).
The OECD Model Rules (solution)

**GENERAL RULE (Article 7.1.1)**

There are two tests with respect to each ownership interest (both tests must be met):

- Taxable period test
- Minimum tax test

**Taxable period test**

The holder must be subject to tax on his share of UPE’s GloBE income for a period that ends within 12 months of the end of the MNE Group fiscal year to meet the test — There is no requirement to pay the tax in the same period.

“Subject to tax” = GloBE income includable in the holder’s taxable income under the laws of the country where the holder is a tax resident or includable in the taxable income of a PE holder.

The model rules also states that timing differences will not make the holder to fail the test.
Minimum Tax Test

It has two conditions and only one of them must be satisfied:

1. The holder subject to tax on the full amount of GloBE income at a nominal rate that is equal or above the minimum rate (15%) — No ETR calculation is needed.

2. The ‘reasonably expected’ covered taxes paid condition.
The OECD Model Rules (solution)

Minimum Tax Test (First Condition)

Holder must be "subject to tax" at a nominal rate of 15% on his 30% GloBE income.

Minimum Tax Test (Second Condition)

Net amount of covered taxes paid by the UPE & holder are equal or above the minimum.

Country A

Country B

Paid 5% at a state level

Paid 10% at a federal level
Final remarks and open questions

- The model rules on “tax neutrality regimes” recognise the importance of tax transparency — Otherwise, the main effect of transparency (i.e., taxing in the hand of a single taxpayer) would be unfairly affected.

- The rules are highly technical and not easy to apply (did we expect otherwise, though?)

- From a policy perspective: simplification and ease of administration are certainly forgotten/ however the rules are coherent and play an important role to maintain the neutrality of tax transparency regimes.