

Computation of GloBE Income or Loss

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Source: OECD (2022), *Tax Challenges Arising from the Digitalisation of the Economy – Commentary to the Global Anti-Base Erosion Model Rules (Pillar Two)*, OECD, Paris, <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>, OECD (2022), *Tax Challenges Arising from the Digitalisation of the Economy – Global Anti-Base Erosion Model Rules (Pillar Two) Examples*, OECD, Paris, <https://www.oecd.org/tax/beps/tax-challenges-arising-from-the-digitalisationof-the-economy-global-anti-base-erosion-model-rules-pillar-two-examples.pdf>

Chapter 3

Article	Description
Article 3.1	Financial Accounting Net Income or Loss of the Constituent Entity
Article 3.2	Adjustments to be made for differences between financial accounting and taxable income to determine GLoBE Income or Loss
Article 3.3	Specific exclusion for International Shipping Income and Qualified Ancillary International Shipping Income
Article 3.4	Allocation of income/ loss between a Main Entity* and a Permanent Establishment
Article 3.5	Allocation of income derived from a Flow-through Entity to other Constituent Entities

** In Article 10.1.1, main Entity is defined as the Entity that includes the Financial Accounting Net Income or Loss of the Permanent Establishment in its financial statements*

Article 3.1

Financial Accounting Net Income or Loss of the Constituent Entity calculated in accordance with the rules

Sub-article	Description
Article 3.1.1	Computation of GloBE Income/Loss begins with the Financial Accounting Net Income or Loss of the Constituent Entity and then adjustments in Article 3.2 to Article 3.5 are carried out
Article 3.1.2	Net income/ loss determined for all constituent entity in preparing Consolidated Financial statement of the UPE and taking into consideration following points: <ul style="list-style-type: none">- Consolidation adjustments for intra-group transactions is not to be eliminated- Income or expenses attributable to purchase accounting for an acquired business when taken in account at consolidated level is not to be taken into account at constituent entity level- A Constituent Entity may not take into account ‘push down’ adjustments to the carrying value of assets and liabilities attributable to the purchase of a business if the acquisition date is on or after 1 December 2021- The net income or loss of the Constituent Entity has to be determined using the accounting standard that was used to determine the Constituent Entity’s income or loss in preparing the Consolidated Financial Statements <Deviations allowed in certain cases>- Items of Other Comprehensive Income from the Consolidated Financial Statements are generally excluded from the computation of GloBE Income or Loss – exception: 3.2.1(d)
Article 3.1.3	Addresses situation where the Constituent Entity maintains its entity level financial accounts using an accounting standard that is different from the standard used in the preparation of the UPE’s Consolidated Financial Statements. Different accounting standards can be used subject to the following conditions: <ul style="list-style-type: none">- the information in the financial accounts maintained according to the other accounting standard is reliable- the use of the other accounting standard must not result in permanent differences in excess of EUR 1 million from the financial accounting standard of the UPE

Article 3.2

Adjustments to be made for differences between financial accounting and taxable income

Sub-article	Description
Article 3.2.1	Set out nine adjustments to the Financial Accounting Net Income or Loss that are required in the computation of each Constituent Entity's GloBE Income or Loss <discussed in later slides in detail>
Article 3.2.2	Stock-based Compensation – <ul style="list-style-type: none">- Provides for an option of election to substitute in the computation of GloBE Income or Loss the amount of stock-based compensation allowed as a deduction in the computation of a Constituent Entity's taxable income in place of the amount expended in its financial accounts.- If the election is made in respect of an option that expires without exercise, the Constituent Entity must treat the amount previously included as an expense in the computation of the GloBE Income or Loss pursuant to the election as additional income under the GloBE Rules.- Election is a Five-Year Election and must be applied consistently and is made on jurisdictional basis
Article 3.2.3	Arm's length requirement for cross-border transactions. Issues covered: <ul style="list-style-type: none">- When transaction are not recorded in same amount in financial accounts of both Constituent Entities- When transaction not consistent with Arm's Length Principle Certain differences may arise because of transfer price audit adjustment. Arm's length requirement for same-country transactions: where the sale or other transfer of an asset produces a loss and that loss is taken into account in the computation of GloBE Income or Loss

Article 3.2

Adjustments to be made for differences between financial accounting and taxable income

Sub-article	Description
Article 3.2.4	Qualified Refundable Tax Credits <ul style="list-style-type: none">- shall be treated as income in the computation of GloBE Income or Loss of a Constituent Entity- May tantamount to reflect feature similar to government grants
Article 3.2.5	Election to use realisation method in lieu of fair value accounting – <ul style="list-style-type: none">- Constituent Entity must exclude fair value or impairment gain or loss in respect of assets or liabilities subject to the election from the computation of GloBE Income or Loss and must include gain or loss determined under the realisation method- Five-year election – If election is revoked, in the year of revocation the GloBE Income or Loss is adjusted by the difference between the fair value of the asset or liability at the beginning of the year and the carrying value of the asset or liability determined pursuant to the election
Article 3.2.6	Election to spread capital gains over five years – <ul style="list-style-type: none">- Permits an MNE Group to spread the effect of gains and losses from the sale of Local Tangible Assets over a period of up to five years
Article 3.2.7	Special Rule for Intragroup Financing Arrangements – <ul style="list-style-type: none">- Treatment for Intragroup Financing Arrangements that increases the amount of expenses taken into account in computing the GloBE Income or Loss of a Low-Tax Entity without corresponding increase to the taxable income of the High-Tax Counterparty to such arrangement

Article 3.2

Financial Accounting Net Income or Loss of the Constituent Entity calculated in accordance with the rules

Article 3.2.8	Election to consolidate transactions in same jurisdiction – - permits consolidated accounting treatment between Constituent Entities of the same MNE Group located in the same jurisdiction
Article 3.2.9	Exclusion of certain insurance company income – - Excludes cases where Insurance companies are subject to current tax on returns that must be contractually paid over to policyholders. These taxes are passed to the policyholders through a charge.
Article 3.2.10	Additional Tier One Capital – - Generally treated as equity for financial accounting purposes. However, these are treated as debt for tax purposes in some Inclusive Framework jurisdictions. Thus, for many Constituent Entities, payments in respect of Additional Tier One Capital are deductible as interest expense by the issuer and includible as interest income of the holder for tax purposes
Article 3.2.11	Adjustments to a Constituent Entity's Financial Accounting Net Income or Loss where necessary to reflect the requirements of Chapters 6 and 7 Chapter 6: corporate restructurings and holding structures Chapter 7: tax neutrality and distribution regimes For example, if a Constituent Entity is required to use the historical carrying value of an asset pursuant to Article 6.2 and it used the fair value of that asset to compute its depreciation expense for the Fiscal Year, it must adjust the depreciation expense to the amount that would have been computed using the historical carrying value of the asset

ARTICLE 3.2.1: ADJUSTMENTS

Para a: Net Taxes Expense

- (a) any Covered Taxes accrued **as an expense** and any current and deferred Covered Taxes **included in the income tax expense**, including Covered Taxes on income that is excluded from the GloBE Income or Loss computation
- (b) any deferred tax asset attributable to a loss for the Fiscal Year (would reduce the Net taxes)
- (c) any Qualified Domestic Minimum Top-up Tax accrued as an expense
- (d) any taxes arising pursuant to the GloBE rules accrued as an expense
- (e) any Disqualified Refundable Imputation Credit accrued as an expense

Para b: (Subtract) Excluded dividends, except for:

- (a) a Short-term Portfolio Shareholding and
- (b) an Ownership Interest in an Investment Entity that is subject to an election under Article 7.6

Para c: Excluded Equity Gains or Losses (Gain subtracted/ Losses added back)

- (a) gains and losses from **changes in fair value** of an **Ownership Interest**, except for a **Portfolio Shareholding** - Excluded fair value gains require a negative adjustment and excluded fair value losses require a positive adjustment to the Financial Accounting Net Income or Loss
- (b) **profit or loss in respect of an Ownership Interest included under the equity method of accounting** - Equity method net income is a negative adjustment to the Financial Accounting Net Income or Loss. An equity method loss is a positive adjustment to the Financial Accounting Net Income or Loss
- (c) gains and losses from **disposition** of an **Ownership Interest**, except for a disposition of a **Portfolio Shareholding**

ARTICLE 3.2.1: ADJUSTMENTS

Para d: Included Revaluation Method Gain or Loss

- Any revaluation losses or subsequent incremental increase in depreciation are allowed in the computation of GloBE Income or Loss to the extent they are attributable to revaluation increases (gains) included in the computation of GloBE Income or Loss pursuant to Article 3.2.1(d).

Para e: Gain or loss from disposition of assets and liabilities excluded under Article 6.3

- **Disposing Constituent Entity** excludes such gain or loss from its computation of GloBE Income or Loss - **Acquiring Constituent Entity** inherits carrying values of disposing Constituent Entity

Para f: Asymmetric Foreign Currency Gains or Losses <<Discussed in examples>>

These are generally foreign currency exchange gains or losses that arise due to differences between the functional currency for accounting purposes and the one used for local tax purposes

ARTICLE 3.2.1: ADJUSTMENTS

Para g: Add: Policy Disallowed Expenses -

- Covers expenses accrued by the Constituent Entity for **illegal payments, including bribes and kickbacks** and expenses accrued by the Constituent Entity for **finances and penalties** that equal or exceed EUR 50,000

Para h: Prior Period Errors and Changes in Accounting Principles

- **If change in opening equity is positive:** that amount should be **added** to profit or loss - **if change in opening equity is negative:** that amount should be **deducted** from profit or loss

- Does not apply to an error correction that requires a corresponding decrease in Covered Taxes in a previous Fiscal Year of EUR 1000000 or more. Such error corrections are subject to the rules of Article 4.6.1.

Para i: Accrued Pension Expense: Pension liabilities are allowed as expenses in the computation of GloBE Income or Loss to the extent of contributions to a Pension Fund during the Fiscal Year. The adjustment is equal to the difference between:

(a) the amount of pension contributions during the year and

(b) the amount accrued as an expense in the computation of Financial Accounting Net Income or Loss during the Fiscal Year

Positive amount: added to profit or loss/ Negative amount: deducted from profit or loss

Examples: ARTICLE 3.2.1(b) Excluded dividends

Year 1				Year 2			
Jan.-March	April -June	July – Sept.	Oct. – Dec.	Jan.-March	April -June	July – Sept.	Oct. – Dec.
		200 Shares					
				100 Shares			
		1 July Acquisition 200		31 March Acquisition 100			31 December Dividend 30

Dividend per share EUR 0.10

% shareholding of A co. in B co. <10%

Short-term portfolio holding – 100 shares

So, dividend of EUR 10 will be taken in GLoBE income

Year 1				Year 2			
Jan.- March	April -June	July – Sept.	Oct.-Dec.	Jan.-March	April -June	July – Sept.	Oct. – Dec.
		200 Shares					
				60 Shares			
				40 Shares			
		1 July Acquisition 200		31 March Acquisition 100		30 September Sale 40	31 December Dividend 26

Dividend per share EUR 0.10

% shareholding of A co. in Bco. <10%

Sale will be presumed from the latest acquired shareholding

So, dividend of EUR 6 will be taken in GLoBE income

Year 1				Year 2			
Jan.- March	April - June	July – Sept.	Oct. – Dec.	Jan. - March	April - June	July – Sept	Oct. – Dec.
		150 Shares					
		50 Shares		100 Shares			
		1 July Acquisition 200	31 December Sale 50	31 March Acquisition 100			Dividend 25

Dividend per share EUR 0.10

% shareholding of A co. in Bco. <10%

Sale will be presumed from the latest acquired shareholding

So, dividend of EUR 10 (on short term portfolio holding) will be taken in GLoBE income

Examples: Article 3.2.1(f): Asymmetric Foreign Currency Gains or Losses

Tax Functional Currency (Euros)		Accounting Functional Currency (Dollars)	
Other income	500	Other income	625
Foreign currency gain (loss)	(200)	Foreign currency gain (loss)	-
Total profit	300	Total profit	625
Country A Tax	60	Country A Tax	75
ETR	20%		12%

Accounting Functional Currency (Dollars)	
Other income	625
Asymmetric Foreign Currency Gain (Loss) Adj.	(250)
Total profit	375
Country A Tax	(75)
ETR	20%

Non-interest bearing bond of \$1,000
 \$:€ – \$1: € 1.25; loss because of fx recorded in tax books €(200)
 Situation of Asymmetric fx gains/ losses - losses in tax books translated to \$ and subtracted in Financial accounting net income/ loss

Tax Functional Currency (Euros)		Accounting Functional Currency (Dollars)	
Other income	1,000	Other income	1,250
Foreign currency gain (loss)	-	Foreign currency gain (loss)	(125)
Total profit	1,000	Total profit	1,125
Tax	(200)	Tax	(250)
ETR	20%		22.2%

Accounting Functional Currency (Dollars)	
Other income	1250
Foreign Currency Gain (Loss)	(125)
Asymmetric Foreign Currency Gain (Loss) Adj.	125
Total profit	1,250
Country C Tax	(250)
ETR	20%

Loan/ interest in Euro
 \$:€ – €1:\$1.25; loss because of fx recorded in accounting books \$(125)
 Situation of Asymmetric fx gains/ losses - fx in accounting books nullified since no actual gain/ loss

Examples: Article 3.2.3 - Arm's length requirement for cross-border transactions

Entity	Tax rate
A (Country A)	25%
B (Country B)	No taxes for entities located in Country B

Situation 1

- B co. provides services to A co.
- **Financial accounts of A Co reflect an expense of 100 and the financial accounts of B Co reflect income of 100 in respect of the transaction**
- For tax purposes, however, **A Co deducts 150 in respect of the services**
- **As a result, 50 of the MNE Group's income is not subject to tax in Jurisdiction A and is not exposed to Top-up Tax in Jurisdiction B**
- A Co to include the 50 of additional expense in the computation of its GloBE Income or Loss for Year 1 and B Co to include 50 of additional income in the computation of its GloBE Income or Loss for Year 1

Situation 2

- A Co reported **80 of expense from the transaction with B Co in its Jurisdiction A tax return** (as a result of unilateral APA)
- A Co reported **80 of expense in its Jurisdiction A tax return for Year 1 and 100 of expense in its financial accounts for Year 1**
- As a result, A Co is subject to tax in Jurisdiction A on 20 of income that is also exposed to Top-up Tax in Jurisdiction B. To avoid double taxation under the GloBE Rules, Article 3.2.3 requires A Co to reduce the expense by 20 in the computation of its GloBE Income or Loss and B Co to include 20 less income in the computation of its GloBE Income or Loss

Examples: Article 3.2.6 - Election to spread capital gains over five years

- A Co is incorporated and tax resident in Country A and holds Local Tangible Assets
 - Year 3: A Co disposed of a Local Tangible Asset and incurred a Net Asset Loss of EUR 25
 - Year 5: A Co disposed of its remaining Local Tangible Assets for EUR 300
 - Carrying value of the Local Tangible Assets disposed of in Year 5 was EUR 100
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- Net gain – Year 5 : EUR 200

Because of election, gain in Year 5 must first be attributed to loss of Year 3 i.e., EUR 25 < *Aggregate Asset Gain in the Election Year must first be carried-back to the earliest Loss Year and set-off against any Net Asset Loss*>

A Co must allocate the remaining EUR 175 evenly to each Fiscal Year in the Look-back Period, which consists of the four prior Fiscal Years and the Election Year.

Aggregate Asset Gain	Year 1	Year 2	Year 3	Year 4	Year 5 / Election year
EUR 200	EUR 35	EUR 35	EUR 60	EUR 35	EUR 35

Article 3.3 - International shipping income exclusion

Article 3.3.1	Exclusion of income/ loss from shipping income
Article 3.3.2	Defines International Shipping Income
Article 3.3.3	Excludes not only International Shipping Income from the computation of GloBE Income or Loss but also Qualified Ancillary International Shipping Income
Article 3.3.4	Provides a limitation on the amount of ancillary income that qualifies for the exclusion. The rationale for the limitation is that ancillary activities should only qualify for the exclusion where they are providing necessary support to the primary activity of the international shipping operation
Article 3.3.5	Related to the deduction and allocation of costs related to International Shipping Income and Qualified Ancillary International Shipping Income. Costs directly incurred by a Constituent Entity from the operation of an international shipping business should be allocated on a facts and circumstances basis to compute the net income of a Constituent Entity from its international shipping activities

Examples: Article 3.3 - International shipping income exclusion

Situation 1:

Financial Accounting Net Income - EUR 200

Income from activities not covered in 3.3 - EUR 60

International Shipping Income - EUR 100; Qualified Ancillary International Shipping Income - EUR 40

GLoBE income - EUR (200-140) = EUR 60

Situation 2:

Financial Accounting Net Income - EUR 200

Income from activities not covered in 3.3 - EUR 40

International Shipping Income – EUR 100; Qualified Ancillary International Shipping Income - EUR 60

Article 3.3.4 provides that the aggregated Qualified Ancillary International Shipping Income of all Constituent Entities located in a jurisdiction shall not exceed 50% of those Constituent Entities' International Shipping Income

GLoBE income - EUR (200-160+10) = EUR 50

Situation 3:

Financial Accounting Net Income - EUR 200

Income from activities not covered in 3.3 - EUR 360

International Shipping Income - (EUR 100); Qualified Ancillary International Shipping Income - (EUR 60)

Article 3.3.4 provides that the aggregated Qualified Ancillary International Shipping Income of all Constituent Entities located in a jurisdiction shall not exceed 50% of those Constituent Entities' International Shipping Income

GLoBE income - EUR (200+160) = EUR 360

Article 3.4 - Allocation of Income or Loss between a Main Entity and a Permanent Establishment

Article 3.4.1	Article 3.4.1 refers to cases where a PE exists for purposes of the GloBE Rules by virtue of paragraphs (a), (b), and (c) of the definition included in Article 10.1. Financial accounting Net income or loss: <ul style="list-style-type: none">– profit or loss reflected in separate financial accounts of PE, or– if no separate financial accounts: profit or loss which would be reflected in separate financial accounts of PE if prepared on standalone basis, in accordance with accounting standard used in preparation of Consolidated Financial Accounts of UPE
Article 3.4.2	If PE satisfies para. (a) or (b) of definition, adjustment is made: to reflect only the amounts and items of income and expense that are attributable to the PE in accordance with the applicable Tax Treaty or domestic law of the jurisdiction where it is located regardless of the amount of income subject to tax and the amount of deductible expenses in that jurisdiction If PE satisfies para. (c) of definition, adjustment is made: to reflect only the amounts of income and expense that would have been attributed to it in accordance with Article 7 of the OECD Model Tax Convention

Article 3.4 - Allocation of Income or Loss between a Main Entity and a Permanent Establishment

Article 3.4.3	Article 3.4.3 describes the attribution of income to a PE that arises under paragraph (d) of the PE definition in Article 10.1. Financial Accounting Net Income or Loss is computed: <ul style="list-style-type: none">– using income exempted in jurisdiction where Main Entity is located– using expenses which are not deducted for tax purposes in jurisdiction where Main Entity is located
Article 3.4.4	The Financial Accounting Net Income or Loss of a Permanent Establishment is not taken into account in determining the GloBE Income or Loss of the Main Entity, except as provided in Article 3.4.5
Article 3.4.5	GloBE Loss of PE is regarded as expense of Main Entity in computation of domestic taxable income of Main Entity, and is not set-off against taxable income in both jurisdictions Subsequent GloBE Income of PE is regarded as GloBE Income of Main Entity up to the amount of previous GloBE Loss

Article 3.5 -Allocation of Income or Loss from a Flow-through Entity

Article 3.5 outlines how the GloBE Income or Loss of a Flow-through Entity is allocated between different Constituent Entities. Flow-through Entities can be divided into two categories: Tax Transparent Entities and Reverse Hybrid Entities. *A Flow-through Entity is treated as a Tax Transparent Entity if the direct owners of the Entity treat it as fiscally transparent. A Flow-through Entity is treated as a Reverse Hybrid Entity if the direct owners treat the Entity as opaque or not fiscally transparent.*

Article 3.5.1	Allocates the Financial Accounting Net Income or Loss of a Flow-through Entity among PEs, Constituent Entity-owners and the Entity itself
Article 3.5.2	<ul style="list-style-type: none">- It recognises that the same Flow-through Entity can be treated as a Tax Transparent Entity by some of its owners and a Reverse Hybrid Entity by its other owners- In such cases, Article 3.5.1 are to be applied separately from the perspective of each Constituent Entity-owner- In such cases, Article 3.5.1 applies the Tax Transparent Entity treatment with respect to Constituent Entity-owners that treat the entity as tax transparent, and applies the Reverse Hybrid Entity treatment with respect to the other Constituent Entity-owners
Article 3.5.3	<ul style="list-style-type: none">- Deals with the situation where the Flow-through Entity has non-Group owners- The provision reduces the Financial Accounting Net Income or Loss of the Flow-through Entity by the amount that belongs to the non-Group owners.- This is done to ensure that the jurisdictional ETR of the Constituent Entities is properly computed because it does not take into account any taxes paid by non-Group members
Article 3.5.4	Sets out two cases where Article 3.5.3 does not apply. The first one is included in paragraph (a) which covers the case where the UPE is a Flow-through Entity. Paragraph (b) covers the situation where the Flow-through Entity is held by a Flow-through UPE through a Tax Transparent Structure. These cases are not contemplated in Article 3.5.3 because all of the owners of the Flow-through Entity are non-Group owners, which is covered by Article 7.1
Article 3.5.5	Article 3.5.5 requires a Flow-through Entity to reduce its Financial Accounting Net Income or Loss by the amount of its income allocated to other Constituent Entities (Constituent Entity-owners or PEs). This is necessary to avoid double-counting that income or loss under the GloBE Rules