UNITED STATES

Treasury Aiming for Research Credit Fix In Pillar 2 Guidance

by Stephanie Soong

The United States is working to protect the benefits of the research credit under pillar 2 global minimum tax, possibly through OECD administrative guidance, a top Treasury official said.

"We're trying to come up with a kind of a range of potential fixes," Scott Levine, acting Treasury deputy assistant secretary for international tax affairs, said March 19 at the Tax Executives Institute's midyear conference in Washington, adding that Treasury is open to speaking with stakeholders about the issue. "As far as our immediate goals, I think that we will ultimately try to get this fixed through administrative guidance, if possible, and if not, then we'll go to Plan B."

Pillar 2 is a key feature of a two-pillar global tax reform plan that was designed and agreed on by nearly all 145 of the member jurisdictions participating in the OECD inclusive framework on base erosion and profit shifting as a follow-up to action 1 of the BEPS project.

The OECD's global anti-base-erosion (GLOBE) model rules are the foundation of pillar 2 and were designed to ensure that large multinational enterprises are subject to an effective tax rate of 15 percent in all jurisdictions in which they operate. The GLOBE rules comprise the income inclusion rule and a measure many jurisdictions call the undertaxed profits rule. Countries can also adopt domestic minimum top-up taxes that are qualified as being in line with the GLOBE rules. The U.S. global intangible low-taxed income regime inspired the IIR, but it needs reforms to be considered a qualified IIR under the GLOBE rules.

Stakeholders have expressed concerns about the research credit, which is nonrefundable under the GLOBE rules and would lower an MNE's ETR for the purposes of determining its top-up tax liability, thereby leading to GLOBE tax liabilities. Treasury has raised the issue in inclusive framework negotiations, and other member jurisdictions have similar concerns with their incentives, according to Levine. Whatever solution the inclusive framework comes up with must have strict guardrails to ensure that it won't undermine pillar 2's goals, he added.

It's clear that protecting the research credit will require either an interpretation of the GLOBE model rules or a safe harbor, according to Michael Plowgian, former Treasury deputy assistant secretary for international tax affairs.

Plowgian also cautioned against using the distinction between refundable and nonrefundable tax credits to protect pillar 2's policy objectives. "What we've seen is some proposals in some jurisdictions to use refundable credits to try and circumvent the policies of pillar 2 by using refundable credits that are based on percentage of income," Plowgian said. The situation illustrates the dangers of using the distinction between refundable and nonrefundable tax credits as a way to police pillar 2's policy goals, he said. "I do think there is a possibility here for a broader policy conversation," he added.

Levine also said that negotiators working on further OECD pillar 2 administrative guidance are aiming to issue three more tranches of guidance in 2024, with the next round possibly released next month.

"There was hope that we [could] get something out in April, but it could slip a little," Levine said. He added that the process for countries to reach consensus on the guidance could take a while.

The OECD has already published three tranches of pillar 2 administrative guidance.

The next round of pillar 2 guidance will likely address GLOBE and accounting carrying value differences and the cross-border allocation of current and deferred taxes. "It's not final yet, so it could slip, but the hope is that that will be out sooner than later," Levine said.

Forthcoming pillar 2 administrative guidance is also likely to include hybrid anti-arbitrage and intercompany financing rules, Levine said, noting the long list of issues that still need to be addressed. There is also an issue related to employee stock ownership plans that is on the inclusive framework's radar, he added.

When asked about Treasury's March 11 green book and its proposed modifications to the GILTI regime to align with the GLOBE rules, Levine expressed optimism about the amendments. "I can say I'm quite confident, and we as the government [are] quite confident, that the modifications to GILTI as described in the green book will be a qualified IIR at the end of the day, so I don't lose too much sleep over that," he said. ■