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September 29, 2023

The Honourable Chrystia A. Freeland, P.C., M.P.
Deputy Prime Minister and Minister of Finance
Department of Finance Canada
90 Elgin Street
Ottawa, Ontario K1A 0G5
Canada

RE: Consultation on the Global Minimum Tax Act

Via email: Consultation-Legislation@fin.gc.ca

Dear Minister Freeland:

On behalf of the Tax Executives Institute, Inc. ("TEI"), I am pleased to share our comments on the draft legislative proposals ("the Draft Legislation") released on August 4, 2023, to implement the new Global Minimum Tax Act ("GMTA").

We understand that the Department of Finance took into consideration the guidelines published by the Organisation for Economic Co-operation and Development (the "OECD") with respect to its project on the digitalization of the economy, when developing the Draft Legislation. However, we also understand that these rules need to work within the current tax legislation in Canada, as represented by the Income Tax Act (the "Act"). We appreciate the opportunity to provide comments and would be pleased to discuss these comments with the Department of Finance ("the Department").

About TEI

TEI was founded in 1944 to serve the professional needs of in-house tax professionals. Today, the organization has 56 chapters across North and South America, Europe, and Asia, including four chapters in Canada. Our over 6,000 members represent 2,800 of the world's leading companies, many of which either are resident or do business in Canada. Over 15% of TEI's membership comprises tax professionals who work for Canadian businesses in a variety of industries across the country. The following comments and recommendations reflect the views of TEI as a whole but, more particularly, those of our Canadian membership.

TEI is dedicated to the development of sound tax policy, compliance with and uniform enforcement of tax laws, and minimization of administration and compliance costs to the mutual benefit of government and taxpayers. TEI is committed to fostering a tax system that works—one that is administrable and with which taxpayers can comply in a cost-efficient manner. The diversity, professional training, and global viewpoints of our members enable TEI to bring a balanced and practical perspective to the compliance issues discussed herein.

TEI Comments

The OECD introduced the concept of a minimum tax in its Pillar Two model rules following an agreement in October 2021 by 137 countries and jurisdictions under the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting. Since that time, the OECD has released administrative guidelines as well as commentary on the Global Anti-Base Erosion (GloBE) rules and a GloBE Information Return.

The rules define the scope and set out the mechanism for the GloBE rules under Pillar Two, introducing a global minimum corporate tax rate of 15%. The minimum tax will apply to multinational companies with revenue above EUR 750 million and is estimated to generate around USD 150 billion in additional global tax revenues annually.

The GloBE rules provide for a coordinated system of taxation intended to ensure large multinational groups pay this minimum level of tax on income arising in each of the jurisdictions in which they operate. The rules create a "top-up tax" to be applied on profits in any jurisdiction whenever the effective tax rate, determined on a jurisdictional basis, is below the minimum 15% rate.

Delay of Coming into Force Date

The IIR and the Qualifying Domestic Minimum Top-up Tax ("QDMTT") under the GMTA are proposed to apply to fiscal years of a qualifying Multinational Enterprise ("MNE") group that begin on or after December 31, 2023, with the UTPR to apply one year later. In our view, the coming into force date of the IIR and QDMTT under the GMTA should also be deferred by a year for several reasons.

First, to protect the competitiveness of Canadian based MNEs, Canada should not implement the GMTA before other key global economies. For example, it is highly unlikely the United States will adopt the OECD guidelines under Pillar Two into its domestic law, and certain elements of the U.S. federal government have threatened to apply retaliatory measures in respect of jurisdictions that apply UTPR rules to U.S. companies. Canadian businesses/MNEs could be severely affected by any such retaliatory measures as the United States remains Canada's main trading partner. Canada should also not implement the GMTA in advance of other key global economies, such as China and India. To protect the competitiveness of Canadian based MNEs, Canada should defer the implementation of the GMTA until such other major economies have already done the same. Adopting such an approach would also allow Canada to monitor any problems and issues facing any "early-adopters," and ideally address such issues prior to implementation in Canada.

Second, the GMTA, being a stand-alone legislative act that introduces a global minimum tax ("GMT"), has yet to be synchronized with the Act and its Regulations. The integration between these two distinct tax statutes is extremely important – and to date no amendments (in draft form or otherwise) have been announced to assist with integration. As a result, MNE groups will likely face taxation well above the intended 15% minimum tax rate because of the GMTA. For example, double taxation could arise where a Canadian company is taxed under the GMTA in respect of income of a foreign affiliate and is then taxed again in Canada (i) when the earnings of the foreign affiliate are distributed to Canada, or (ii) when the Canadian company sells shares of the foreign affiliate. These issues are particularly relevant for Canada as most of the other countries that have agreed to adopt Pillar Two in 2024 have a much more generous "participation exemption" regime that will generally prevent such double taxation from arising. Canadian based MNE groups will need to account for such double taxation in their financial statements – creating a competitive disadvantage relative to MNE groups outside of Canada.

Third, the GMTA is a complicated new set of rules that will have a broad impact on Canadian companies (including the potential for increased taxes in respect of Canadian operations through the QDMTT). Rather than rushing this legislation through Parliament, Canada should ensure that the legislation does not inadvertently create a negative impact on Canada. In particular, further review and study should confirm whether the QDMTT will inadvertently negate the intended policy effects of various government incentives (such as Canada's investment and Scientific Research & Experimental Development tax credits), including whether any modifications to those incentive regimes may be warranted to best comply with Pillar Two.

Finally, the Inclusive Framework on BEPS has yet to finalize all rules and guidance on the GMT that Canada will follow with respect to the GMTA. Moreover, the GMTA omits various key definitions from the OECD model rules and does not consider all of the administrative guidance that the Inclusive Framework on BEPS has released to date. It is doubtful that all of these important amendments can be made to the GMTA sufficiently in advance of the coming into force date. Also, the GMTA has delegated to the Inclusive Framework on BEPS the ability to decide which regimes qualify for a safe harbor exemption. It will be important for the Inclusive Framework to have designated its list of qualifying regimes prior to the GMTA coming into force.

Deferred Tax Calculations Not Expensed in the Financial Statements

Background

As provided by the OECD, a QDMTT is defined as a minimum tax included in the domestic law of a jurisdiction and that:

1. Determines the Excess Profits of the Constituent Entities located in the jurisdiction (domestic Excess Profits) in a manner that is equivalent to the GloBE Rules;
2. Operates to increase a domestic tax liability with respect to domestic Excess Profits to the Minimum Rate for the jurisdiction and Constituent Entities for a Fiscal Year; and

3. Is implemented and administered in a way that is consistent with the outcomes provided for under the GloBE Rules and the Commentary, provided that such jurisdiction does not provide any benefits that are related to such rules.[1]

Part IV of the GMTA governs the calculation of a Domestic Minimum Top-up Tax ("DMTT"). In subsection 50(1), the references to the calculation of the top-up tax essentially require a top-up tax where the effective tax rate ("ETR") of an entity is less than 15%. In calculating the ETR in Subdivision A of Division D of Part II, "Adjusted Covered Taxes" (as defined in section 22 of Subdivision A of Division C of Part II) includes current tax expense in the financial accounts, adjusted by certain additions and reductions to covered taxes in paragraph 22(1)(a) and, also, for:

> (b) the total deferred tax adjustment amount of the constituent entity for the year, unless paragraph 26(b) or (c) applies in respect of the year and the jurisdiction in which the constituent entity is located; and
>
> (c) each amount recorded in the equity or other comprehensive income of the constituent entity for the year that can reasonably be considered to relate to an increase or decrease in respect of covered taxes, if
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> > (i) the covered taxes are in respect of an amount (referred to in this paragraph as the "included amount") included in the constituent entity's GloBE income or loss for the fiscal year, and
> >
> > (ii) the included amount is subject to tax under the laws of the jurisdiction in which the constituent entity is located.

The "Deferred Tax Adjustment Amount" is defined in subsection 25(1) in Subdivision C of Division C of Part II as the deferred tax expense in respect of covered taxes, adjusted for certain items.

Issue

Regulated businesses that prepare their financial statements in accordance with U.S. GAAP are required to follow Accounting Standards Codification ("ASC") 980 "Regulated Operations." The purpose of ASC 980 is to ensure that the financial statements recognize the economic effects of the actions of the regulator, and results in the timing of recognition of certain revenues and expenses in these operations and the presentation of certain assets and liabilities that may differ from what is otherwise expected under IFRS, or U.S. GAAP for non-rate-regulated entities.

Under ASC 980, "Regulatory Assets" represent amounts that are expected to be recovered from customers in future periods through rates and "Regulatory Liabilities" represent amounts that are expected to be refunded to customers in future periods through rates or to be paid to cover future

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[1] OECD (2021), *Tax Challenges Arising from Digitalisation of the Economy – Global Anti-Base Erosion Model Rules (Pillar Two): Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris,* https://doi.org/10.1787/782bac33-en.

abandonment cost in relation to the Canada Energy Regulator's Land Matters Consultation Initiative ("LMCI") for future removal and site restoration costs as approved by the OEB. Deferred tax expenses related to regulatory assets and liabilities are required under ASC 980 to be recorded as an offset to the regulatory asset/liability rather than in deferred tax expense on the income statement. The mechanics of this are that deferred income tax expense is recorded on the income statement, and then a second accounting entry is made to reclassify this amount to the balance sheet as a regulatory asset, resulting in no deferred tax expense on the income statement.

The types of adjustments to deferred tax expense made under ASC 980 are not expressly discussed in the draft GMTA legislation or OECD commentary. It is contemplated in paragraph 22(1)(c) of the draft GMTA legislation that amounts included in equity or other comprehensive income ("OCI") that relate to covered taxes on income that is included in GloBE income should be included in the calculation of the ETR, but there is no discussion regarding taxes that are recorded in other balance sheet accounts. We believe that, based on OECD guidance, it is intended that deferred taxes recorded in balance sheet accounts should be included in the "Total Deferred Tax Adjustment Amount" as defined in GMTA subsection 25(1) and as a result make up part of "Adjusted Covered Taxes" as defined in GMTA subsection 22(1).

Excluding certain temporary differences from the Total Deferred Tax Adjustment Amount simply because GAAP requires them to be recorded on the balance sheet rather than through deferred tax expense seems inconsistent with the OECD guidance.

There is another view with respect to these types of deferred tax amounts that are recorded in balance sheet accounts. These amounts may already be included in the "Adjusted Covered Taxes" because of the "Total Deferred Tax Adjustment Amount" in section 25 of the GMTA based on the interpretation of the legislation as currently written. There are two possible interpretations that could result in this conclusion:

1. Subsection 25(1) of the GMTA determines the "Total Deferred Tax Adjustment Amount" by a formula which includes the deferred tax expense of an entity, adjusted to 15%. Subsection 25(2) of the GMTA states that, for determining the amount of deferred tax expense under subsection 25(1), any portion of deferred tax expense that is in respect of "an item that is not included in computing GloBE income or loss" is to be excluded. As the adjustment to reclassify the deferred tax expense to the balance sheet for ASC 980 does not relate to an item included in computing GloBE income or loss, the adjustment should be excluded when determining the Total Deferred Tax Adjustment Amount. Therefore, the initial deferred tax expense that would have been recorded in the income statement (i.e., before any adjustment under ASC 980) would be the amount included in the calculation of the ETR.

2. Component A of subsection 25(1) includes the language "deferred tax expense in respect of taxes, accrued in its financial accounts for the year" in the "Total Deferred Tax Adjusted Amount." As the deferred tax expense on regulated assets and liabilities is

> accrued in the financial accounts of a taxpayer, the fact that it is reclassified to a balance sheet account should not impact its inclusion in the "Total Deferred Tax Adjusted Amount".

In both interpretations above, the impact of rate regulated accounting under ASC 980 should not impact the ETR calculation.

Clarification of the treatment of accounting adjustments made under ASC 980 is critical to entities in rate regulated industries. If deferred tax recorded on the balance sheet under these accounting rules is not included in deferred tax expense for purposes of determining Adjusted Covered Taxes, this could result in situations where the ETR of rate regulated entities is below 15%, and the DMTT could apply, resulting in an unfair tax burden. This would be an unexpected result and would not be consistent with the OECD's underlying policy intentions as explained in its commentary. It would result in an inequitable treatment of taxpayers who report under U.S. GAAP because the same entity reporting under IFRS would not have the issue.

For all the reasons set out herein, we kindly request that the Minister provide clarity on how adjustments to deferred tax under ASC 980 should be treated under the GMTA by amending the draft legislation to specifically address deferred tax expense booked to balance sheet accounts.

Domestic Top-up Amount – Subsection 50(1)

TEI welcomes the relief provided by the Permanent and Transitional Safe Harbors. Pursuant to paragraphs 50(1)(b) and (c) of the GMTA:

> (b) the total amount of tax payable for any fiscal year in respect of constituent entities of the MNE group located in Canada, under a qualified domestic minimum top-up tax, were deemed to be nil; and
>
> (c) any election made or removed under Part II of this Act or the equivalent law of another jurisdiction were taken into account, if the election is included in a [GIR] that has been received by the Minister in respect of the MNE group and would affect the calculation of top-up tax amounts (or results relevant to the determination of top-up amounts) for the fiscal year

To eliminate the administrative and filing burden on Canadian constituent entities, we propose to exclude the requirement for the GIR to be received by the Minister if an Ultimate Parent Entity ("UPE") or a Designated Filing Entity is located in a jurisdiction that has a Qualified Competent Authority Agreement in effect. Canada signed the Multilateral Competent Authority Agreement on the Automatic Exchange of Financial Account Information (the "MCA") in September 2018. If a UPE or a Designated Filing Entity is located in a jurisdiction that is a signatory to the MCA and files the GIR in that jurisdiction, then Canada can obtain relevant elections, included in the GIR, related only to Canadian constituent entities. Information with respect to constituent entities located in jurisdictions other than Canada is not required for the purposes of determination of the DMTT under the GMTA.

The GIR should be submitted to the Minister only if a Constituent entity that files the GIR is located in a jurisdiction that has not signed the MCA.

GIR Notification Requirement – Subsection 59(3)

Subsection 59(3) of the GMTA states:

> If there is a qualifying foreign filing entity of a qualifying MNE group for a fiscal year that is filing the GIR in respect of the MNE group for the fiscal year with the tax authority of the jurisdiction where it is located, a constituent entity of the MNE group located in Canada must notify the Minister in prescribed form and manner, on or before the GIR due-date for the fiscal year, of
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> (a) The identity of the qualifying foreign filing entity; and
>
> (b) The jurisdiction in which the qualifying foreign entity is located.

If more than one constituent entity located in Canada, in respect of the same MNE group, is required to notify the Minister, the MNE group can appoint a Canadian entity to notify the Minister on behalf of all Canadian entities. We welcome this simplified form of designation of the Canadian entity that must notify the Minister.

Furthermore, the GIR notification requirement for Canada can be eliminated mirroring the country-by-country ("CbC") reporting in Canada where there is no obligation for the UPE or the surrogate parent entity of the MNE group or a constituent entity resident in Canada to notify the CRA, in advance of the filing of the CbC report, of the name and jurisdiction of tax residence of the reporting entity.

Part IV Return – Subsection 60(2)

Subsection 60(2) of the GMTA provides that:

> A person that is liable to pay tax under Party IV for a fiscal year must file in prescribed manner with the Minister, not later than the GIR due-date, a return for the fiscal year in prescribed form containing an estimate of the tax payable under Part IV by it for the year.

To simplify compliance and avoid duplicative returns, instead of the requirement to file a return in a prescribed form for the year in Canada for DMTT, we suggest adopting a single filing system or technology, where the GIR return is filed by the UPE in the UPE jurisdiction.

There is no provision in the draft GMTA regarding how a taxpayer would amend the proposed GIR or Part IV return (i.e., DMTT return). Further guidance would be welcomed as part of the GloBE Implementation Framework regarding amendments to the GloBE information return, including the time frame and the method for the filing and exchange of information between Competent Authorities.

Refund – Payment in Error – Subsection 74(1)

Subsection 74(1) of the GMTA states:

> If a person, otherwise than because of an assessment, has paid any moneys in error to His Majesty in right of Canada, whether by reason or mistake of fact or law or otherwise, and the moneys have been taken into account by His Majesty in right of Canada as taxes, penalties, interest or other amounts under this Act, then an amount equal to the amount of the moneys must, subject to this Act, be refunded to the person if the person applies for the refund of the amount within two years after the day on which the moneys were paid.

The requirement to apply for the refund and time limitation within two years after the payment is an unnecessary, onerous provision for taxpayers and limits their ability to receive a refund of payments made in error. There is no such provision in the GloBE Rules, Commentary or the February and July administrative guidance. In addition, the Act has no such requirement to apply for the refund of payment in error within two years after the payment. Therefore, we suggest that this paragraph be amended or deleted.

Failure to File a GIR – Subsection 97(1)

The proposed penalties in subsection 97(1) are significant, including up to $1 million for failing to timely file the requisite GloBE information return or for providing a notification to the Minister. We recommend reducing the proposed penalties and align them with penalties applicable to the filing of a country-by-country report in Canada, where the penalty is equal to $25 per day of default, subject to a $100 minimum and a $2,500 maximum.

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TEI appreciates the opportunity to share our feedback at this important stage and looks forward to engaging in meaningful, substantive consultations with the Department and Canada Revenue Agency ("CRA") officials as they continue to contemplate the implementation of Pillar Two in Canada. TEI members stand ready to assist the Department and CRA in their efforts to strike the appropriate balance between administrability and fiscal policy in furtherance of the government's overall policy aims. We look forward to further discussing our comments with you.

Should you have any questions about TEI's submission, please do not hesitate to contact Steve Saunders, Chair of TEI's Canadian Income Tax Committee, at 403-801-4657 or steve.saunders@atco.com, or Benjamin R. Shreck of TEI's legal staff at bshreck@tei.org or 202.464.8353.

Respectfully submitted,

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