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Global Tax Alert

The Latest on BEPS and Beyond

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Highlights

The publication of the GloBE Model Rules by the Inclusive Framework on 20 December confirmed what the global tax community had already started to realize: the Pillar Two rules are not only highly complex, they also herald a new wave of tax reporting requirements. In the same week, the European Commission (Commission) added to that. On 22 December, it presented a draft directive against the use of shell entities for tax purposes, called "UNSHELL" for short.

To protect the European tax base, UNSHELL would introduce a look-through approach to deny benefits of intra-European Union (EU) tax treaties and Directives to "shell companies." At first glance, the measures target a limited group of companies in the EU. Under the proposal, an entity is generally regarded as a shell company if established with the aim to obtain tax benefits while earning specific types of cross-border income, provided it has outsourced its day-to-day administration, lacks substance and does not conduct genuine economic activities. However, a closer look at the initiative indicates that the impact will be more significant.

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First, the proposed framework will require all entities to self-assess the extent to which they are in scope of the proposed rules. Under the seven-step analytical framework of the draft Directive, a large number of European companies will have to provide tax authorities specific information on their nature and characteristics. Tax authorities in the EU will exchange this information automatically, potentially sparking a new wave of tax audits.

Second, the Commission has already announced that it will supplement the proposal with an initiative that will address entities in third states. This would level the playing field between EU Member States and third states, but also underlines the Commission's objective to lead in global tax standard setting.

The UNSHELL proposal is now subject to negotiation between the 27 Member States. Businesses and investors should prepare for the new reporting requirements and review existing structures. Though it remains to be seen whether UNSHELL will be adopted at the EU level, national legislators in the EU and beyond may take inspiration from the proposal and develop similar initiatives, riding the new wave of tax reporting requirements.

European Union

Draft Directive for implementing BEPS 2.0 Pillar Two Model Rules

On 22 December 2021, the Commission published a legislative proposal for a Directive setting forth rules to ensure a global minimum level of taxation for multinational groups (the draft Directive). The proposed rules are generally consistent with the agreement reached by the Inclusive Framework on BEPS on 8 October 2021 (the October Statement), and closely follow the Model Rules published on 20 December 2021.

The draft Directive aims at consistently implementing among all 27 Member States, the Model Rules that include an Income Inclusion Rule (IIR) and an Under Taxed Payments Rule (UTPR), referred to collectively as the "GloBE rules." However, it also extends its scope to large-scale purely domestic groups, in order to ensure compliance with the fundamental freedoms. In addition, the draft Directive makes use of an option contemplated by the Inclusive Framework whereby the Member State of a constituent entity applying the IIR is required to ensure effective taxation at the minimum agreed level not only for foreign subsidiaries but also for all constituent entities resident in that Member State.

The proposal will now move to the negotiation phase among the Member States with the aim of reaching a final agreement. In the EU, the adoption of tax legislation requires unanimity between all 27 Member States. The Commission proposes that the Member States shall transpose the Directive into their national laws by 31 December 2022 for the rules to come into effect as of 1 January 2023, with the exception of the UTPR, for which the application will be deferred to 1 January 2024.

See EY Global Tax Alert, *European Commission proposes tax Directive for implementing BEPS 2.0 Pillar Two Model Rules in the EU*, dated 22 December 2021.

Draft Directive for preventing the misuse of shell entities (UNSHELL)

Also on 22 December, the Commission published a legislative proposal for a Directive setting forth rules to prevent the misuse of shell entities for tax purposes (the draft Directive, UNSHELL, is also referred to as the Anti-Tax Avoidance Directive (ATAD) III). This initiative was announced by the Commission in its Communication on Business Taxation for the 21st century published in May 2021.

The draft Directive aims at introducing an EU-wide "substance test," including a reporting obligation for taxpayers, to assist Member States in identifying undertakings that are engaged in an economic activity but which do not have minimal substance and, in the view of the Commission, are misused for the purpose of obtaining tax advantages (shell companies). In addition, the Commission proposes to attach consequences to the qualification of a company as a shell company for tax purposes. It also envisages the automatic exchange of information by amending the Directive on administrative cooperation in the field of taxation (Directive 2011/16/EU or DAC) as well as a potential request by one Member State to another for tax audits.

The draft Directive will now move to the negotiation phase among Member States with the aim of reaching a final agreement. In the EU, adoption of tax legislation generally requires unanimity between all 27 Member States. The Commission proposes that the Member States shall transpose the Directive into their national laws by 30 June 2023 for the rules to come into effect as of 1 January 2024.

See EY Global Tax Alert, *European Commission publishes draft Directive for preventing the misuse of shell entities (UNSHELL)*, 22 December 2021.

Pillar One will help to finance EU recovery fund

The Commission also published on 22 December a Communication on the next generation of the EU own resources for the EU budget (the Communication). This follows the establishment of the €750 billion EU recovery instrument (NextGenerationEU) in 2020 and the agreement to introduce new EU-own resources that will generate revenues to help repay the financing of the NextGenerationEU.

The Communication outlines the Commission's proposals to use portions of revenues from the EU emissions trading system (ETS), the carbon border adjustment mechanism (CBAM), and the taxation of reallocated profits of large multinationals under Pillar One of the G20/OECD BEPS 2.0 project to finance the EU budget. The Communication provides the revenue estimates for new own resources and percentages of the revenues that will become own resources, and it details how each levy would operate as an own resource.

Together with the Communication, the Commission also published the proposal for amendments to the EU-own resources decision to reflect the three new EU-own resources and the proposal for revisions of the Regulation establishing the 2021 to 2027 multinational financial framework.

The Communication also mentions that the Commission will present a proposal for a second basket of new own resources by the end of 2023, which will include a Financial Transaction Tax and another own resource linked to the corporate sector.

See EY Global Tax Alert, *European Commission proposes that green levies and Pillar One help finance EU recovery fund*, dated 22 December 2021.

Country developments

Australia: Final guidance on imported hybrid mismatch rule

On 16 December 2021, the Australian Taxation Office (ATO) released in final Practical Compliance Guideline PCG 2021/5. PCG 2021/5 replaces draft PCG 2021/D3 and provides final guidance on the ATO's assessment of the relative levels of tax compliance risk associated with the imported mismatch rule. Broadly, the imported hybrid mismatch rule disallows a deduction for a payment if the income from such payment is set off, directly or indirectly against a deduction that arises under a hybrid mismatch arrangement in an offshore jurisdiction.

The guidance provides a framework of seven color-coded risk zones ranging from white (where the ATO has provided clearance to the taxpayer) through green (low risk) to red (very high risk). Taxpayers who are required to prepare a Reportable Tax Position Schedule may be required to self-assess the risk of the imported hybrid mismatch rule applying to their related-party arrangements. If the taxpayer's risk rating is not low, there is no presumption that the arrangements do not comply with Australian tax law, but the ATO is more likely to conduct some form of engagement and assurance activity to further test the taxation outcomes of the arrangements.

The guidance practically applies from 1 January 2019, the commencement date of the hybrid mismatch rules.

See EY Global Tax Alert, *Australian Taxation Office releases final guidance on imported hybrid mismatch rule*, dated 16 December 2021.

Azerbaijan: Revision of the Tax Code, including changes to CFC and TP rules

On 29 December 2021, Azerbaijan adopted a law to amend the Tax Code. Among other items, the amendments include introduction of a Controlled Foreign Corporation (CFC) regime, and changes to the transfer pricing (TP) rules.

Under the CFC legislation, profits of nonresident entities incorporated under the jurisdictions with a preferential tax regime determined as such under the Decision of Cabinet of Ministers and satisfying the following conditions should be subject to tax in Azerbaijan:

- More than 50% interest in a nonresident entity is directly or indirectly owned by an Azerbaijani company or together with its resident or nonresident related party.
- The effective tax rate in the foreign jurisdiction is lower than half of the one to be paid in Azerbaijan for the same income.
- 30% or more of the foreign company's income consists of specific items, like royalties from intellectual property, proceeds received from financial leasing, financial assets, sales of shares and interests and others.

As for TP rules, new transactions are considered to be in scope including:

- Transactions between a resident and its permanent establishments (PEs) in other jurisdictions
- Transactions between a resident and a PE of a nonresident with a nonresident entity on sales/purchase of goods traded on the international stock exchange
- Transactions between a resident and a PE of a nonresident with a nonresident entity provided that annual total revenue of the resident or PE of nonresident exceeds AZN30 m and the total volume of transactions with such nonresident is more than 30% in total income/expenses of resident or PE of nonresident

The fines for failure to submit a TP report or when the submission is incomplete or includes inaccurate information have been increased from AZN500 to AZN2,000 (from US$294 to US$1,177). The same sanction is prescribed for the non-submission, incomplete or inaccurate submission of a CFC notification. The form of Notification as well as rules on taxation of CFC's income in Azerbaijan are expected to be issued by the tax authorities.

The rules are effective as of 1 January 2022.

Belgium: Update to the list of low-tax jurisdictions and non-cooperative states

On 20 December 2021, the Belgian Tax Authorities published Circular 2021/C112 updating the list of low-tax jurisdictions and non-cooperative states. As part of the tax obligations in Belgium, taxpayers need to report in their tax returns any payments exceeding €100,000 to any jurisdiction treated as a tax haven. From a Belgian perspective, a jurisdiction is treated as a tax haven if: (i) the nominal tax rate is less than 10%; (ii) does not follow the OECD standards on transparency and exchange of information; and (iii) is listed on the EU list of non-cooperative jurisdictions. Accordingly, payments made to a jurisdiction considered as a tax haven and not reported in the tax return are considered as non-deductible payments.

The updated list includes: Abu Dhabi, Ajman, American Samoa, American Virgin Islands, Anguilla, Bahamas, Bahrain, Barbados, Bermuda, Botswana, British Virgin Islands, Cayman Islands, Dominica, Dubai, Fiji, Fujairah, Ghana, Guam, Guatemala, Guernsey, Isle of Man, Jersey, Kazakhstan, Liberia, Malta, Marshall Islands, Micronesia (Fed.), Monaco, Montenegro, Nauru, Palau, Panama, Pitcairn Islands, Ras al Khaimah, Saint-Barthélemy, Samoa, Seychelles, Sharjah, Somalia, St. Maarten, Trinidad and Tobago, Turkey, Turkmenistan, Turks and Caicos Islands, Umm al Quwain, Uzbekistan, Vanuatu and Wallis and Futuna Islands.

Canada: Proposal for implementation of a Digital Services Tax

On 14 December 2021, Canada's Deputy Prime Minister and Minister of Finance tabled in the House of Commons a notice of ways and means motion to implement a Digital Services Tax (DST).

The DST is expected to apply to large businesses operating in the digital sector. The proposal contains the following tax liability thresholds: (i) €750 million of total revenue from all sources during a fiscal year that ends in the preceding calendar year; and (ii) CA$20 million of Canadian digital services revenue. The tax base depends upon whether revenue is associated with users in Canada, and consists of the Canadian online marketplace, advertising and social media services revenue, and the Canadian user data revenue. The tax rate is currently set at 3%. The proposed legislation also contains detailed administration, enforcement and anti-avoidance provisions.

The DST, if implemented, will be payable in respect of taxable Canadian digital services revenue earned as of 1 January 2022. The DST would not be imposed earlier than 1 January 2024 and only if the multilateral convention implementing Pillar One has not come into force within the expected timeline. In the event of a delay or failure of the implementation of Pillar One, the DST will be payable in respect of revenues earned as of 1 January 2022, but no earlier than 1 January 2024.

Finally, stakeholders have been invited to provide comments by 22 February 2022.

See EY Global Tax Alert, *Canada's Minister of Finance tables Digital Services Tax*, dated 20 December 2021.

Cyprus: Introduction of withholding tax on passive income payments to companies in non-cooperative jurisdictions

On 21 December 2021, Cyprus published in the *Official Gazette* the bills amending the Income Tax Law and the Special Contribution for the Defense of the Republic Law. The changes introduced include among others the following:

- The definition of corporate tax residency has been extended to include the incorporation test, on top of the management and control criteria, which will apply to companies that are not resident for tax purposes in any tax jurisdiction.
- A withholding tax on outbound payments of dividends, interest and royalties made to companies resident or registered in jurisdictions included on the EU list of non-cooperative jurisdictions on tax matters (Annex I). The tax rate differs depending on the income type (17% on dividends, 30% on interest and 10% on royalties).

Both laws will be effective as of 31 December 2022.

See EY Global Tax Alert, *Cyprus amends definition of corporate tax residency and introduces withholding tax on payments of dividends, interest and royalties to companies in non-cooperative jurisdictions*, dated 23 December 2021.

Denmark: Amendment to the list of jurisdictions subject to defensive tax measures

On 28 December 2021, Denmark published Law No. 2613 to update the list of jurisdictions subject to the defensive measures for non-cooperative jurisdictions. The defensive measures that are applicable in Denmark include a withholding tax on dividend payments and the denial of deductions for payments to non-cooperative jurisdictions. In this update, Denmark removed Anguilla, Dominica, and Seychelles from the list and added Trinidad and Tobago. The updated list is aligned with the EU list of non-cooperative jurisdictions (Annex I).

Germany: Publication of updated domestic list of non-cooperative jurisdictions

On 23 December 2021, Germany published in the *Official Gazette* the Tax Haven Ordinance listing the non-cooperative jurisdictions for tax purposes. The list is in line with the EU list of non-cooperative jurisdictions (Annex I) and includes American Samoa, Fiji, Guam, Palau, Panama, Samoa, Trinidad and Tobago, US Virgin Islands, and Vanuatu. This list is relevant for the defensive tax measures taken by Germany. For example, payments made to the listed jurisdictions can be denied and German taxpayers are required to provide extended information.

The updated list became effective on 24 December 2021.

Greece: List of Non-Cooperative Jurisdictions for 2020

On 29 November 2021, the Greek Government published Decision A. 1246 to update the domestic list of non-cooperative jurisdictions for fiscal year 2020. The updated list includes the following jurisdictions for the entire 2020 fiscal year:

Anguilla, Antigua and Barbuda, Barbados, Benin, Botswana, Burkina Faso, Cambodia, Chad, Djibouti, Dominica, Eswatini, Gabon, Ghana, Guatemala, Guinea, Guyana, Haiti, Honduras, Ivory Coast (Cote d' Ivoire), Jordan, Kazakhstan, Lesotho, Liberia, Madagascar, Maldives, Mali, Mauritania, Namibia, Niger, Oman, Palau, Panama, Papua New Guinea, Paraguay, Philippines, Rwanda, Seychelles, Sint Maarten, Tanzania, Thailand, Togo, Trinidad and Tobago, and Vanuatu.

Further, some jurisdictions have been included in the list for part of fiscal year 2020 starting 1 January such as Kenya considered as a noon-cooperative jurisdiction until 31 October 2020 and Cape Verde, Mongolia, Montenegro until 30 April 2020.

Ireland: Public consultation with respect to the possible introduction of to introduce a territorial system of taxation

On 22 December 2021, the Irish Department of Finance issued a public consultation seeking input on the potential move to a territorial system of taxation. The purpose of the consultation is to obtain views from stakeholders on the issues detailed in the public consultation document which will inform potential further consultation on this matter in the future. Following a period of reform to Ireland's corporation tax framework and wider global reforms, including the recent Agreement at OECD to address the tax challenges arising from digitalization, the Department of Finance considers that it is timely to revisit the possible transition to a participation exemption and/or branch exemption regimes.

The consultation period runs from 22 December 2021 until 7 March 2022.

Korea: Guidance on Mutual Agreement Procedure (MAP)

On 18 November 2021, the Korean National Tax Service issued an updated version of the Guidance on Mutual Agreement Procedure (Guidance). The updated version of the Guidance aims to comply with the international standards. The Guidance consists mainly of an overview of the MAP, the MAP's application, procedure and closing, and the implementation of the MAP's outcome. The Guidance also includes the forms relevant for MAP documentation.

Netherlands: List of low-tax jurisdictions for 2022 published

On 28 December 2021, the Netherlands published in the *Official Gazette* Decree No. 48346 to implement a number of tax measures. Among other items, the Decree updated the list of low-tax jurisdictions for purposes of the application of the conditional withholding tax on interest and royalties on payments to a related party. The updated list includes jurisdictions that have a corporate income tax rate lower than 9% (i.e., Anguilla, Bahamas, Bahrain, Barbados, Bermuda, British Virgin Islands, Cayman Islands, Guernsey, Isle of Man, Jersey, Turkmenistan, Turks and Caicos Islands, Vanuatu and the United Arab Emirates). Also, the list contains the jurisdictions that are included on the EU list for non-cooperative jurisdictions.

The Decree became effective on 1 January 2022.

Netherlands: Conditional withholding tax on interest and royalties to be expanded to dividends as of 2024

On 4 November 2021 the Netherlands enacted a change to the conditional withholding tax on interest and royalties. Under this amendment, the scope of the conditional withholding tax will be expanded to dividends distributed to beneficiaries in "low-taxed jurisdictions." A jurisdiction is a low-tax jurisdiction if it is included on the list of low-taxed jurisdictions published annually by Decree. This measure will exist together with the dividend withholding tax. The applicable withholding tax rate for the conditional withholding tax on dividends is equal to the prevailing corporate income tax rate (now: 25.8%); the tax due will be reduced by any dividend withholding tax due.

The effective date of this amendment is 1 January 2024.

Romania: Government approves the ratification of the MLI

On 4 January 2022, the Romanian President promulgated Decree No.14/2022 ratifying the *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting* (MLI). The instrument of ratification still needs to be deposited before the MLI will enter into force with respect to its covered tax agreements (CTAs). Romania submitted its provisional MLI positions at the time of signature, listing its reservations and notifications as well as the 91 CTAs it wishes to be covered by the MLI. A definitive list of reservations and notifications will also need to be provided upon the depositing the instrument of ratification.

Thailand: Deadline for CbC reporting extended

On 23 December 2021, the Thai Ministry of Finance announced the extension of the deadline for the Country-by-Country (CbC) report filing obligation (previously set at no later than 150 days from the close of the financial year). The changes introduced are:

- A deadline of 12 months starting from the end of the relevant accounting period for ultimate parent companies incorporated under Thai law and for Thai surrogate entities
- A deadline of 60 days starting from the receipt of a notice from the tax authority to file for a subsidiary carrying on business in Thailand and required to file a report in the country

The CbC reporting obligation applies for accounting periods as of 1 January 2021.

Thailand: Approval of the MLI

On 28 December 2021, the Thai Council of Ministers approved the signature of the MLI. It is now expected that the Thai Minister of Finance will send a letter to notify the OECD of the country's intention to join the MLI. At the time of signature, Thailand must submit a list of tax treaties in force that it would like to designate as CTAs and a preliminary list of its MLI positions. Following the signature of the MLI, Thailand will need to deposit its instrument of ratification of the MLI with the OECD. At the time of depositing the instrument of ratification, Thailand must confirm its MLI positions.

United Kingdom: Public consultation on Pillar Two Model Rules

On 11 January 2022, Her Majesty's Revenue and Customs (HMRC) released a public consultation on Pillar Two Model Rules as published by the OECD on 20 December 2021. In this consultation, the United Kingdom (UK) seeks input on the application of the Model Rules as well as on a series of wider implementation questions. Also, the public consultation asks for views on the introduction of a UK domestic minimum tax and wider reforms to existing UK BEPS measures. The UK Government is also planning to engage stakeholders over the coming months to seek views on the detailed design of Pillar One as well as to address the provisions of the multilateral convention and domestic legislation required to implement Pillar One in the UK.

The public consultation runs from 11 January 2022 until 4 April 2022. Following that, the UK Government expects to publish draft legislation for the implementation of Pillar Two in summer 2022.

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