July 2024

Tax Alert

Australian 15% global and domestic minimum taxes law introduced into Parliament

At a glance

- Legislation introduced to implement:
  - An Income Inclusion Rule (IIR) applying to years starting from 1 January 2024
  - An Undertaxed Profits Rule (UTPR) applying to years starting from 1 January 2025
  - A domestic minimum tax (DMT) applying to years starting from 1 January 2024.
- In-scope MNE Groups will be required to lodge at least three new returns in an approved form to the ATO:
  - A GloBE Information Return (GIR)
  - An Australian IIR/UTPR Tax Return
  - DMT Return(s)
- How EY can help

On 4 July 2024, the Australian Government introduced legislation into Parliament, to implement Australia's adoption of the OECD/G20 Pillar Two solution, including a 15 per cent global minimum tax and domestic minimum tax (DMT) following public consultation of exposure drafts (EDs) in March 2024.

This Tax Alert outlines the key aspects of the primary legislation, the major changes from the EDs released in March 2024 and the implications of those changes.

The introduction of the Bills to Parliament represents a significant step forward in Australia's implementation of Pillar Two. All three Bills have been referred to the Senate Economics Legislation Committee for inquiry with a report due by 14 August 2024. Following this, the Bills should advance quickly through the remaining legislative process and be enacted.

Australian-based and global groups with a presence in Australia should continue to progress their Pillar Two impact assessments, modelling and BEPS software implementation projects, as well as assess the impact of this development on their June 2024 financial statements.

Key features of the legislation

Consistent with the EDs released in March 2024 (EY Global Tax Alert link here), the Government introduced three Bills including:

- Taxation (Multinational – Global and Domestic Minimum Tax) Bill 2024 (Assessment Bill)
- Taxation (Multinational – Global and Domestic Minimum Tax) Imposition Bill 2024 (Imposition Bill)
- Treasury Laws Amendment (Multinational – Global and Domestic Minimum Tax) (Consequential) Bill 2024 (Consequential Bill).

The legislation implements:

- A global minimum tax by imposing top-up tax through an Income Inclusion Rule (IIR), applying to fiscal years starting from 1 January 2024.
- An Undertaxed Profits Rule (UTPR), applying to fiscal years starting from 1 January 2025.
- A DMT applying to fiscal years starting from 1 January 2024.
- Consequential amendments that facilitate the administration of the top-up tax, including the preparation of three new returns for filing in Australia for in-scope multinational groups (MNE Groups).

The Taxation Multinational Global and Domestic Minimum Tax Rules (the Rules) (ED rules were also issued for consultation in March 24) which largely resemble the OECD Model Rules are contained in subordinate legislation and therefore were not introduced in the Parliament. They will be executed by the Minister by way of Legislative Instrument and will be tabled in the Parliament once finalised.

Key changes in the Bills from the March EDs

Following the release of the March EDs, the primary legislation was subject to a short public consultation process which closed on 16 April 2024. Certain changes have been made to the Bills following that consultation and because of further work undertaken by Treasury.

Interaction with Australia's domestic tax laws

In line with the positions set out by Treasury in the discussion paper released for consultation in March 2024, the following amendments to the *Income Tax Assessment Act 1936* (ITAA 1936) and *Income Tax Assessment Act 1997* (ITAA 1997) have been included in the Consequential Bill to address the interaction between the global and domestic minimum taxes and Australia's hybrid mismatch rules, foreign hybrid rules, controlled foreign company (CFC) regime and foreign income tax offset (FITO) rules:

- Hybrid mismatch rules - Divisions 830 and 832 of the ITAA 1997 are amended to ensure that the operation of the Australian hybrid mismatch rules and targeted integrity rule, remain unaffected by foreign GloBE tax.
- Foreign hybrid rules - References to 'foreign income tax' in Sections 830-10 and 830-15 are amended to exclude foreign GloBE tax and other foreign minimum tax.
- CFC regime - Section 393 of the ITAA 1936 is amended to provide for a notional allowable deduction for foreign DMT tax, but not for foreign IIR tax and foreign UTPR tax.
- FITO rules – Division 770 of the ITAA 1997 is amended to exclude foreign IIR tax and foreign UPTR tax from being eligible to claim a FITO. This is to ensure that a FITO can only be claimed in respect of a foreign DMT tax, subject to the new integrity rule below.

Denial of FITO in certain circumstances

In the March 2024 discussion paper, that there could be future jurisdictional responses to global and DMT rules designed to compensate MNE Groups for the imposition of top-up tax, such as where a foreign jurisdiction implements a DMT but to maintain its competitiveness, effectively redirect the additional tax revenue back to the relevant MNE Groups through government grants, credits, or other incentives.

The Bill introduces a new Section 770-145 in the ITAA 1997 to target such responses, which will need to be assessed by the Australian entity which is claiming the FITO.

Section 770-145 provides that an entity will be denied a FITO for 'foreign DMT tax' paid where it (or another group or joint venture (JV) entity) is entitled to:

- A refundable tax credit which is computed as an excess over the entity's income tax liability;
- Consideration for the transfer of a transferable tax credit;
- Cash or cash equivalent amounts recognised as government grants; or
- A benefit of a kind specified by the Minister (by way of legislative instrument) in respect of a specified jurisdiction.

Importantly, the definition of 'foreign DMT tax' includes tax that is payable under a foreign qualified domestic minimum tax (QDMTT). This means that a FITO may be denied for taxes paid under a foreign QDMTT that has been certified as qualified by the OECD Peer Review process where one or more of the above criteria is satisfied.

The three examples provided in the Explanatory Memorandum (EM) all relate to FITOs claimed in respect of income attributed under Australia's CFC regime. The first example in the EM is as follows:

> Entity A is a Constituent Entity located in Jurisdiction A and a CFC which is wholly owned by Aus Co and part of the same MNE Group. Entity A pays $10 of corporate income tax and $5 of foreign DMT tax in Jurisdiction A. Entity A also receives a $6 government grant. Absent the new integrity rule in Section 770-145, the amount of FITO that could have been available for Aus Co is $15. However, the FITO will be reduced by the government grant ($6), capped at the amount of foreign DMT ($5). Therefore, the FITO is $15 - $5 = $10.

Interaction with Australia's tax cost resetting process under tax consolidation

There is no clarification included in the Bills as to the interaction with Australia's tax consolidation rules specifically in relation to the tax cost resetting on the formation, joining or exit from an Australian Tax Consolidated Group (TCG) under Division 705 and Division 711 of the ITAA 1997.

However, the recent OECD Administrative Guidance issued in June 2024 (EY Global Tax Alert link here) provides some clarification as to how the local tax basis is included in the determination of 'deemed' DTAs and DTLs which are relevant for the determination of the total deferred tax adjustment Amount. The guidance sets out that the deferred tax expense or benefit included in the total deferred tax adjustment amount should be calculated by reference to the GloBE carrying value (rather than the accounting carrying value) and the local tax basis.

For example, in circumstances where the GloBE carrying value of an asset or liability is adjusted to be aligned with the local reset tax basis, the related deferred tax expense or benefit recorded for accounting purposes will be disregarded for GloBE purposes. However, if the GloBE carrying value does not match the local reset tax basis, a 'deemed' DTA or DTL based on the GloBE carrying value must be taken into account for purposes of determining the adjusted covered taxes, even if there was no DTA or DTL recorded (for instance, because the accounting carrying value and local tax basis were equal).

However, this guidance does not apply to assets acquired in transactions within the scope of Article 9.1.3. (i.e., intra-group transfers of assets during the Pre-GloBE Period that started on 1 December 2021 through to when the relevant jurisdiction no longer qualifies for or applies the transitional safe harbour) or where the initial recognition exception under the relevant accounting standard would apply.

Joint and several liability

The provision in the March ED that the head company of a tax consolidated group would be liable for the top-up tax of the members of the group has been removed.

The Consequential Bill now provides for joint and several liability of tax-related liabilities amongst group entities and JV groups.

The EM states that the provisions "are necessary to ensure the effective and efficient collection of top-up tax, and other tax-related liabilities. Otherwise, an applicable MNE group could locate its assets in jurisdictions beyond the reach of the Commissioner, frustrating the collection of these liabilities or making collection challenging and inefficient. The operation of these integrity provisions, which may involve the application of a number of these provisions sequentially, ensures that the Commissioner can collect on these tax-related debts in an efficient and timely manner."

In the absence of a clear exit mechanism similar to that which operates under Australia's tax consolidation regime, the introduction of joint and several liability amongst group entities will likely give rise to significant tax due diligence considerations for any group entity which is transferred even when that entity did not have a primary top-up tax obligation or give rise to the top-up tax.

Collection of tax from partnerships, joint ventures and trusts

The Consequential Bill introduces rules designed to ensure obligations and liabilities imposed under the minimum tax law can be enforced and collected effectively and efficiently with respect to partnerships, JVs (including unincorporated JVs), trusts and other arrangements that are treated as entities under the minimum tax law but lack legal capacity.

Effectively, these rules identify the legal entity behind each of these deemed entities, upon whom obligations can be enforced and against whom liabilities can be collected.

Australian DMT returns

The Consequential Bill requires each group entity in Australia to give a DMT return to the Commissioner within the time period required for lodging the GloBE Information Return (GIR), even if there is a nil amount of DMT payable. Consistent with the March ED, the Bill does not allow for the filing of a single aggregated DMT return covering all Australian entities. However, the Bill introduces the ability for the Commissioner to make a determination, by way of legislative instrument, specifying the circumstances in which a group entity need not lodge a DMT return. It is unclear whether these specific circumstances will include exemptions for members of tax consolidated or multiple entry tax consolidated groups, where the lodgement obligation is met by the head company of the group.

The DMT returns must be lodged electronically in the approved form. A group entity's obligation to lodge a DMT return may be met a designated local entity (which is an entity appointed by all group entities within the MNE Group to lodge the Australian DMT return on behalf of each of those group entities which have an obligation to lodge).

Australian IIR/UTPR tax returns

The Consequential Bill requires each group entity of an applicable MNE group that is located in Australia to give the Commissioner an Australian IIR/UTPR tax return (even if there is nil Australian IIR/UTPR payable). This requirement may be met by a designated local entity, which gives the Commissioner an Australian IIR/UTPR tax return on behalf of a group entity. It introduces the ability for the Commissioner to make a determination, by way of legislative instrument, specifying the circumstances in which a group entity is exempt from giving an Australian IIR/UTPR tax return.

Changes and clarifications to entity definitions

The Bills and EM include several changes from the March EDs and clarifications to defined terms and introduces new defined terms relating to the treatment of certain entities. Some key changes include:

- The EM states that it is generally expected that an Australian complying superannuation fund (within the meaning of complying superannuation fund in Section 45 of the *Superannuation Industry (Supervision) Act 1993*) would meet the definition of a pension fund.
- The definition of government entity has been amended to include an entity carrying on a business that only provides products or services for use by that government to fulfil a government function.

- The definition of investment fund now includes rules to determine when an investor is connected to another investor.
- The treatment of Permanent Establishment (PE) has been further clarified, for example, if the main entity in respect of a PE is a JV or a JV subsidiary, then any PEs of the main entity are a JV subsidiary of the JV. Also, if the main entity is an excluded entity, a PE in respect of that main entity is deemed to be an excluded entity.

How EY can help

Our EY Team of BEPS advisors can assist you with:

- Navigating the complexities of the new global and domestic minimum tax regime.
- Understanding the financial reporting and compliance obligations.
- Assisting with your Pillar Two impact assessment and technical advice.
- Providing advice on the interaction of Pillar Two with Australia's local tax rules.
- Training for your internal tax teams and other key stakeholders.
- Current-state assessment of data availability, systems and processes and assistance with software implementation and process redesign.
- Considering any other implications for your commercial arrangements.

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