



ATOZ ALERT

Pillar Two: The OECD grants Luxembourg the transitional qualified status and releases new guidance on deferred tax assets and the GloBE Information Return

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Introduction

On 15 January 2025, the Inclusive Framework (“IF”) on Base Erosion and Profit Shifting (“BEPS”) of the Organisation for Economic Co-operation and Development (“OECD”) published the list of countries that have already implemented the Global Anti-Base Erosion Model Rules (“GloBE Model Rules”) introducing a global minimum level of taxation for multinational enterprise (“MNE”) groups and large-scale domestic groups. The list details the jurisdictions whose legislation is considered to comply with the OECD framework. Luxembourg is on that list.

In addition, the OECD released new guidance addressing the treatment of certain deferred tax assets (“DTAs”) that arose prior to the application of the global minimum tax under the GloBE Model Rules as a result of certain governmental arrangements or following the introduction of a new corporate income tax. It also published updates to the GloBE Information Return (“GIR”) released by the IF in July 2023 to facilitate compliance with and administration of the GloBE Model Rules.

Qualified status for Luxembourg Pillar Two rules

Why does it matter?

The effectiveness of the global minimum tax under the GloBE Model Rules results from the combination of three types of provisions that apply in accordance with the following order:

1. the Qualified Domestic Minimum Top-up Tax (“QDMTT”) which applies first, at the level of source jurisdiction, in respect of any low-taxed profits arising in that jurisdiction,
2. the Qualified Income Inclusion Rule (“IIR”) which applies in respect of remaining low-taxed profits.
 - a. The IIR is applied first at the level of the Ultimate Parent Entity (“UPE”) of the MNE Group and then shifts to the next Intermediate Parent Entity (“IPE”) in the ownership chain in line with a top-down approach,
3. the Under Taxed Payment Rule (“UTPR”) which works as a backstop rule and applies at the level of any Constituent Entity within the MNE Group, to the extent low-taxed profits are not subject to a Qualified IIR.

Recognition of qualified status is thus important for determining the order in which global minimum tax rules apply, i.e. to ensure coordinated outcomes and provide tax certainty for MNE Groups. To achieve this, the GloBE Model Rules establish a qualification system to ensure that the legislation of jurisdictions implementing the global minimum tax aligns with the GloBE Model Rules.

Since it is not feasible to complete a comprehensive legislative review for each jurisdiction implementing IIR and/or DMTT legislation effective from 2024 in the short term, the IF has introduced a simplified procedure for an initial transitional qualification mechanism that relies on a self-certification process. This transitional qualification mechanism acknowledges that national legislation aligns with the key provisions of the GloBE Model Rules. It aims to help tax authorities and other stakeholders determine whether a jurisdiction has implemented a QDMTT, a Qualified IIR, or qualifies for safe harbours like the Transitional country-by-country reporting (“CbCR”) Safe Harbour and the QDMTT Safe Harbour.

While the full legislative qualification process and ongoing monitoring process are still being developed by the IF, Luxembourg has recently completed the transitional qualification mechanism process for the IIR, DMTT or QDMTT Safe Harbour.

This means that the amended law of 22 December 2023, as further amended by the law of 20 December 2024 (the “**Pillar Two Law**”), which implements the EU Directive of 15 December 2022 on ensuring a global minimum level of taxation for MNEs, will be considered as qualified as from the effective date of the legislation. This effective date is when the legislation becomes applicable to in-scope taxpayers, specifically on 31 December 2023, the date on or after which the first covered fiscal year of an in-scope MNE Group begins. This enhances predictability and legal certainty for business groups operating in Luxembourg.

Indeed, the IIR and the QDMTT introduced by the Pillar Two Law should be recognized as qualified, on a transitional basis, by other jurisdictions applying the GloBE Model Rules. Additionally, the confirmation that Luxembourg can also benefit from the QDMTT Safe Harbour eases things for MNE groups established in Luxembourg. This allows these groups to perform the necessary QDMTT calculations solely at Luxembourg level, without needing to repeat them in the jurisdiction of the UPE, e.g. for IIR purposes.

What's Next?

A full legislative review and ongoing monitoring process will be developed to ensure that rules are applied and administered in line with the GloBE Model Rules.

If the full legislative review is not started within the agreed timeframe or concludes that the domestic regulations such as the Pillar Two Law, as amended or revised, do not qualify, the transitional qualified status may be revoked. However, the loss of this status will not be applied retroactively.

To prevent uncoordinated outcomes, if an MNE Group is subject to legislation that loses its qualified status during a Fiscal Year, it will still be treated as subject to qualified rules for the Reporting Fiscal Year that began before the transitional qualified status expires or is revoked.

For example, if a jurisdiction’s transitional qualified status expires on 31 December 2026, an MNE Group with a Reporting Fiscal Year starting on 1 April would still be considered as being subject to qualified rules for that jurisdiction for its Reporting Fiscal Year that began on 1 April 2026 and ended on 31 March 2027.

New OECD guidance on deferred tax assets

The GloBE Model Rules outline transition rules to prevent distortions when a Constituent Entity of a MNE Group enters the GloBE regime. On 15 January 2025, the OECD released new administrative guidance on the treatment of certain DTAs that arose before the global minimum tax was applied, due to certain governmental arrangements or the introduction of a new corporate income tax, and are excluded under these transition rules.

Background

The general transition rule allows an MNE Group to incorporate DTAs in the GloBE calculation at the beginning of the first year they are subject to the GloBE Model Rules (the "Transition Year"). These DTAs or deferred tax liabilities ("DTLs") must be measured at the lower of the minimum rate of 15% or the applicable domestic tax rate and must be reflected or disclosed in the financial accounts of the Constituent Entities.

The GloBE Model Rules deal specifically with DTAs arising from tax benefits provided by General Government (i.e., the central administration, agencies whose operations are under its effective control, state and local governments and their administrations).

After 30 November 2021, some MNE Groups have entered into arrangements with General Governments that provided tax benefits such as tax credits or step-ups in the tax basis before the GloBE Model Rules or a DMTT come into effect in their jurisdiction. Some MNE Groups have recorded these benefits as DTAs in their financial accounts and may plan to take them into account under the transition rules for DTAs and DTLs.

However, transition rules are not meant to be used by MNE Groups or General Governments to engage in transactions or provide tax attributes that create DTAs, which, when reversed, would shelter future low-taxed income from the GloBE Model Rules. Therefore, the transition rules include specific exclusions or limitations to prevent outcomes that do not align with the policy objectives. This is particularly relevant for events occurring after 30 November 2021. These rules do not have retroactive tax implications but outline how certain tax attributes are considered in fiscal years to which the GloBE Model Rules apply.

Clarification provided in the new administrative guidance

The new administrative guidance clarifies that deferred tax expenses resulting from the reversal of DTAs due to governmental arrangements, as well as DTAs and DTLs arising from similar events like retroactive elections or General Governments granting MNE Groups a step-up in basis when introducing a new corporate income tax regime before the GloBE Model Rules come into effect, but after 30 November 2021, are excluded under the transition rules. This limits the recognition of certain tax benefits granted to taxpayers after 30 November 2021 for GloBE purposes.

Nevertheless, according to the new administrative guidance, a jurisdiction that has implemented the GloBE Model Rules must ensure its domestic law is implemented and administered in a way that is consistent with the outcomes specified under the GloBE Model Rules and its commentaries. Therefore, if a jurisdiction's General Government has provided such benefits, its legislation would not obtain the qualified status under the transitional qualification mechanism.

Given that Luxembourg has obtained the qualified status under the transitional qualification mechanism, we can infer that its General Government did not engage in transactions or provide tax attributes that create DTAs, which, when reversed, would shield future low-taxed income from the GloBE Model Rules. Consequently, Luxembourg entities should not be impacted by the exclusion clarified in the new administrative guidance.

Updates to the GloBE Information Return

The IF has updated the GIR to simplify and clarify its use. The revised GIR includes detailed instructions on how to complete it, incorporate the administrative guidance released in December 2023 and June 2024, provides a template for notifying jurisdictions that they will receive the GIR through exchange of information and addresses situations where no jurisdictions have taxing rights under the GloBE Model Rules.

The obligation to prepare a GIR is distinct from the requirement to declare and pay taxes under a domestic (Luxembourg) tax return. The GloBE Model Rules allow each jurisdiction to determine its own tax return filing and payment obligations, which are generally expected to align with the existing tax filing and payment procedures in that jurisdiction.

Do you have any questions?



ANDREAS MEDLER

Partner,
International & Corporate Tax
andreas.medler@atoz.lu
T +352 26 940 237