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Your reference: Fi 2021/04066

Stockholm, 2022-02-04

The European Commission proposals for a Council Directive on ensuring a global minimum level of taxation for multinational groups in the Union, SWD (2021) 580 final

Opinion

From a principal point of view, Näringslivets skattedelegation (NSD) is not in favor of introducing a global minimum tax. We believe that it constitutes a serious blow to the principle of tax sovereignty, which is not in the interest of a small export-oriented economy like Sweden. In addition, a global minimum tax will significantly increase the administrative burden for many Swedish companies, even though they already pay taxes at a rate above the proposed minimum level.

However, we recognize the international political pressure for international tax reform and welcome the efforts made by the OECD/Inclusive Framework (IF), resulting in a two-pillar based agreement to reform international taxation rules. The tax challenges stemming from the digitalization of the economy is a global issue requiring a global solution.

We are of the opinion that pillar 1 and 2 of the OECD/IF agreement must be treated as an integrated package to be implemented in a concerted way at a global level. If both pillars are not implemented by the US and other major trading partners at the same time as in the EU, European, and consequently Swedish, businesses could be at a competitive disadvantage.

We support the Commissions intention to make the Directive on a global minimum tax fully in line with the OECD Model Rules. The rules are extremely complex and there must be no discrepancies between the two regulatory frameworks, resulting in parallel systems. The OECD is still working on finalizing the details and will present an Explanatory Commentary in February 2022 and a detailed Implementation Framework on administration, compliance, and safe harbor rules at the end of 2022.

The Commentary and Implementation Framework are expected to include clarifications and simplifications essential for the new system to function in a manageable way. NSD believes that it is of utmost importance that the final version of the OECD Model Rules is transposed into the Directive.

This, however, is not feasible if the EU rushes the implementation ahead of the OECD rules being fully finalized. For these reasons, NSD strongly objects to and questions the Commission's intention to finalize the Directive during the spring 2022 to have the GloBe Model Rules operational and applicable from 1 January 2023.

NSD believes that sufficient time must be given for the OECD to conclude its work before Member States should agree on a final text in the Directive. If not, we could end up in a situation where a newly signed Directive, national legislation and business systems must be amended shortly after they have been put in place. This would not only be time-consuming but also costly for businesses. In addition, amending the Directive may prove to be very difficult if some countries find it against their interest.

NSD urges the Swedish Government not to agree to the Directive until the OECD work on the GloBe Rules is completed, major trading partners are implementing the same agreed rules, and the finalized OECD rules have been transposed into the final text of the Directive.

Background

Following the conclusion of the OECD Base Erosion and Profit Shifting (BEPS) project in 2015, the G20 and the OECD Inclusive Framework (IF) have presented a two-pillar based agreement of how to address the increasing tax challenges stemming from the digitalization of the economy. Pillar 1 implies a partial re-allocation of taxing rights towards market jurisdictions of excess profits, and Pillar 2 introduces a minimum effective

corporate tax rate (ETR) of 15% for multinational enterprises with an annual revenue of EUR 750 million.

On December 22, 2021, the EU-Commission presented a proposal for a Directive on ensuring a global minimum level of taxation for multinational groups in the Union.[1]

General comments

From a principal point of view, NSD is not in favor of introducing a global minimum tax.

We are concerned that the introduction of a minimum tax regime will impose additional taxation on companies, increase the administrative burden and raise the cost of investment and impede tax sovereignty of states.

We believe that the introduction of a minimum tax constitutes a serious blow to the principle of tax sovereignty, which is not in the interest of a small export-oriented economy like Sweden. It is important to respect the political will of national parliaments. The EU-treaty allocates taxation to the decision sphere of Member States. In almost all countries parliaments ask for the preservation of the right to structure their tax systems without undue interference from other governments. The introduction of a global minimum tax undermines the possibility of a country to design its tax system in accordance with its economic policies and priorities.

NSD favors fair transparent tax competition. Such competition increases pressure on governments to implement efficient and competitive tax legislation which in turn facilitates investments, growth, and new jobs. An overall increase in the corporate income tax burden on the other hand, will have a negative impact in the areas mentioned.

For several years there has been an absolute focus in the EU on anti-avoidance rules. We regret that very little attention has been given to investment- and growth friendly initiatives. Instead, a patchwork of anti-tax avoidance measures has been implemented, adding further complexity to existing complexity. We believe that if the European market shall have any

[1] Council Directive on ensuring a global minimum level of taxation for multinational groups in the Union, COM (2021) 823 final.

chance to remain competitive, it is time to shift focus to investment and growth friendly initiatives in the tax area as well as in other areas.

Furthermore, we find the introduction of a minimum tax to be inconsistent with the EU plan for a Green Deal. EU Member States have already introduced or may introduce tax incentives specifically to facilitate the adoption of renewable energy resources. Some of these incentives will not be possible to retain or may become less attractive from an investment point of view under the new minimum tax regime. The reason is primarily the fact that taxation will be based on accounting rules and not tax rules decided by parliaments. The incentives risk bringing the effective tax rate below the minimum effective rate and thereby being clawed back or eroded.

However, we do recognize the immense international political pressure for international tax reform related to the digitalization of the economy. All businesses are becoming digitalized making this a truly global issue requiring a global solution. On these grounds, NSD welcomes the efforts made by the OECD, resulting in a tax package consisting of a two-pillar based agreement to reform international taxation rules.

Integrated package deal – Global implementation

NSD agrees with the Commission that “the effectiveness and fairness of the global minimum tax reform heavily relies on its worldwide implementation”.

NSD believes that Pillar 1 and 2 of the OECD/G20 agreement should be treated as an integrated package to be implemented in a concerted way at a global level. However, we are concerned that some countries, in particular the US, will not implement both pillars, or even any of the pillars in conformity with the agreed rules. If the two pillars are not implemented by major trading partners, such as the US, it will place European, and consequently Swedish companies, at a competitive disadvantage.

Alignment with OECD Model Rules - Timetable

The Commission’s Directive proposal aims at transposing the OECD Model Rules of Pillar 2 in the EU through uniform rules and implementation. NSD finds it positive that the Commission has stated its intent to make the rules in the Directive fully in line with the OECD Model Rules, the only adjustments

being those that are necessary for the Directive to comply with primary Union law.

The OECD is still working on finalizing the details of the Model Rules and are expected to present an Explanatory Commentary in February 2022 and a detailed Implementation Framework on administration, compliance, and safe harbor rules at the end of 2022.

Parallel to the ongoing work at the OECD, businesses have already identified several provisions in the Model Rules that needs to be amended or clarified to provide certainty and to avoid future disputes. Business at OECD (formerly BIAC) has in a recent letter[2] to the OECD highlighted technical and policy issues that will require urgent clarification or modification in the model rules to avoid double taxation and ensure workability.

The regulatory framework surrounding the proposed minimum tax is extremely complex and every group in the EU that comes within the scope, MNEs as well as purely domestic groups, are likely to face high administrative costs. The OECD Commentary and Implementation Framework are expected to include clarifications and simplifications that will be essential for the new system to function in a manageable way. It is crucial that these products also are transposed into the Directive.

However, this is not feasible if the EU rushes the implementation ahead of the OECD rules being fully finalized. NSD strongly objects to the timetable presented by the Commission. We believe that sufficient time must be given for the OECD to conclude its work before Member States agree on a final text in the Directive.

Should the Directive be signed before the OECD process is completed, we may end up in a situation where, not only the newly signed Directive, but also national legislation and business systems will need to be amended shortly after they have been put in place. This would not only be time consuming but also costly for businesses. Amending the Directive may prove to be very difficult if some countries find it against their interest.

We note that countries like the United Kingdom and Switzerland have already indicated their intention to delay their implementation.

[2] https://biac.org/wp-content/uploads/2022/01/01-06-2022-Business-at-OECD-BIAC-6-Jan-Pillar-Two-Issues-Letter-1.pdf.

EU aspects

We understand that the OECD Model Rules need necessary amendments to comply with EU-law. Making the IIR applicable for pure domestic groups may seem the easiest way to ensure compliance with primary Union law, and in particular, the freedom of establishment. However, as stated in the Directive, the GloBe Model Rules have a strong cross-border dimension. The rules are obviously not intended to be applied in a pure domestic context. Furthermore, if the policy goal is to deal with remaining BEPS challenges i.e., to counter cross-border abusive behavior, this clearly does not apply for purely domestic groups.

Interestingly enough, the Commission has previously been very critical about Member States extending cross-border tax avoidance rules to purely domestic situations. As explicitly stated by the Commission in their Communication on the application of anti-abuse measures in the area of direct taxation – within the EU and in relation to third countries[3]

"In the Commission's view it would be regrettable if, in order to avoid the charge of discrimination, MSs extended the application of anti-abuse measures designed to curb cross border tax avoidance to purely domestic situations where no possible risk of abuse exists. Such unilateral solutions only undermine the competitiveness of the MSs' economies, and are not in the interest of the Internal Market."

A more proportionate and targeted approach to counter abuse and still be compliant with EU-law would have been to limit the scope to companies where there is no economic substance.[4] However, such an approach would of course come into conflict with the other policy goal, i.e., to put a floor on excessive tax competition.

This only shows the ambiguous nature surrounding the discussion on the introduction of minimum taxation as part of Action 1 of the BEPS project. Action 1 was initiated to deal with the challenges, or more precisely, the base eroding aspect, stemming from the digitalization of the economy. As it has turned out, neither the regulatory system of Pillar 1 nor Pillar 2 is specifically targeting the digitalization of the economy.

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[3] DGtaxud-PE-COM_2007_785-1695 - Anti-abuse measures_EN_ACTE.doc (europa.eu), page 6.
[4] See CJEU, 12 September 2006, case C-196/04, Cadbury Schweppes, EU:C:2006:544, paras. 54 and 67-68.

NSD believes that making the rules applicable for purely domestic groups changes the character of the proposal and, in addition, has nothing to do with the twin policy goals to tackle profit shifting and excessive tax competition. Instead, it will unnecessarily and significantly, increase the administrative burden for purely domestic groups. NSD questions the proportionality of such a measure.

Review of current anti-tax avoidance measures

In the Communication on Business Taxation for the 21st Century[5] the Commission points out that governments have engaged in adopting a patchwork of anti-tax avoidance and evasion measures and that the measures have added further complexity to existing complexity. NSD fully agrees with this view.

The IIR overlaps with existing and already implemented CFC regimes, such as the Swedish, with similar objectives on a national level. The Commission concludes that it is not necessary to amend the ATAD CFC rules on the grounds that it will be taken into consideration in the GloBe Model Rules by attributing any additional tax under a CFC regime to the relevant low-taxed entity for the purpose of computing its jurisdictional effective tax rate. While the combination of the IIR and the CFC rules may not necessarily be in conflict, it will certainly further increase the complexity and administrative burden for businesses. Clearly, a review of the appropriateness of various anti-abuse rules and the costs associated with them, is long overdue.

Consequently, we urge the Swedish Government to explore the possibilities of a review of the CFC regulations in the ATAD Directive.

Administrative simplifications

As stated above, we have underlined the importance of having the rules in the Directive fully in line with the OECD Model Rules. The upcoming OECD Commentary and Implementation Framework will hopefully provide some simplifications and additional certainty.

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[5] COM (2021) 251 final.

NSD welcomes the inclusion, in line with the OECD Model Rules, of the *“de minimis exclusion”*, allowing for an exclusion of an MNE entity when the entity’s profits do not exceed EUR 1 million and revenues are below EUR 10 million. However, we note that the provision does not have an indexation mechanism. Therefore, rising inflation will result in more and more companies exceeding the threshold, thereby eroding the potential simplification of such a measure. We encourage the Swedish Government to explore the possibilities of having such an indexation mechanism included in the Directive.

Competitiveness for Swedish companies

NSD believes that close attention must be paid to the effects the new rules may have on the Swedish corporate tax system. We are particularly concerned with any potentially negative impact relating to the Swedish rules on accelerated depreciation (överavskrivningar), group contributions (koncernbidrag), tax allocation reserves (periodiseringsfonder) and loss carry forward (förlustavdrag). For real estate companies, the extended repair deduction allowance (utvidgade reparationsbegreppet) is also of significant importance. It is important that the Swedish rules are not disproportionally affected in a way that would impact the competitiveness for Swedish companies.

Should this prove to be the case we urge the Swedish Government to consider appropriate adjustments in the corporate tax code for it to remain competitive on an international level.

Furthermore, if the US and other major trading partners decide not to introduce an equivalent minimum tax there is an obvious risk that European, and consequently Swedish, companies will find themselves at a competitive disadvantage vis-à-vis such third countries.

The risk of such a scenario increases the importance of the role of the Undertaxed Payments Rule (UTPR). The UTPR intends to work as a ‘backstop’ to the IIR and NSD welcomes the Commission’s inclusion in the Directive of a provision to assess whether a minimum tax introduced in a third country should be considered as equivalent to the IIR in the Directive. If the third country minimum tax does not pass the test, then the UTPR will be applied. As we understand the provision, a minimum tax regime in a third country jurisdiction which does not apply an effective tax rate of at least 15%

and jurisdictional blending cannot be considered equivalent to the IIR in the Directive.

Sanctions

The design of Article 44(1) is similar to the corresponding articles of the DAC6 and DAC7 respectively. This is particularly true of the last sentence of paragraph 1, which has the same wording in all three directives. NSD therefore assumes that it is up to each Member State to construct their own sanction system and grounds for exemption. Given the vague nature of the proposed regulatory framework, which bears more resemblance to accounting standards than to regulatory standards in taxation law, it is important from a legal certainty perspective that appropriate exemptions are designed and applied generously.

The proposed paragraph 2 raises several questions. It is stated that if a top-up tax information return is not submitted by a constituent entity within the prescribed time limit or if the declaration contains false information, a fee of 5% of its turnover shall be paid. At the same time, the paragraph states that this penalty shall apply only if a top-up tax information return has not been submitted no later than six months after a reminder. The wording in the last sentence of the paragraph therefore argues against the imposing of a penalty in the case of false information.

The concept of false information is not common in Swedish tax law. In our view, it does not correspond to the concept of incorrect information but refers to a more limited area of application where it is rather a question of an intentional procedure.

Given that the proposed regulatory system is unprecedented and extremely complex, NSD finds the penalty proposed exceedingly harsh. A company with a low profit margin could potentially face a sanction exceeding 100% of its profit. NSD requests more proportionate sanctions. There must be room for minor errors and misunderstandings. This holds particularly true the first years after implementation when the rules are new and particularly burdensome for both taxpayers and tax authorities.

Impact assessment

NSD questions why the Commission has not made a complete impact assessment of the proposal for a Directive.

Considering the potential implications that the new proposals could have on investments, revenue streams and administrative costs for businesses, we find it unacceptable that governments are not provided with adequate information to make a proper assessment for their countries and their businesses.

Instead, the Commission refers to a preliminary impact assessment that was presented to the Council October 25, 2019, and to an impact assessment by the OECD. These assessments have previously been criticized by businesses.[6] None of those are attached to the proposal for a Directive. Nor do those assessments take into consideration the impact of overlapping anti-avoidance measures such as CFC rules, the consequence of applying the IIR rule to purely domestic situations or the right for governments to introduce a domestic top-up tax. Furthermore, what is the potential impact if the US and other major trading partners do not implement the rules?

NSD is also concerned that wholly domestic (Swedish) groups, e.g., real estate businesses, will have to bear totally unnecessary costs for administrating the calculations according to the Directive.

Given the lack of impact assessment from the EU, we consider it necessary that the Swedish Government performs an impact assessment focusing on costs and impact on competitiveness for Swedish groups and entities.

The need for dispute resolution mechanisms

NSD is concerned that many disputes will arise as a consequence of the introduction of this complex legislation. The use of accounting rules rather than tax rules for tax purposes creates a lot of uncertainty and increases the risk for disputes due to different interpretations in various Member States. We request that further consideration be made in relation to dispute resolution

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[6] 14-12-2020-FINAL-Business-at-OECD-Letter-on-Pillar-1-and-2-Blueprints-1.pdf (biac.org) page 7 and 58 ff.

mechanisms. One way forward could be to explore the possibilities of making the Directive on tax dispute resolution mechanisms[7] applicable also in relation to disputes that may arise in the Directive on a minimum effective corporate tax rate.

Incorporation of future OECD clarifications and updates

As stated above, the inclusion in the Directive of the upcoming OECD Implementation Framework on administration, compliance, and safe harbor rules will be crucial for the functioning of the new tax system. Still, NSD notes that there is no reference in the Directive to the Safe Harbors (OECD 8.2) or Administrative Guidance (OECD 8.3). NSD requests clarifications as to how the content of these future rules will be incorporated into the Directive and domestic law in Sweden. In addition, it must be clarified how any changes to the rules needed to comply with the Implementation Framework will be incorporated into the Directive and domestic law.

Specific comments

Need for amendments

The following comments align with the remarks made by Business at OECD in their recent letter to the OECD (see footnote 2). As stated in the letter, these provisions are considered as fundamentally inconsistent with the policy objective of Pillar 2 or will lead to double taxation. We are aware that amendments in these provisions in the Directive may depend on the outcome of the discussion at the OECD.

Article 20.5 Top-up tax despite Net qualifying loss

Directive
Where, for a fiscal year, there is a net qualifying loss in a jurisdiction and the amount of adjusted covered taxes for that jurisdiction is negative and less than an amount equal to the net qualifying loss multiplied by the minimum tax rate (the "expected adjusted covered taxes"), the amount equal to the difference between the amount of adjusted covered taxes and the amount of expected adjusted covered taxes shall be treated as an additional top-up tax for that fiscal year. The amount of additional

[7] COUNCIL DIRECTIVE (EU) 2017/ 1852 - of 10 October 2017 - on tax dispute resolution mechanisms in the European Union (europa.eu).

topup tax shall be allocated to each constituent entity in the jurisdiction in accordance with Article 28(3).

OECD 4.1.5
In a Fiscal Year in which there is no Net GloBE Income for a jurisdiction, if the Adjusted Covered Taxes for a jurisdiction are less than zero and less than the Expected Adjusted Covered Taxes Amount the Constituent Entities in that jurisdiction shall be treated as having Additional Current Top-up Tax for the jurisdiction under Article 5.4 arising in the current Fiscal Year equal to the difference between these amounts. The Expected Adjusted Covered Taxes Amount is equal to the GloBE Income or Loss for a jurisdiction multiplied by the Minimum Rate.

Comments
This rule applies top-up tax in circumstances where there is no net qualifying income for a jurisdiction, and where adjusted covered taxes are negative and are less than the qualifying income or loss for that jurisdiction multiplied by the minimum rate. We believe this tax charge, when there is no income, is fundamentally inconsistent with the overall policy goals articulated in the preamble of the OECD Model Rules.

We understand that the policy concern sought to be addressed is that a permanent difference benefit (e.g., an additional tax deduction) should not result in additional GloBE attributes (e.g., a tax loss that can be carried forward) that may shelter undertaxed income. However, it seems contrary to the “minimum tax” concept to levy tax in a year when there is no income. We urge the Swedish Government to consider other alternatives to address this issue. These could involve either reducing the attribute generated so undue benefit would not be gained in future years, and/or applying Top-up Tax in the year in which the attribute of concern benefits the MNE. We firmly believe that the policy of Pillar 2 dictates that in a year where there is no economic profit, there should not be any Pillar 2 tax.

Another consequence of this article is to subject to Top-up Tax any permanent benefit that arises in a jurisdiction in a year in which there is a tax loss. This will occur, regardless of the materiality of that benefit relative to the profit or income in the jurisdiction, and regardless of whether that permanent difference will in fact have the effect of resulting in an ETR in the jurisdiction below the minimum tax rate.

Finally, the Top-up Tax is applied to an attribute when it arises with no regard given to whether that attribute is ever utilized or whether any economic

benefit is ever received by the MNE (for example, where the resulting tax loss is never utilized). Again, this seems inconsistent with the overall policy goals.

Article 21.2 Recasting deferred taxes at minimum rate

Directive
Where the domestic tax rate in a jurisdiction is above the minimum tax rate, the total deferred tax adjustment amount to be added to the adjusted covered taxes of a constituent entity for a fiscal year pursuant to point (b) of Article 20(1) shall be the deferred tax expense accrued in its financial accounts with respect to covered taxes recast at the minimum tax rate, subject to the adjustments under paragraphs 3 to 6.

OECD 4.4.1
The Total Deferred Tax Adjustment Amount for a Constituent Entity for the Fiscal Year is equal to the deferred tax expense accrued in its financial accounts if the applicable tax rate is below the Minimum Rate or, in any other case, such deferred tax expense recast at the Minimum Rate, with respect to Covered Taxes for the Fiscal Year subject to the adjustments set forth in Articles 4.4.2 and 4.4.3 and the following exclusions:

Comments
The requirement that deferred tax balances be recast at the minimum rate undermines the ability of the rules to achieve the policy objective of smoothing the ETR. Recasting deferred tax amounts at the minimum rate does not provide recognition of the actual rate of tax that will be borne in respect of the relevant underlying timing difference when looking at the annual ETR and will result in top-up tax both in respect of timing and permanent differences. This consequence will arise notwithstanding that the true ETR borne by the MNE over time is higher than the minimum rate. For example, top-up tax will arise in circumstances where tax losses or other temporary differences, e.g., non-deductible warranty provisions, are being reversed and there is a permanent difference, regardless of the materiality of that permanent difference or its impact on the ETR, and regardless of the level of tax paid by a MNE over time. The outcome of this is double taxation.

Article 24.1 Post-filing adjustments

Directive

Where a constituent entity records an adjustment to its covered taxes in its financial accounts for a previous fiscal year, such adjustment shall be treated as an adjustment to covered taxes in the fiscal year in which the adjustment is made, unless the adjustment relates to a fiscal year in which there is a decrease in covered taxes for the jurisdiction. Where there is a decrease in covered taxes that are included in the constituent entity's adjusted covered taxes for a previous fiscal year, the effective tax rate and top-up tax for such fiscal year shall be recomputed in accordance with Article 28(1) by reducing adjusted covered taxes by the amount of the decrease in covered taxes. The qualifying income for the fiscal year and any relevant fiscal years shall be adjusted accordingly.

OECD 4.6.1

An adjustment to a Constituent Entity's liability for Covered Taxes for a previous Fiscal Year recorded in the financial accounts shall be treated as an adjustment to Covered Taxes in the Fiscal Year in which the adjustment is made, unless the adjustment relates to a Fiscal Year in which there is a decrease in Covered Taxes for the jurisdiction. In the case of a decrease in Covered Taxes included in the Constituent Entity's Adjusted Covered Taxes for a previous Fiscal Year, the Effective Tax Rate and Top-up Tax for such Fiscal Year must be recalculated under Article 5.4.1. In the Article 5.4.1 recalculations, the Adjusted Covered Taxes determined for the Fiscal Year shall be reduced by the amount of the decrease in Covered Taxes and GloBE Income determined for the Fiscal Year and any intervening Fiscal Years shall be adjusted as necessary and appropriate.

Comments

The rules in Article 24.1 require the taxpayer to correct the previous fiscal year if there is a tax decrease, but it does not allow correction in case of an increase. This means that additional top-up tax can be levied, but a top-up tax paid can never be repaid.

This goes against the Swedish tax system, which generally requires that income and expenses are allocated to the fiscal year which they relate. The reassessment system allows/requires a taxpayer to correct a previous fiscal year six years after the year expired, regardless of if it is an upward or downward adjustment.

We request that the Swedish Government explore the possibilities of making the rules optional for the taxpayer as to what year upward adjustments are

taken into account to secure that those taxpayers get a refund of top-up tax in cases where the local tax is increased in a subsequent year.

By way of example, in most (if not all) bilateral tax cases (notably TP) there will be an upward adjustment in one jurisdiction and a downward adjustment in the other. If you are allowed to allocate the upward adjustment to the same year as the downward adjustment, you will reduce/eliminate the risk of unintended top-up tax due to differences in the timing of the upward and downward adjustment.

Also, it would eliminate the risk of double taxation in a case where the UPE has paid top-up tax due to an income which was treated as non-taxable in the local tax return, but which is later denied or adjusted.

When it comes to the wording *(see highlight in yellow above)*, the Directive deviates from the OECD model rules which leads to a different meaning. The Directive seems to indicate that an adjustment is recorded in the financial accounts for a previous fiscal year. An adjustment to the taxes in a previous fiscal year does not, however, change the financial statements of that year. Instead, it is reflected as a prior year adjustment in the financial statements of the year the adjustment is made. This is properly reflected in the OECD wording; ”An adjustment to a Constituent Entity's liability for Covered Taxes for a previous Fiscal Year recorded in the financial accounts shall be treated as an adjustment to Covered Taxes in the Fiscal Year in which the adjustment is made”.

Need for clarifications

The comments below refer to areas in the Directive where we request clarifications in order to provide greater certainty.

Article 15.1/19.1 Treatment of Pillar 1 tax / profits

Directive 15.1 Adjustment to determine the qualifying income or loss /19.1 Covered taxes

OECD 3.2.1 Adjustment to determine the qualifying income or loss /4.2.1 Covered taxes

Comments
There is no information in the directive whether Pillar 1 tax is a covered tax. Assuming that Pillar 1 tax, Amount A, shall be included as a covered tax, it is important to clarify that such a tax will be recorded in the company that has recorded the underlying income in its financial accounting net income or loss.

Article 15.8 Intra-Group Financing arrangement

The proposed text on Intra-Group Financing arrangement in Art 15.8 in the proposed directive is very different from the art. 3.2.7 in the OECD Model Rules. It should be in line with the OECD text or at least clarified, in order to reduce the risk of misinterpretation.

Article 21.7 – DTL recapture determination

Directive
A deferred tax liability that is not paid or reversed within the five subsequent fiscal years shall be recaptured to the extent it was taken into account in the total deferred tax adjustment amount of a constituent entity.

The amount of the recaptured deferred tax liability determined for the fiscal year shall be treated as a reduction to the covered tax of the fifth preceding fiscal year and the effective tax rate and top-up tax of such fiscal year shall be recomputed in accordance with Article 28(1).

OECD 4.4.4
To the extent a deferred tax liability, that is not a Recapture Exception Accrual, is taken into account under this Article and such amount is not paid within the five subsequent Fiscal Years, the amount must be recaptured pursuant to this article. The Amount of the Recaptured Deferred Tax Liability determined for the current Fiscal Year shall be treated as a reduction to Covered Taxes in the fifth preceding Fiscal Year and the Effective Tax Rate and Top-up Tax of such Fiscal Year shall be recalculated under the rules of Article 5.4.1. The Recaptured Deferred Tax Liability for the current Fiscal Year is the amount of the increase in a category of deferred tax liability that was included in the Total Deferred Tax Adjustment Amount in the fifth preceding Fiscal Year that has not reversed by the end of the last day of the current Fiscal Year, unless such amount relates to a Recapture Exception Accrual as set forth in Article 4.4.5.

Comments
We believe that an option to track DTLs by "category" is necessary as tracking by individual assets/liabilities may, depending on the type of asset/liability, not be possible in practice.

Additional guidance is also needed on how to determine whether a DTL has reversed within 5 years. The DTL-movement of a category between year 0 and year 5 by simply comparing the closing balance amounts on a DTL general ledger account level, will not appropriately indicate whether a DTL recorded in year 0 has actually reversed within the relevant timeframe.

The rules ought to recognize that movements in the underlying pool of assets/liabilities within a category should be considered when calculating the DTL subject to recapture. A potential approach could be to allow the taxpayer to prove, by movements in sub ledgers or in other ways, that a DTL related to an individual asset/liability or to a pool has reversed (even if the gross balance has increased).

Article 21.8 (a) – Recapture exception accruals (Tangible Assets)

According to paragraph 8 of article 21, certain items are excluded from the recapture mechanism stated in paragraph 7 of the same article. The underlying policy reason for these exceptions is that temporary differences related to these items are typically tied to substantive activities in a jurisdiction and/or are not prone to taxpayer manipulation. Accordingly, section (a) of the article excludes "cost recovery allowances on tangible assets".

From a tax perspective, tangible assets are commonly understood broadly to include physical assets with a finite monetary value that are not intangible assets. Hence, from a tax perspective, tangible assets include both current (e.g., Inventory and Stockpile) and non-current (e.g., Property, Plant and Equipment) physical assets.

From an accounting perspective, however, the term "tangible assets" could be interpreted as only applying to non-current assets. Although the IFRS accounting standards do not provide a clear definition of tangible assets, such a conclusion could be drawn from the structure of a balance sheet prepared under IFRS, whereby the term "tangible assets" is used only under the non-current asset category, even though there are assets also in the current asset category which are, in fact, tangible, such as inventory.

Given the intended policy outcome, it appears obvious that the term "tangible assets" in section (a) should be interpreted to include both current and non-current assets. A definition whereby only certain categories of tangible/physical assets would qualify would distort the applicability of the recapture accrual exception depending on the mix of physical assets used between different industries and business models. Hence, we would welcome that this is clarified by way of a definition in the directive which explicitly states that both current and non-current assets are covered.

Also, for insurance companies it is important that contingency reserves (säkerhetsreserven) get the same treatment as other insurance reserves and that should be made clear in the directive. Due to the insurance business model, insurance companies must make assumptions of the future. Contingency reserves are a legitimate way for insurance companies to cater for factors that are random or otherwise difficult to assess.

Article 26.1/42.5 (c) (i) administrative simplification

Directive Article 26 para 1 + para 5 Computation of the top-up tax / Article 42 para 5 (c) (i) the effective tax rate for each jurisdiction and the top-up tax of each constituent entity.

OECD 5.2.4 Top up tax 8.1.4 Filing obligation

Comments
For both calculation of top-up tax and filing obligation it ought to be clear that if the Ultimate Parent Entity is applying an IIR, all the top-up tax computed for the LTCEs is allocable to the UPE and therefore, as a practical matter, the UPE should not need to calculate nor file information relating to allocation of Top-Up tax of each LTCE.

Article 27.4 – substance based carve-out with respect to property held for lease

Article 27 provides a substance based carve-out which allows constituent entities to reduce its net GloBE income for the purpose of calculating the Top-up tax in relation to its eligible payroll costs and tangible assets. The

policy rationale for this carve-out is to exclude a fixed return from substantive activities within a jurisdiction from the application of the GloBE rules.

Paragraph 4 of the article makes an exemption for property, including land and building, that is held for sale, lease or investment. The reason for this is seemingly that a MNE should not be able to generate a larger carve-out by purchasing investment property in a jurisdiction.

Whilst this appears reasonable in principle, the paragraph fails to recognize situations where the property is held for lease (or rent) for the use in the commercial activities of another constituent entity in the same jurisdiction (which are fully owned within the same MNE). It is quite common that property used in the production or operation of a group is located into separate real estate entities or that one of the operating entities owns all property for all other constituent entities in a jurisdiction. As the rule is currently drafted, such property would not be accounted for when calculating the eligible carve-out even though the property is used for fully commercial activities within the same group. This seems to go against the intended policy outcome. Although the lessee may include the leased property under paragraph 1 (c) (iii), this requires that the property is accounted for in the books of the lessee, since reference is made in paragraph 4 to the carrying value of the eligible tangible assets. This would typically only be the case in a financial lease and not in a normal rental situation, where the economic ownership remains with the lessor, who accounts for the asset.

Another concern with the current drafting of the paragraph 4 of the article is that it does not appropriately consider the nature of a company's business activities. In many industries, leasing and rental to third parties is a significant part of the business model. By way of example, it is unclear why a real estate company which sole operation is to rent out property should not be able to utilize the substance based carve-out.

Equally, in many industries where the produced goods have a substantial value, the business include a customer finance activity which leases or rents out the products to customers as a way to finance the "acquisition". One example here is in the automotive industry.

For these reasons, we believe that paragraph 4 of the article should be amended to ensure that the exception of property held for sale, lease or investment should not apply where it is done for the benefit of the commercial activities of another constituent entity in the same jurisdiction. Likewise, the

paragraph should make clear that the exception does not apply where leasing or rent etc. is the core commercial activity of the constituent entity.

Definitions; covered taxes, tax credits etc.

In order to ensure a consistent implementation of the Directive throughout the various Member States it is vitally important that critical elements of the rules are clearly defined. Although Article 3 of the Directive proposal provides a number of definitions, we note that further clarification is needed, notably with respect to “covered taxes” and “tax credits”.

Covered Taxes, as further defined in Article 19, includes taxes imposed “In lieu of” generally applicable corporate income taxes. Although it can be assumed that withholding taxes would qualify for the “in lieu of” test, given the importance of clarity on this matter, we would recommend that this is expressly stated in para. 1(c) of the article (e.g. by stating that “*taxes imposed in lieu of generally applicable corporate income tax, such as withholding taxes levied on payments of interest or royalties…*”.

Article 21 para. 5 (e) stipulates that the total deferred tax adjustment amount shall not include the deferred tax expense with respect to *tax credits*. Whereas this appropriately address potential timing differences that may occur where e.g., a tax credit cannot be fully utilized one year due to local limitations (and thus is carried forward to a later year), the definition of what constitutes a tax credit for this purpose is not clear. Whereas one would assume that tax credits in this context refers to various kinds of incentives and not e.g., foreign tax credits, this ought to be clarified.

Presumed that the above understanding is correct, a potential definition of the term “tax credits” could be “*A tax credit is an amount related to a tax incentive that taxpayers can subtract directly from its taxes owed” with the potential further clarification that “A tax credit does not include tax credits available in a jurisdiction due to a tax liability imposed in another jurisdiction or imposed on profits distributed by another entity such as foreign tax credits and franking/imputation credits”.*

Furthermore, *Ultimate Parent Entity* is not defined in the Directive. We suggest including the definition as per OECD model rules Article 1.4.

Lack of definitions of *accounting terms*; the Directive should confirm that accounting terms used within GloBE have the meaning per commonly accepted accounting principles.

Deviations from the OECD model rules

We note that the Commission in the Directive has re-arranged and sometimes changed the wording of the OECD Model Rules, making a comparison between the two very cumbersome and time-consuming. Below we provide comments in relation to some provision where the Directive deviates from the OECD Model Rules. However, given the time-constraint we have not been able to make a complete analysis. Since this is a necessary step to verify the Directive's alignment with the OECD Model Rules, we urge the Swedish Government to make such an in-depth analysis before agreeing to sign the Directive.

"Long-term differences" vs "permanent differences"

Directive Article 14.2 (c)
(c) long-term differences in excess of EUR 1 000 000 that arise from the application of a particular principle or standard to items of income or expense or transactions, which differs from the financial standard used in the preparation of the consolidated financial statements of the ultimate parent entity, shall be adjusted to conform to the treatment required for that item under the accounting standard used in the preparation of the consolidated financial statements.

OECD 3.1.3:
(c) permanent differences in excess of EUR 1 million that arise from the application of a particular principle or standard to items of income or expense or transactions that differs from the financial standard used in the preparation of the Consolidated Financial Statements of the Ultimate Parent Entity are conformed to the treatment required under the accounting standard used in the Consolidated Financial Statements of the Ultimate Parent Entity.

Comments
The OECD uses the term "permanent differences", whereas the Directive proposal introduces its own non-defined term "long term differences".
IAS 12 defines temporary differences as follows:

Temporary differences are differences between the carrying amount of an asset or liability in the statement of financial position and its tax base.

Temporary differences may be either:

(a) taxable temporary differences, which are temporary differences that will result in taxable amounts in determining taxable profit (tax loss) of future periods when the carrying amount of the asset or liability is recovered or settled; or

(b) deductible temporary differences, which are temporary differences that will result in amounts that are deductible in determining taxable profit (tax loss) of future periods when the carrying amount of the asset or liability is recovered or settled.

Conversely, the term permanent differences is commonly used to describe a business transaction that is reported differently for financial and tax reporting purposes, and for which the difference will never be eliminated. The Directive term indicates that also temporary differences, which reverse over a "long term", should be included. To comply with the Model Rues, the Directive should be changed to "permanent".

Portfolio shareholding

Directive Article 15 (b) (i)

an ownership interest in an entity of less than 10% (a "portfolio shareholding") in respect of which a constituent entity is entitled to all or substantially all of the rights to profits, capital or reserves, irrespective of whether the constituent entity owns the legal ownership of such portfolio, for less than one year at the date of the distribution;

OECD page 64

Portfolio Shareholding means Ownership Interests in an Entity that are held by the MNE Group and that carry rights to less than 10% of the profits, capital, reserves, or voting rights of that Entity at the date of the distribution or disposition.

Comments

The definition of Portfolio shareholding in the Directive deviates from the OECD. This could generate different outcomes. The OECD refers to MNE Group ownership, whereas the Directive refers to a single entity ownership. In addition, there is no reference to voting rights in the directive.

Ultimate parent entity subject to deductible dividend regime

Directive Article 37.3 (c)
a governmental entity, an international organisation, a non-profit organisation or a pension fund other than a pension services entity that is tax resident in the jurisdiction where the ultimate parent entity is located and that holds ownership interests representing a right to 5 % or less of the profits and assets of the ultimate parent entity.

OECD 7.2.1 (c)
the dividend recipient is resident in the UPE Jurisdiction and is:

- *(i) a Governmental Entity,*
- *(ii) an International Organisation,*
- *(iii) a Non-profit Organisation or*
- *(iv) a Pension Fund that is not a Pension Services Entity.*

Comments
The wording in the Directive is more restrictive than in the OECD model rules and should consequently be amended.

Adjusted covered taxes

Directive Article 20.1
The adjusted covered taxes of a constituent entity for a fiscal year shall be determined by adjusting the sum of the tax expense accrued in its financial accounting net income or loss with respect to covered taxes for the fiscal year, by:

(a) the net amount of its additions and reductions to covered taxes for the fiscal year as set out in paragraphs 2 and 3;

(b) the total deferred tax adjustment amount as set out in Article 21; and

(c) any increase or decrease in covered taxes accrued in equity or other comprehensive income relating to amounts included in the computation of qualifying income or loss that will be subject to tax.

OECD 4.1.1
The Adjusted Covered Taxes of a Constituent Entity for the Fiscal Year shall be equal to the current tax expense accrued in its Financial Accounting Net Income or Loss with respect to Covered Taxes for the Fiscal Year adjusted by:

(a) the net amount of its Additions to Covered Taxes for the Fiscal Year (as determined under Article 4.1.2) and Reductions to Covered Taxes for the Fiscal Year (as determined under Article 4.1.3);

(b) the Total Deferred Tax Adjustment Amount (as determined under Article 4.4); and

(c) any increase or decrease in Covered Taxes recorded in equity or Other Comprehensive Income relating to amounts included in the computation of GloBE Income or Loss that will be subject to tax under local tax rules.

Comments
In order not to double count the deferred taxes, the starting point must be current tax expense as per the OECD Model Rules.

Concluding remark

NSD believes that the number of specific comments above, relating to the need for amendments and clarifications etc. of the rules, show the importance of not having the Directive signed before the OECD work on the Model Rules is completed and the outcome has been fully incorporated into the Directive.

Naturally, NSD stands ready to further discuss our comments or reply to any questions you might have.

NÄRINGSLIVETS SKATTEDELEGATION

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