The end of tax incentives?

How will a global minimum tax affect tax incentives regimes in developing countries

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ICRICT/FES/G-24 ROUNDTABLE – GLOBAL MINIMUM TAX

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IISD
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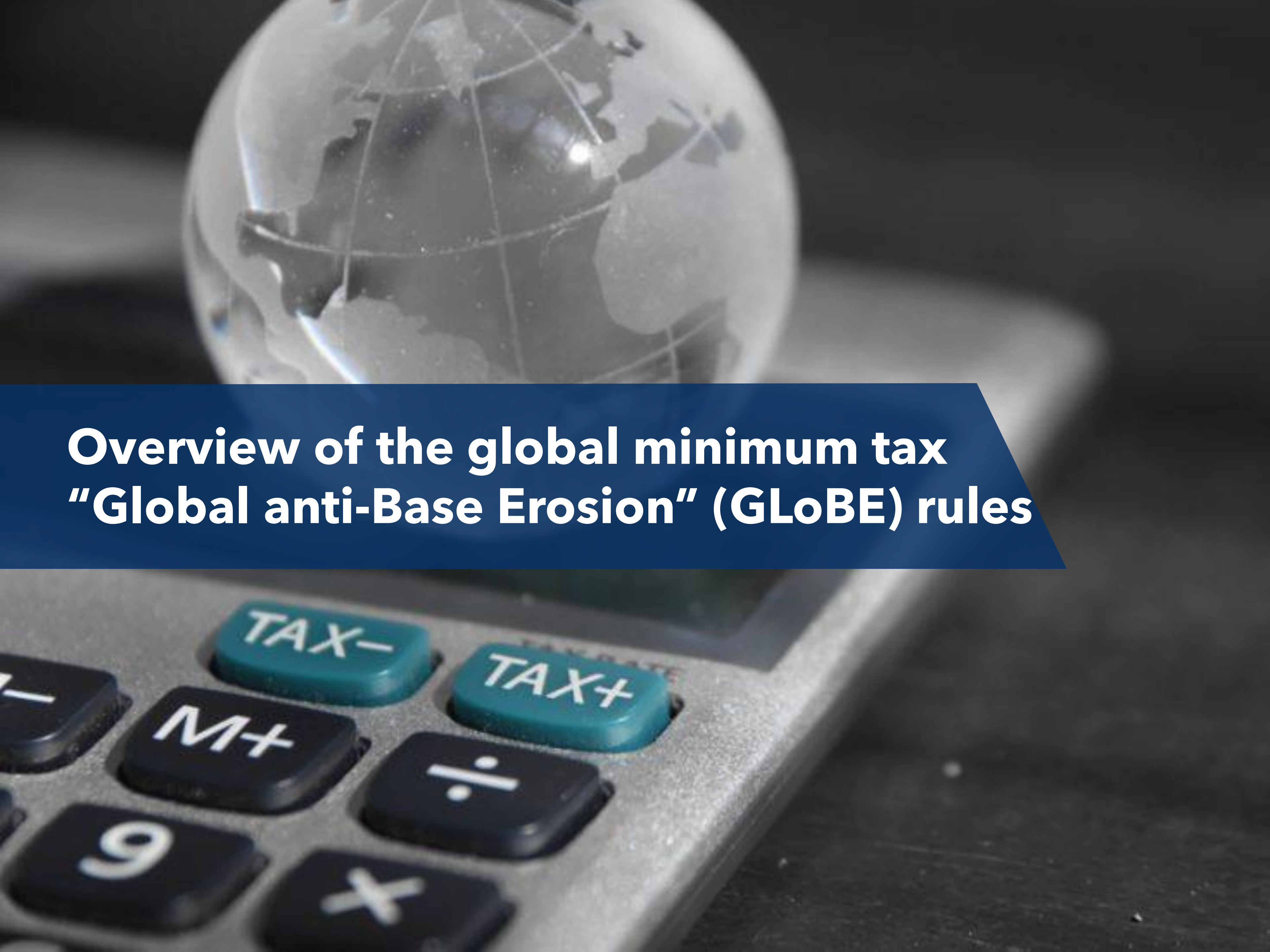
Agenda

Overview of the global minimum tax “Global anti-Base Erosion” (GLoBE) rules

How will tax incentives be affected?

Possible policy responses

Overview of the global minimum tax "Global anti-Base Erosion" (GLoBE) rules



Overview of the GloBE Rules: Scope by Company

Which firms are in scope?

Multinational enterprise group ("MNE Group")

- MNE Group has at least one entity or Permanent Establishment in a jurisdiction other than the jurisdiction of the "Ultimate Parent Entity" ("UPE")
- MNE Group ≥ EUR 750 million in 2 of prior 4 years
- Revenue based on consolidated financial accounts

Which firms are excluded?

Entities that are typically recognized as tax exempt under international tax principles

Certain holding vehicles used by other excluded entities

Overview of the GloBE Rules: Minimum Tax by MNE and by Country

Calculate Effective Tax Rate (ETR) in each jurisdiction

If ETR ≥ 15%

No further tax with respect to that jurisdiction under the GloBE Rules

If ETR < 15%

Calculate "Top-up Tax" for that jurisdiction
= (15% - ETR) * income

Apply priority rules to determine which entity (in which jurisdiction) pays tax

Overview of the GloBE Rules: Effective Tax Rate by MNE and by Country

Adjusted Covered Taxes
of all entities in the jurisdiction*

Net GloBE Income
of the jurisdiction**

=

Effective Tax Rate (ETR)
% for the jurisdiction

*Adjusted Covered Taxes include shareholder CFC taxes that are attributed to income from the jurisdiction.
**Before the substance-based income exclusion.

Overview of the GloBE Rules: Priority of Country Tax Rights

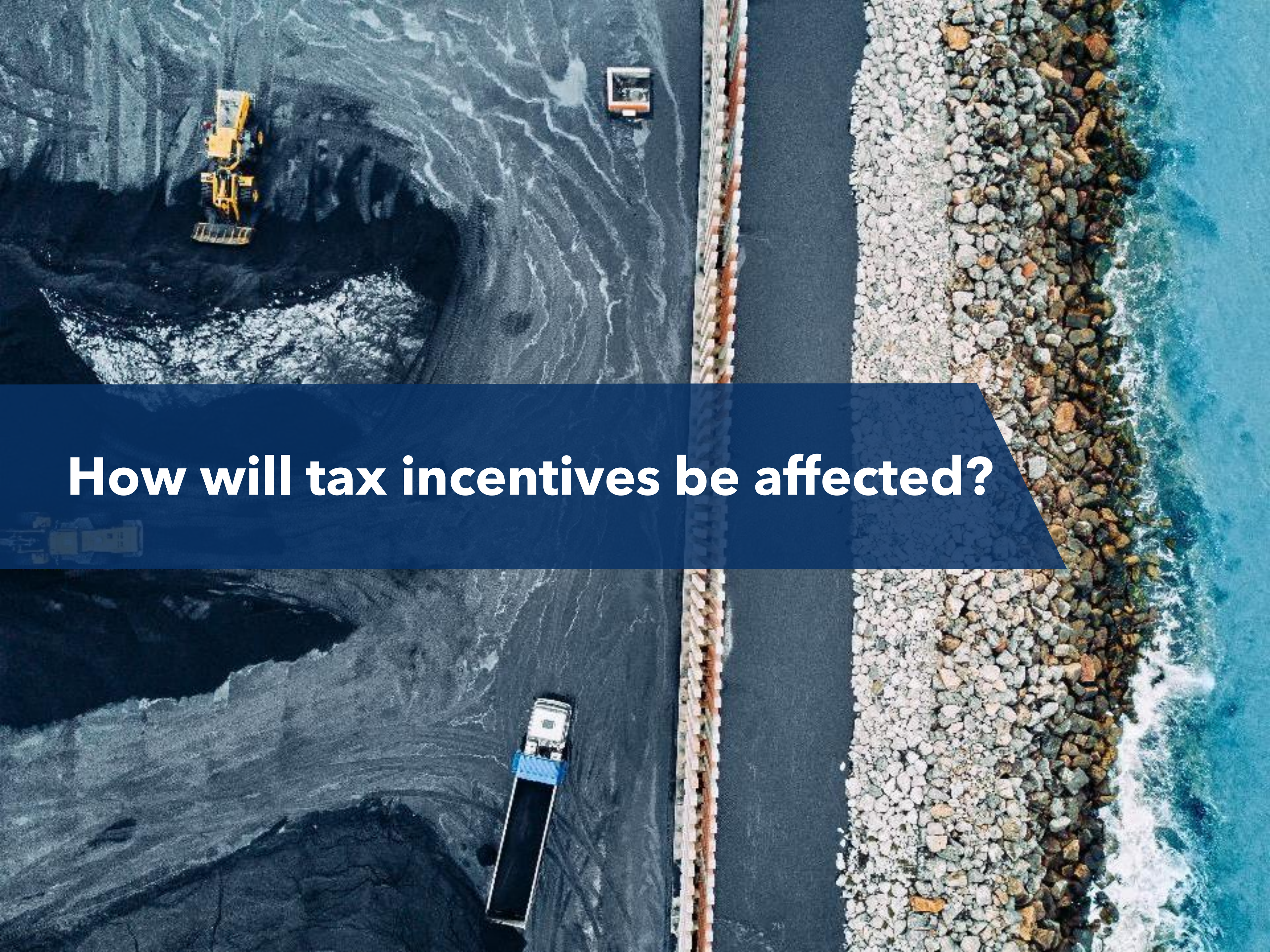
- **First Priority: Local taxing authority may impose a "Qualified Domestic Minimum Top-up Tax" ("QDMTT") – a domestic version of the GloBE rules.**

- **Second Priority: "Income Inclusion Rule" ("IIR") imposes any remaining Top-up Tax on a parent entity**

IIR is generally applied at the top, by the UPE's jurisdiction

- **Third Priority: Undertaxed Payment Rule ("UTPR")**

If the Top-up Tax is not paid under the IIR, other jurisdictions in which Constituent Entities operate may impose their allocable share of the Top-up Tax under the "UTPR"



How will tax incentives be affected?

Tax incentives will lose their effectiveness

- Tax incentives have had mixed results in attracting investment.
- They will be further undermined by a global minimum tax – a "floor" on effective tax rates: any income taxed under a 15% ETR could be taxed by another jurisdiction.
- Risk of discrimination between in-scope MNEs and other companies.
- There are two main categories of tax incentives:
  - "Profit-based tax incentives" that exempt corporate income from taxation, e.g., "tax holidays". These are the most likely to be affected.
  - "Cost-based incentives" that allow companies to defer taxation, e.g., "accelerated depreciation". These are meant to be preserved but might be affected depending on final design and implementation of GloBE rules.
- Incentives on VAT, custom duties, labor taxes and other on-tax contributions will not be affected. Neither will government subsidies.

Possible policy responses

How to prepare for the implementation of the global minimum tax?

Five steps :

1. Assess the potential impact in your country: Are there many branches of in-scope MNEs? What is their effective tax rate? Do they benefit from large tax exemptions?
2. Review headline corporate income tax rate – generally applicable rate and any sector-specific rate – is it higher than 15%?
3. Review tax incentives in tax codes, investment or sectoral laws, export processing zones and investment agreements.
4. Consider implementing a qualified domestic minimum tax (QDMT)
5. Review stabilization clauses in contracts and treaties in case they “lock-in” fiscal regimes and tax incentives.

Thank You!

For more information:

Email: tlassourd@iisd.org

https://www.iisd.org/articles/global-minimum-tax-deal

https://www.iisd.org/itn/en/2021/10/07/the-end-of-tax-incentives-how-will-a-global-minimum-tax-affect-tax-incentives-regimes-in-developing-countries-alexandra-readhead-thomas-lassourd-howard-mann/