Technology Industries of Finland

4/6/2022

Technology Industries of Finland's submission to the public consultation: Directive proposal on minimum level of taxation for large multinational groups

6 April 2022

The Commission has requested comments regarding the Council Directive on the minimum level of global taxation of multinational groups in the Union ("the Directive" or "Minimum Tax Directive"). The version open for feedback is the original version published on 22 December 2021. However, the Minimum Tax Directive has already been discussed at ECOFIN-meetings in March and April, with a goal to find an agreement. A Compromise Proposal was released on 12 March 2022 ("Compromise Proposal"). Technology Industries of Finland (TIF) welcomes the opportunity to comment the Directive proposal.

1 Summary

The Technology Industries of Finland (TIF) agrees that minimizing tax evasion and avoidance and combating harmful tax competition are important goals. Global, EU-level and national minimum tax regulations must be as consistent as possible. Otherwise, the risk of breaching interpretations by member states, double taxation and tax disputes is high.

The biggest challenge in preparing the Minimum Tax Directive is the tight schedule. The preparation schedule should be extended by at least one year to allow for consistency. The OECD will continue its work for 2022 providing much needed clarification and simplification to the minimum taxation rules. All the differences between the Directive and Model Rules will only be visible when the OECD's work is ready.

One important question discussed in the OECD at the moment are **R&D tax incentives and whether they should be excluded from the ETR calculation.**[1] Without huge R&D-investments we will not be able to reach the agreed carbon neutral targets. This question should be analysed and discussed also in the EU, before the Directive text is agreed.

Even though the Compromise Proposal gave a much needed extension to the transposition schedule until 31 December 2023, there should be an additional one year before agreeing on the Directive text. Deciding based on the situation on December 2021, is premature. **Thus, TIF hopes that the Directive text would be amended to comply with the OECD Model Rules, Commentary and Implementation framework and agreed Q1/2023.** In addition, companies and tax authorities need time to manage the technical changes required, after the Directive is agreed and comes into force. **TIF suggests that the Directive would be applied for fiscal years beginning from 1 January 2025.**

[1] Qualified refundable tax credits are discussed in the Directive in article 15(5), OECD Model Rules Article 3.2.4 and R&D costs in the OECD Commentary in article 4.4.5, paragraph C (Recapture Exception Accrual Rule).

Technology Industries of Finland
Eteläranta 10, P.O.Box 10, FI-00131 Helsinki
Telephone +358 9 192 31
www.techind.fi
Business ID: 0215289-2

Technology Industries of Finland

2 The Directive must comply with changes due to the continuing work of the OECD

The Commission's proposal for a Directive is largely based on the OECD's proposal of 20 December 2021 for Model Rules on global minimum taxation for multinational groups: Tax Challenges Arising from the Digitalisation of the Economy - Global Anti-Base Erosion Model Rules (Pillar Two), The Global Anti-Base Erosion Rules). The Commission has stated that the Minimum Tax Directive is fully in line with the OECD's GloBE proposal, but there are already now some substantial differences.

Extensive international cooperation is the only sensible way to modernize the tax system in a sustainable way, as companies do business globally. Changes to tax systems should, in principle, be OECD-driven. Throughout the project, the OECD has emphasized the importance of international co-operation and warned the EU not to rush into its own solutions. The EU, on the other hand, has given its strong public support to the OECD's preparations.

Based on the timetable envisaged by the Commission, it would appear that drafting processes are now differentiating. The Commission proposes that the Directive be finalized and agreed before summer 2022. The Directive text to be agreed is largely based on the original wording of December 2021. The OECD has announced that the work regarding Pillar 2 will continue in 2022. As the OECD's preparatory work continues, there will be even more differences in the models. It is certain that the draft Directive, which was finalized in December 2021, will become obsolete and contradictory when the OECD global model is completed at the end of 2022.

We do warmly welcome the principle added to the compromise proposal that the OECD Model Rules, the Commentary[2] and Implementation Framework[3] should be used as a source of illustration and interpretation.

- *In implementing this Directive, Member States should use the 'Tax Challenges Arising from the Digitalisation of the Economy Global Anti-Base Erosion Model Rules (Pillar Two)' agreed by the OECD/G20 Inclusive Framework on BEPS and the explanations and examples in the OECD Commentary on the GloBE Rules under Pillar Two, as well as the GloBE Implementation Framework, including its safe harbours rules, as a source of illustration or interpretation in order to ensure consistency in application across Member States to the extent that they are consistent with the provisions of this Directive and with Union law. The safe harbours rules should be of relevance as regards MNE groups as well as large-scale domestic groups.*

This is however not adequate. Implementing a tax model different from the rest of the world would create significant uncertainty and reduce tax predictability, undermining the attractiveness, competitiveness and functioning of the EU internal market. Conflicts of interpretation cause costs

[2] https://www.oecd.org/tax/beps/tax-challenges-arising-from-the-digitalisation-of-the-economy-global-anti-base-erosion-model-rules-pillar-two-commentary.pdf Further technical guidance ("The Commentary") clarifying the pillar 2 GloBE model rules was published on 14 March 2022. According to the OECD, the Commentary elaborates on the application and operation of the Global Anti-Base Erosion (GloBE) rules and provides MNEs and tax administrations with detailed and comprehensive technical guidance on the operation and intended outcomes under the rules and clarifies the meaning of certain terms. It also illustrates the application of the rules to various fact patterns. The Commentary is intended to promote a consistent and common interpretation of the GloBE Rules that will facilitate co-ordinated outcomes for both tax administrations and MNE Groups.

[3] https://www.oecd.org/tax/beps/oecd-invites-public-input-on-the-implementation-framework-of-the-global-minimum-tax.htm Implementation Framework to support MNEs and tax authorities in the implementation and administration of the GloBE Rules are being drafted and published in late 2022 or early 2023. The aim is also to help minimize compliance costs. As the first step, there is a request for public consultation to collect input from stakeholders.

Technology Industries of Finland
Eteläranta 10, P.O.Box 10, FI-00131 Helsinki
Telephone +358 9 192 31
www.techind.fi
Business ID: 0215289-2

for both businesses and tax administrations, tax disputes and double taxation. Increasing administrative costs tie up money that companies should be able to spend on growth and investment, especially in such difficult times where the COVID crisis, the war in Ukraine and the environmental crisis are all increasing the demand for huge investments to green transition. It would therefore be appropriate to take a timeout.

The fact that the OECD and the European Commission published their parallel proposals for a global minimum level of taxation within two days shows that the mutual cooperation is working. Now that the global regulation of minimum taxation is finally starting to take its final form, it would be a shame if this cooperation, that has lasted for years, was ceased “at the final straight”.

TIF hopes that coordination between the OECD and the Commission will continue as closely as possible. Further work on the OECD model rules should be taken into account in the wording of the Directive and in the national legislation of the Member States.

3 Other changes in international taxation also affect minimum taxation

During the spring, the OECD will prepare Pillar 1, which is part of the same overall package. Pillars 1 and 2 are closely linked and, depending on the final model of Pillar 1, changes may also be needed to the GloBE model rules. There is also political pressure on the overall package - many countries are agreeing to accept only a combination of the two pillars, not one without the other, as Poland stated in the April ECOFIN-meeting.

The US is making changes to its GILTI (Global Intangible Low-Taxed Income) regulation to make it compliant with GloBE regulations. For example, there will be changes to the “blending” rules, as GILTI currently accepts global blending, while GloBE uses jurisdictional blending as the model.

The Commission has stated that it will use the regulation of the OECD pillars and the directives based on them, in particular the rules for calculating the tax base and the ETR, as elements of other tax legislation in the future. For example, the calculation rules for Pillar 2 would be used in the BEFIT model. If the calculation rules are now hastily drafted, the BEFIT model will face serious problems if its “building blocks” are non-functional.

Once again, **TIF repeats the demand that the entry into force and application of the Minimum Tax Directive must be postponed**, to ensure compatibility with the international tax regulations.

4 The Minimum Tax Directive is overly complicated and burdensome

Companies must be able to be tax compliant: tax laws must be clear, comprehensive and efficient, predictable and as simple as possible. One of the main objectives of the Commission’s Communication on Business Taxation for the 21st Century is to reduce the administrative burden of taxation. The Commission has also launched projects (including an Action Plan to Fight Tax Evasion and Making Taxation Simple and Easy) to increase the use of digital taxation tools and to simplify tax reporting. This objective must also be reflected in the Minimum Tax Directive.

The cumulative effect of the combination of all the rules is unreasonably heavy. Companies cannot handle reporting manually but must have their financial management systems in place so that the data needed for reporting is available without error. Upgrading such huge enterprise-wide ERP

systems (ERP systems to control production, sales, distribution, invoicing, accounting, inventory management, etc.) can only be done once the legislation is in place. Upgrading systems is not just in the company's own hands, but software companies must make changes to the entire system, after which companies can adapt the ERP system to suit their own company's operations.

This complexity affects not only companies but also tax authorities. The authorities need to have a functioning software and instruct their personnel so that taxation is conducted correctly. The tax administration cannot develop and update its tax systems until national legislation is in place. The extension for opt-out period suggested in the Compromise Proposal is a partial solution, but only temporary. The only original wording in the Directive on simplifying tax reporting is Article 54, which states that the EU may conclude agreements with third countries to simplify reporting. This is not enough. The Directive should include clear guidance and a template for reporting. This is another reason why the Commission should await more detailed guidelines in the OECD in spring 2022.

The OECD attaches great importance to reducing complexity and simplifying procedures in its ongoing work during 2022. Among other things, there has been talk of various safe harbor models. Article 8.2 of the Model Rules outlines the possibility of such models to reduce administrative burdens and refers to the GloBE Implementation Framework[4], which will be completed by the end of 2022. This text cannot be found in the Directive. TIF is pleased that the Compromise Proposal mentions the safe harbour rules to be used as a source of illustration and interpretation "*in order to ensure consistency in application across Member States to the extent that they are consistent with the provisions of this Directive and with Union law. The safe harbours rules should be of relevance as regards MNE groups as well as large-scale domestic groups."*

In the past, the OECD was preparing, for example, "tax administrative guidance" or "white list" models, which mean excluding low-risk countries from minimum tax regulation. This would significantly simplify regulation and encourage Member States to simplify their tax systems. For example, under the OECD's Pillar 2 Blueprint, published a year ago, tax authorities would work with stakeholders (e.g., the Business Advisory Group) to publish guidelines containing a list of low-risk jurisdictions. Multinational companies located in listed jurisdictions would not be required to perform ETR calculations. This would encourage companies to relocate to countries with a broad tax base, a tax rate above the minimum tax rate, neutral and transparent taxation and a functioning tax system.

TIF is very concerned about the complexity of the Minimum Tax Directive and the administrative burden and extensive additional compliance costs for companies. The directive should also include concrete proposals to reduce tax reporting, as well as detailed reporting guidelines, such as a template.

5 The effective tax rate calculation must be manageable

Calculating the effective tax rate (ETR) is the backbone of the Minimum Tax Directive. The directive lacks clear, detailed rules on how timing differences and deferred tax assets should be treated. Temporary timing differences arise from changes in the International Financial Reporting Standard (IFRS) to local GAAP and then in comparison to taxable income in accordance with national tax laws. Comparing the figures for accounting purposes with the tax paid poses challenges even in

[4] https://www.oecd.org/tax/beps/pillar-two-model-GloBE-rules-faqs.pd fIn addition, the forthcoming Implementation "Framework will include additional administrative guidance with respect to filing obligations. Safe harbours may be developed to help mitigate compliance burdens for MNEs."

Technology Industries of Finland

the current legislative situation. The sum of taxes paid, means the taxes paid calculated according to local tax laws. According to the Minimum Tax Directive, the earnings before taxes would be calculated according to IFRS / other acceptable accounting systems. The basic problem is that the taxation of a taxable company depends on the accounting and tax rules of other countries and on the consolidated financial statements. In practice, the rules applicable to other countries would affect the tax liability for the parent company. This places a significant burden on businesses and the tax administrations. For many businesses, especially capital-intensive ones, the taxable income differs significantly from the accounting result due to timing differences in the recognition of income and expenses under national tax law and IFRS.

One important question discussed in the OECD at the moment are R&D tax incentives and whether they should be excluded from the ETR calculation. Without huge R&D-investments we will not be able to reach the agreed carbon neutral targets. If R&D tax incentives are not excluded, countries that have increased their attractiveness and competitiveness to reach R&D-functions and investments to their country, might be considered to be taxing below minimum level of tax and other countries would be able to apply top-up tax. **The treatment of R&D tax incentives in the ETR calculation should be analysed and discussed also in the EU, before the Directive proposal is agreed.**

6 Deviations from the OECD model rules should be eliminated

The Commission has stated that the Minimum Tax Directive is fully in line with the OECD's GloBE proposal. However, there are significant differences in the proposals, especially in the application to fully domestic groups and the domestic top-up tax. These deviations cannot be considered justified, and they should be eliminated from the Directive.

The need for a minimum tax mechanism arises specifically from the Group's operations in several countries and the utilization of a lower tax rate in the country of operation. **There is no need to regulate the minimum tax when all the Group's units are located in the territory of one state.** It is not clear whether the realization of the fundamental freedoms of the Union will indeed require the application of a minimum tax to pure domestic groups as well. This should be evaluated and analysed in more detail before any agreement on the Directive.

The other large deviation is enabling the collection of a minimum tax in the country of operation of a low-taxed entity, i.e., a domestic top-up tax, instead of the minimum tax levied by the residence country of the ultimate parent entity. A domestic top-up tax would mean that the minimum tax would no longer accrue to the headquarters state, in line with the OECD model, but that the benefit of the minimum tax would accrue to the low-level taxation country. The original idea of the minimum tax has been - as in the Controlled Foreign Company (CFC) legislation - that the parent company of the group is taxable and pays the difference between the minimum tax and the tax paid to the constituent entities location country to the residence country of the parent company.

A domestic top-up tax would mean that a minimum tax would be paid to the low-level taxation country. **However, this would not mean that a low-level taxation country would have an interest in raising its national tax rate. On the contrary, such a change would in practice lead to the creation of two parallel corporate tax systems in low-level taxation countries.** A low-level taxation country could still engage in tax competition at a low rate for companies that would not be subject to the minimum tax and, in addition, levy a minimum tax on other companies. Thus, tax competition would not be eliminated, but its nature would change. This is hardly the Commission's intention.

Technology Industries of Finland
Eteläranta 10, P.O.Box 10, FI-00131 Helsinki
Telephone +358 9 192 31
www.techind.fi
Business ID: 0215289-2

7 The Directive wording must be similar to the OECD model rules wording

The Directive largely follows the content of the OECD Model Rules, the December 2021 version. For some reason, however, it has been decided to rewrite the articles to the Directive. It is understandable that a difference in content (e.g., the directive also applies to purely national situations) or structure (e.g. definitions to be listed at the beginning of the directive) cause the article texts to differ. With a view to applying as uniformly as possible, the Directive should have identical text as the OECD Model Rules. Now, companies and tax authorities have to consider whether the different wording of each article has a deeper purpose and whether they constitute differences of interpretation. EU Member States will use the wording of the Directive as a basis for their own legislation, so it would be simplest and less burdensome to avoid unnecessary conflicts of interpretation. **TIF proposes that the text of the Directive be amended so that the OECD model rules are copied in identical form whenever possible.**

8 The carry-forward transition period of losses must be sufficient

The transition period for losses carry-forward before the entry into force of the minimum tax legislation must be long. This is especially important for industries with volatile nature and long economic cycle, where losses may be made for several years in a row, due to the nature of the industry. Companies that invest heavily can also have multiple loss making years before the investment generates a taxable profit. In the next few years, companies will invest a lot, e.g., investments in tangible and intangible assets are needed for R&D and the green transition. The COVID crisis, which is now in its third year, has also caused and will unfortunately cause losses for many companies. The more devastating reason that causes losses, is the war in Ukraine. In the optimal situation, all old losses should be reduced indefinitely, but the transition period should be at least 10 years.

9 Current overlapping legislation must be abolished

The draft Directive analyzes compatibility with existing legislation, such as ATAD and the recently updated Controlled Foreign Company (CFC). The Commission concludes that no changes are required, that the CFC rules apply first and that any additional taxes paid are taken into account when applying the GloBE rules. The purpose and objective of the OECD's work was to update corporate tax legislation, calm the ongoing change in tax legislation and simplify regulation. It is unreasonable to require companies to adhere to new and overlapping tax models at all times, but the duplication is not removed and taxation is not simplified. The Commission should have seriously considered the possibility of regulating IIRs by updating the existing CFC rules. As this is not the case, it must at least be ensured that the regulations are compatible and that there is no duplication or conflict of interpretation. It is not sufficient to state that 'it is not necessary to amend the ATAD' or CFC rules. **TIF requires a proper analysis and actions on how to minimize overlapping legislation.**

10 Tax penalties must not be unreasonable

Article 44 discusses penalties applicable. Luckily it seems that the disproportionate and harsh penalty rule, whereby a Member State may charge a penalty 5 % of the company’s turnover for non-compliance with the reporting obligation or for errors in the notification, has been removed from the Compromise Proposal. This would have been a completely unreasonable tax increase for

Eteläranta 10, P.O.Box 10, FI-00131 Helsinki
Telephone +358 9 192 31
www.techind.fi
Business ID: 0215289-2

Technology Industries of Finland

a company making a mistake with a really complex and completely new reporting obligation. The article states that the tax increase must be effective, dissuasive and proportionate. A 5% tax increase on a company's turnover due to a delay or inaccuracy in a tax return is far from proportionate. **TIF demands that a transitional period of 5 years will be added to the Directive, during which no tax penalty may be imposed at all. A maximum limit in euros must be set for the tax penalty.**

11 Impact assessment must be updated

The Directive states that the Commission has not carried out an impact assessment on minimum taxation, as the OECD carried out an impact assessment on Pillar 2 in 2020. It estimates that there will be an increase of USD 50-80 billion globally to tax revenues. The estimate is based on data from 2016-2017. Since then, there have been many changes to international tax legistalation, all with the same goal, to minimize tax evasion and avoidance: ATAD, BEPS, U.S. tax reform, including GILTI. While it is understandable that it is challenging to carry out a comprehensive impact assessment in a hurry, the Commission must be careful not to make fundamental changes to EU tax legislation too hastily. In addition, global figures do not reflect EU figures. **TIF hopes that an up-to-date impact analysis will be carried out in the EU, analyzing the effects also in terms of growth, administrative costs, jobs and competitiveness.**

12 Prevention and tax disputes

It is clear that a legislative change this vast and complex will cause uncertainty, unpredictability, double taxation, interpretation problems and disputes for years to come. **TIF highlights the importance and need for effective means to tax dispute resolution and prevention.**

Technology Industries of Finland
EU Transparency Register number: 39705603497-38

more information:
Maria Volanen, Head of Taxation Policy, maria.volanen@teknologiateollisuus.fi

Technology Industries of Finland (TIF) represents Finnish technology industries and has over 1,600 member companies, sizes varying from small SMEs and start-ups to world leading MNEs. The technology industry is comprised of five sub-sectors: electronics and the electrotechnical industry, mechanical engineering, metals industry, consulting engineering and information technology. Technology industry is the most important export industry in Finland, with operations constituting over 50 % of all Finnish exports and responsible for 70 % of all private investments in R&D carried out in Finland. Over 300,000 Finns work in technology companies, while a total of around 700,000 people work in the technology sector directly or indirectly (of a total population of 5,500,000).[5]

[5] For further information of TIF's member companies, please see https://teknologiateollisuus.fi/en