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In this article, the authors identify 10 surprising possible outcomes of the application of the OECD's pillar 2 initiative.

With more countries proposing and enacting pillar 2 legislation,[1] multinational enterprises may be familiar with the general framework of the pillar 2 model rules and the extensive corresponding guidance that has been released to date.[2] A closer examination of the pillar 2 guidance, however, reveals unexpected issues that may come as a surprise to MNEs.

Here are the 10 most common surprise issues that we have encountered to date working with clients globally, particularly as they affect U.S.-based MNE groups.

Some of these issues may stem from unintended glitches in the rules and could perhaps be easily fixed by the OECD/G-20 inclusive framework in the future. Other issues result from deliberate policy choices in the rules, which would likely be more difficult to change. All can pose problems for U.S. MNEs if they are left unexamined in the context of each company's individual facts and circumstances.

[1]Pillar 2 refers to a global taxation mechanism proposed by the OECD/G-20 inclusive framework and designed to ensure that MNEs pay a minimum level of tax. It consists of two interlocking rules (also known as the global anti-base-erosion rules): an income inclusion rule and the UTPR (formerly known as the undertaxed payments rule). It is also considered to include a qualified domestic top-up tax (QDMTT). As of the date of this article, Japan, South Korea, the United Kingdom, and Qatar have enacted pillar 2 legislation. Various EU member jurisdictions, Australia, Canada, New Zealand, Singapore, the United Arab Emirates, and Switzerland have also released draft legislation. For more details, see EY, "BEPS 2.0 — Pillar Two Developments Tracker" (last updated Nov. 10, 2023).

[2]OECD, "Tax Challenges Arising From the Digitalization of the Economy — Global Anti-Base Erosion Model Rules (Pillar Two)" (Dec. 21, 2021); OECD, "Tax Challenges Arising From the Digitalisation of the Economy — Commentary to the Global Anti-Base Erosion Model Rules (Pillar Two), First Edition" (Mar. 14, 2022); OECD, "Safe Harbors and Penalty Relief: Global Anti-Base Erosion Rules (Pillar Two)" (2020) ("Guidance on Safe Harbors and Penalty Relief"); OECD, "Tax Challenges Arising From the Digitalisation of the Economy — Administrative Guidance on the Global Anti-Base Erosion Model Rules (Pillar Two)" (Feb. 2, 2023) ("February 2023 Administrative Guidance"); OECD, "Tax Challenges Arising From the Digitalisation of the Economy — Administrative Guidance on the Global Anti-Base Erosion Model Rules (Pillar Two), July 2023" (July 14, 2023) ("July 2023 Administrative Guidance").

Summary of Top 10 Surprise Issues

1	Potential loss of benefits from U.S. tax basis step-ups arising from pre-GLOBE stock acquisitions subject to purchase accounting
2	Potential reduction of benefits from U.S. tax basis step-ups from section 754 or section 338(h)(10) elections because of challenges in applying the deemed asset transfer rules under article 6.2.2 or article 6.3.4
3	Decreased effective tax rate (ETR) from U.S. green energy credits and low-income housing tax credit despite special GLOBE rules for tax equity investments and transferable and refundable credits
4	Challenges in qualifying for the rule in article 7.1.1 that allows ultimate parent entities (UPEs) that are an S corporation or partnership to reduce GLOBE income
5	Possible acceleration of the transition year for U.S. MNEs that have U.S. entities or permanent establishments held under foreign subsidiaries, or that have foreign subsidiaries holding hook stock
6	Indefinitely long transition period for purposes of the antiavoidance rule in article 9.1.3 for MNE groups below the €750 million revenue threshold
7	Unexpected classifications of check-the-box entities as non-hybrid entities (precluding push-down of U.S. taxes) or as reverse hybrid entities (leading to stateless entity treatment)
8	Lack of clear guidance on how to allocate U.S. taxes to a PE
9	Requirement to perform full GLOBE calculations for purposes of allocating taxes on global intangible low-taxed income taxes, even when the relevant controlled foreign corporations qualify for safe harbors
10	Adoption of QDMTT (and potentially IIR or UTPR), which could trigger a foreign use under the dual consolidated loss (DCL) rules

1. Loss of U.S. Tax Basis Benefits From Pre-GLOBE Purchase Accounting Adjustments

This is probably the most significant issue we have encountered to date, both in terms of how commonly it arises and its effects on computing the U.S. ETR[3] under the GLOBE rules.

For financial accounting purposes, if a member of a consolidated group acquires a controlling interest in the stock of an entity in a business combination transaction, the acquired entity's assets and liabilities are consolidated into the group's financial statements at fair market value as of the date of the acquisition (this accounting practice is commonly referred to as "purchase accounting"). Some accounting standards (for example, U.S. generally accepted accounting practices) permit these FMV adjustments to be pushed down to the financial accounts of the acquired entity as a policy election by the acquiring company (push-down accounting).[4]

If the target entity becomes a constituent entity of an MNE group as a result of an acquisition, article 6.2.1(c) of the model rules requires the target to determine its GLOBE income or loss and adjusted covered taxes using the "historical carrying value" (pre-acquisition value) of the assets and liabilities. The commentary on article 6.2.1(c) states that, in such an acquisition, the effect of any purchase accounting adjustments are generally ignored, irrespective of whether the acquisition was made before or after the applicability date of the GLOBE

[3] Throughout the article, all references to ETR are for purposes of GLOBE and not financial statement purposes.

[4] Financial Accounting Standards Board, Accounting Standards Update (ASU) 2014-17, Business Combinations (Topic 805): Pushdown Accounting.

rules.[5] Relatedly, the commentary on article 6 states that any deferred tax assets (DTAs) or deferred tax liabilities (DTLs) connected with purchase accounting adjustments must also be excluded from the computation of adjusted covered taxes to prevent distortive ETR outcomes.[6]

Because stepped-up basis in assets is generally considered a beneficial attribute in the computation of GLOBE income or loss because of the resulting depreciation or amortization of the assets, the foregoing rules, which prohibit purchase accounting adjustments from being taken into account for GLOBE purposes, may give rise to some surprising GLOBE outcomes for taxpayers. In addition, questions arise regarding how the rules apply to business acquisitions that occurred in pre-GLOBE years.

The first question is whether articles 6.2.2 or 6.3.4 of the model rules apply to pre-GLOBE transactions. Articles 6.2.2 and 6.3.4 operate (on an automatic and elective basis, respectively) to treat certain ownership interest transfers (for example, stock transfers) as deemed asset transfers, thereby enabling the acquired entity to step up its basis in its assets for GLOBE computation purposes.[7] For an acquisition of a U.S. corporation for which an election under section 338(h)(10) is made, for instance, the acquisition is generally expected to meet the requirements outlined in article 6.3.4.[8] The transaction, therefore, may give rise to a beneficial step-up basis under the GLOBE rules despite the prohibition on taking any purchase accounting adjustments.

However, it is unclear whether articles 6.2.2 and 6.3.4, and article 6 are relevant to pre-GLOBE transactions. The OECD secretariat's view appears to be that article 6 (which generally covers transactional issues) is relevant only to transactions taking place after GLOBE enters into force — otherwise, every transaction undertaken before GLOBE would potentially need to be analyzed under the rules in article 6 to compute the carrying value of assets as of the first GLOBE year.[9] Applying article 6 to pre-GLOBE transactions would be unwieldy and potentially contradict the intent and purpose of article 9.1 (which governs which attributes, including basis and deferred tax balances, are taken into account when GLOBE begins). On the other hand, the commentary to article 6 requires the reversal of purchase accounting adjustments even for pre-GLOBE transactions, which suggests that some aspects of article 6 do in fact apply to pre-GLOBE transactions. The fact that this rule is in the article 6 commentary rather than in article 9 creates confusion as to which elements of article 6, if any, are intended to apply to pre-GLOBE transactions.

Assuming that the article 6 rules do not generally apply pre-GLOBE, what could otherwise qualify as an article 6.2.2 or 6.3.4 transaction would not benefit from asset basis step-ups in the hands of the target if the transaction occurs in a pre-GLOBE year. The policy justification for this may be that built-in gains from pre-GLOBE transactions are not subject to GLOBE, so a step-up for the buyer is not justified after GLOBE becomes effective. This result, however, is harder to justify when the transaction was taxable locally to the seller or the target (which is generally the case in a section 338(h)(10) transaction), or when the transaction occurs on or before November 30, 2021 (and therefore before the GLOBE rules were made available to the public). In a related context, article

[5] Commentary on article 6.2.1(c), paras. 50 and 51. *See also* commentary on article 3.1.2, para. 3 (providing rules consistent with the foregoing). The exception to this rule applies if:

- the financial accounting standard used by the UPE in preparing its consolidated financial statements permits the UPE to push down fair value adjustments to the separate accounts of the acquired constituent entity;
- the acquisition occurred before December 1, 2021; and
- the MNE group does not have sufficient records to determine its financial accounting net income or loss with reasonable accuracy based on the unadjusted carrying values of the acquired assets and liabilities.

Commentary on article 6.2.1(c), para. 51; commentary on article 3.1.2, para. 3.

[6] Commentary on article 6, para. 17.

[7] Article 6.2.2 and 6.3.4 are discussed in further detail later in this article.

[8] However, please refer to the discussion of issue no. 2 in this article regarding certain income and tax mismatch issues when applying article 6.3.4 to a section 338(h)(10) election transaction.

[9] In a webinar sponsored by the International Fiscal Association, a representative from the OECD's Centre for Tax Policy and Administration stated that articles 6.2.2 and 6.3.4 are intended to apply only after the GLOBE rules come into effect. International Fiscal Association USA, "A Deep Dive Into the Transactional Aspects of Pillar 2/GloBE," YIN Regional Webinar (Feb. 13, 2023).

9.1.3, which disallows basis step-ups for intragroup transactions, does not apply to transactions occurring on or before November 30, 2021, and contains an exception for transfers that are subject to local tax. Unfortunately for taxpayers, no such exceptions apply in the context of pre-GLOBE purchase accounting adjustments.[10]

The second question concerns whether any DTAs and DTLs created as a result of a pre-GLOBE business acquisition should be taken into account in GLOBE years. The answer to that question appears to differ depending on whether the deferred items are "in connection with"[11] purchase accounting adjustments.

Let's assume that an entity (U.S. or foreign) in an MNE group acquires the stock of a U.S. target corporation in a pre-GLOBE year, and a section 338(h)(10) election is made for the target. Further assume that the target's assets and liabilities are recorded at FMV in the MNE group's consolidated financial statements as a result of purchase accounting applied for the acquisition. However, at the level of the target's local financial accounts, the FMV adjustments are not pushed down. In this case, the target records DTAs for its assets on its local financial accounts because the assets' tax basis (which is stepped up for U.S. tax purposes as a result of the section 338(h)(10) election) is higher than the assets' book basis (which equals its historic carrying value because no push-down accounting applies).

Based on the commentary on article 6, these DTAs are not eliminated because they are not connected with the purchase accounting adjustments made on a consolidated basis or any push-down accounting. Moreover, under article 9.1.1, all pre-GLOBE DTAs and DTLs reflected in the financial accounts of constituent entities carry into the GLOBE income or loss computations (subject to recasting at the minimum rate of 15 percent), except as provided in article 9.1.2 (on DTAs arising from certain excluded items) or article 9.1.3 (relating to intercompany transfers). Therefore, assuming article 9.1.2 or 9.1.3 is not triggered, the foregoing DTAs should be brought into the GLOBE system under article 9.1.1. While the target should not benefit from any stepped-up basis in its assets due to the requirement to back out purchase accounting adjustments for GLOBE purposes, the DTAs here should nevertheless benefit the taxpayer when they are reversed and treated as increases to covered tax in GLOBE years.

Let's consider an alternative scenario with the same facts, except that the acquirer applies push-down accounting. In this case, the target does not record a DTA in its local financial accounts because the book basis in the assets (which is stepped up because of the push-down accounting) equals the tax basis (which is stepped up because of the section 338(h)(10) election). As a result, depending on how one interprets the rules in the commentary on article 6, the acquirer could have a different (and much less favorable) pillar 2 result because amortization from the U.S. tax basis will reduce the U.S. ETR, without any deferred tax expense to increase covered taxes. If this were the case, this would lead to the strange result that companies using push-down accounting could be in a different position than those that do not (for example, push-down accounting is generally not permitted under the international financial reporting standards).

2. Reduction of U.S. Tax Basis Benefits From Section 754 and 338(h)(10) Transactions

Articles 6.2.2 and 6.3.4 under the model rules would treat transfers of ownership interests as if they were transfers of underlying assets and liabilities if certain conditions are met. Under article 6.2.2, deemed asset transfer treatment would be granted if the jurisdiction in which the target is located (or the jurisdiction in which the assets are located for a tax transparent entity):

- treats the transaction in the same or similar manner as a transfer of assets and liabilities; and
- taxes the seller based on the difference between the tax basis in the assets and liabilities and the consideration received or the FMV of the assets and liabilities.

If the target is required or permitted to adjust its basis in assets and liabilities to FMV for tax purposes in its jurisdiction, article 6.3.4 permits the target to elect to include in its GLOBE income

[10] While there is a limited exception, discussed in note 5, *supra*, this is a very difficult standard to meet in our experience.

[11] Commentary on article 6, para. 17.

or loss an amount equal to the difference between the historical carrying value of its assets and liabilities and the FMV of its assets and liabilities immediately after the transfer (subject to certain non-qualifying gain or loss adjustments) and compute its GLOBE income or loss using the FMV of assets and liabilities after the transaction.

The question is whether either article 6.2.2 or article 6.3.4 applies to a transaction to which a section 754 election is made. If an interest in a U.S. partnership is transferred and a section 754 election is filed for the partnership, then section 743(b) requires the partnership to adjust the basis of its property by the difference between the buyer's basis in the partnership (outside basis) and the buyer's proportionate share of the adjusted basis of the partnership property (inside basis). If the former is higher than the latter, the adjustment will be positive; if the former is less than the latter, the adjustment will be negative. Section 743(b) basis adjustments, however, apply only to the buyer.[12]

Article 6.2.2 does not appear to describe a section 754 election. Here, regardless of the inside basis adjustments, the transaction constitutes a transfer of a partnership interest (that is, transfer of a constituent entity) and is not deemed for U.S. tax purposes to be a transfer of partnership assets. This is arguably inconsistent with the article 6.2.2 requirement that the transaction be treated "in the same or similar manner as a transfer of assets and liabilities." Moreover, while a tax on the gain from the transaction would apply to the partner-seller, the amount of the seller's gain is not based on the difference between the tax basis in the assets and the consideration received or the FMV of the partnership's assets. This transaction contrasts with a U.S. seller's sale of a U.S. disregarded entity (which appears to be covered by article 6.2.2), in which the transaction is treated as an asset sale and the seller is taxed based on the tax basis and FMV of the disregarded entity's assets.

Article 6.3.4 may not cover a section 754 transaction either. For article 6.3.4 to apply, the U.S. target should be "required or permitted to adjust its basis in assets and liabilities to fair value" for U.S. tax purposes. In a section 754 transaction, the basis of the partnership assets is adjusted based on the difference between the transferee partner's outside basis in the partnership and its proportionate share of the inside basis. In other words, any basis adjustment is not up to FMV but rather only to a fraction of it, depending on the share that is acquired. In addition, while article 6.3.4 contemplates that the target constituent entity (the partnership) adjusts the basis of its assets, it is not clear this condition is satisfied in a section 754 election when the basis adjustment is made for the transferee partner only. Therefore, it is not clear that section 754 aligns squarely with the language of article 6.3.4.

In a webinar sponsored by the International Fiscal Association, a representative from the U.S. Department of Treasury acknowledged that neither article 6.2.2 nor article 6.3.4 appears to apply to the section 754 transaction.[13] From a policy perspective, this transaction should benefit from the principles of articles 6.2.2 and 6.3.4 because it should give rise to gain, and thus accompanying tax, either under the seller's jurisdiction or under GLOBE, in the hands of the seller.

In the case of a section 338(h)(10) election transaction, article 6.3.4 poses another challenge. A section 338(h)(10) transaction is generally expected to meet the requirements of article 6.3.4, giving rise to a basis step-up in the assets of the target for GLOBE purposes. Despite these benefits, however, the application of article 6.3.4 may give rise to a potential mismatch between where the GLOBE income from the deemed asset transfer accrues and where the covered taxes associated with the transfer accrue.

For U.S. tax purposes, the target in a section 338(h)(10) transaction is deemed to sell all its assets and be liquidated into its corporate parent before the close of the transaction date — any tax on the gain from the target's deemed asset transfer is borne by the seller's group. For GLOBE purposes, however, neither the model rules nor the commentary clearly state whether the buyer or the seller group takes into account GLOBE income from the transfer. The language of article 6.3.4 could suggest that it is the buyer's MNE

[12] *See* section 754(b).

[13] International Fiscal Association webinar, *supra* note 9.

group that reflects GLOBE income from the transfer.

Under article 6.3.4, the party to recognize GLOBE income from the transaction and to use the FMV of the assets for purposes of GLOBE after the triggering event is "a Constituent Entity of an MNE Group that is required or permitted to adjust the basis of its assets . . . to fair value" for tax purposes. The MNE group here (of which the target is a part) seems to refer to the buyer's group because it will be the buyer's group within which the constituent entity will adjust the basis of its assets and use the FMV of the assets going forward. This interpretation is also supported by article 6.3.4(c)(ii), which permits the target constituent entity to spread the gain from the deemed asset transfer over five fiscal years for GLOBE purposes, *unless* the constituent entity "leaves the MNE Group" in a fiscal year (in which case any remaining gains will be wholly included in that fiscal year). Because the target has already left the seller's group upon the deemed asset transfer, the only logical way to interpret the MNE group referenced in the exception phrase above appears to be that it is the buyer's MNE group.

A potential counterview is that article 6.3.4(a)(ii) may imply that the seller's MNE group reflects the GLOBE income from the deemed asset transfer. Article 6.3.4(a)(ii) requires the target constituent entity to decrease the stepped-up basis in the assets deemed transferred by any "Non-Qualifying Gain" arising in connection with the transaction. Non-qualifying gain is the taxable "boot" portion of a GLOBE reorganization (for example a section 368(a)(1) asset reorganization) and, as provided under article 6.3.3, is recognized by the *disposing* constituent entity for GLOBE purposes. Because the non-qualifying gain is to be recognized by the seller, consistent treatment may need to apply when interpreting article 6.3.4.

If the rule, as applied by implementing countries, attributes income to the buyer, the section 338(h)(10) transaction to which article 6.3.4 applies may not be very attractive because of the potential mismatch between the locations of the GLOBE income (the buyer's group) and covered taxes (the seller's group).

3. Decreased ETR From U.S. Green Energy Credits

The July 2023 Administrative Guidance contains special rules on the GLOBE treatment of marketable transferable tax credits (MTTCs).[14] Generally, an MTTC is a tax credit that:

- can be used by the credit holder to reduce covered tax liability in the credit-issuing jurisdiction; and
- meets certain legal transferability and marketability standards.

MTTC status is determined separately in the hands of the credit's original holder (the originator) and in the hands of the credit purchaser. A tax credit qualifying as an MTTC is treated as GLOBE income in a manner similar to government grants or qualified refundable tax credits (QRTCs) (generally, tax credits that are refundable within four years from when a constituent entity satisfies the conditions for receiving them). On the other hand, a non-MTTC (a credit that is transferable but does not meet the definition of an MTTC), is treated as a reduction to covered taxes for GLOBE purposes.[15] While credits reduce the ETR regardless of whether they are treated as GLOBE income or as a tax reduction, MTTCs and QRTCs would reduce the ETR less than non-MTTCs and thus are generally considered more beneficial to taxpayers.

In the United States, the renewable energy-related transferable credits governed under section 6418 and introduced as part of the Inflation Reduction Act (IRA) are expected to be treated as MTTCs for the originators (but not, as discussed later, for the purchasers). The direct-pay credits governed under section 6417 (also enacted under the IRA) are expected to be treated as QRTCs. While the favorable treatment of IRA credits would otherwise be a welcome development for the holders of those credits, the holders would still need to consider certain implications associated with the credits, which are sometimes unexpected and not necessarily favorable.

The GLOBE rules generally require the originator of an IRA transferable credit governed

[14] *See* July 2023 Administrative Guidance, section 2 ("Guidance on Tax Credits"), paras. 34-39.

[15] *See id.*, section 2 ("Guidance on Tax Credits"), paras. 40-44.

under section 6418 to include in its GLOBE income an amount equal to the face value or, in the case of a transfer, the transfer price of the credit (subject to certain exceptions). For U.S. tax purposes, the originator is not subject to any tax when receiving or transferring the credit.[16] Because the IRA transferable credit would be treated as GLOBE income without any corresponding covered taxes, the originator may experience some notable ETR reduction, especially when the size of the credit to be reflected in GLOBE income would be significant. A similar ETR reduction occurs if the taxpayer receives the credit in the form of a direct payment under section 6417 that is treated as a QRTC for GLOBE purposes.

For companies with GLOBE ETRs well above 15 percent, the ETR reduction from treating the MTTC or QRTC as GLOBE income may not pose an issue. But for companies with ETRs at or below 15 percent before taking into account MTTCs or QRTCs,[17] 15 percent of the amount of benefit received from these credits will effectively be subject to a 15 percent top-up tax.

Purchasers of an IRA transferable credit would expect the credit to be treated as a non-MTTC, not an MTTC, because they cannot re-transfer the credit under section 6418, thus failing the legal transferability standard for GLOBE purposes. The July 2023 Administrative Guidance would require the purchaser in that case to reduce its covered tax by any excess of the face value of the credit over its purchase price in proportion to the amount of the credit to satisfy its liability for a covered tax. In other words, the purchaser's covered taxes would be reduced to the extent of any discount it enjoyed from the credit purchase. While this treatment is more favorable than reducing the covered tax by the entire face value or purchase price of the credit, the purchaser would still experience a reduction in its covered taxes by purchasing the credit at a discount. To the extent the purchaser's GLOBE ETR in the United States is already at or below 15 percent, any benefit received from the tax credit purchase will be recaptured once an IIR or UTPR applies to U.S. profits.[18]

4. Challenges in Qualifying for Article 7.1.1

If a tax transparent entity is the UPE of an MNE group, there may be a mismatch between the income and covered taxes associated with that entity for GLOBE purposes. On the one hand, the tax transparent entity's income remains in the UPE jurisdiction under article 3.5.1(c) (although its income for tax purposes would be reflected in its owners' jurisdictions) because its owners are not part of the MNE group. On the other hand, any covered taxes paid by the owners on the income of the tax transparent entity are not allocated to it because the owners are outside the MNE group. This mismatch may result in a significant top-up tax in the UPE jurisdiction even if taxes are duly imposed on and borne by the tax transparent entity's owners. The policy challenge here is that the pillar 2 goal of imposing a 15 percent corporate level tax on MNE groups is difficult to apply when the MNE group is not taxed at the corporate level. Having a flow-through parent entity is common for privately-held U.S. groups (for example, with an S corporation parent) or in certain fund structures for which the UPE is a U.S. partnership.

Article 7.1.1 is intended to address this concern, at least for a flow-through UPE. It requires the GLOBE income of a flow-through entity (an entity that is treated as fiscally transparent in its own jurisdiction, which includes a tax transparent entity) to be reduced by the GLOBE income attributable to each ownership interest if one of three conditions is met:

- the holder of the ownership interest is subject to tax on that income for a tax period ending within 12 months of the end of the MNE group's fiscal year and the holder is subject to tax on the full amount of that

[16] *See* section 6418(b).

[17] This could be for a variety of reasons such as companies benefiting from the foreign-derived intangible income deduction or research credits, or the downward ETR effect of the GLOBE rules recasting deferred tax expenses from a 21 percent statutory rate to 15 percent.

[18] Similar results occur with respect to the net benefit obtained by investors in tax equity partnerships under the OECD's guidance for qualified flow-through tax benefits. *See* February 2023 Administrative Guidance, section 2.9.2, para. 16 (treating an investor's qualified flow-through tax benefits received from its qualified ownership interest as a negative amount in adjusted covered taxes to the extent those benefits exceed the investor's investment). That is, a company with an ETR at 15 percent will have any net benefit it receives from the tax equity investment recaptured under pillar 2.

income at a nominal rate that equals or exceeds 15 percent; or it can be reasonably expected that the UPE's adjusted covered taxes and the holder's taxes on the income equal or exceeding the amount that results from multiplying the full amount of such income by 15 percent;

- the holder is a natural person that is a tax resident in the UPE jurisdiction and holds a minority interest (5 percent or less) of the UPE; or
- the holder is a designated entity (for example, a government entity) that is a tax resident in the UPE jurisdiction and holds a minority interest (5 percent or less) of the UPE.

In applying article 7.1.1, a question arises as to whether the holder referenced in the rule is a direct or indirect holder. For purposes of the second and third conditions, the commentary on article 7.1.1 requires the relevant ownership interest of the UPE to be "directly" held.[19] When it comes to the first condition, however, the commentary is silent on the direct versus indirect distinction. One interpretation is that the holder under the first condition means a direct holder only. This is consistent with the fact that the same term is interpreted for the second and third conditions, and consistent with how the OECD seems to expressly state (for purposes of other articles under the model rules) whether a relevant ownership interest includes an indirect interest.[20]

On the other hand, a counterargument that the holder includes an indirect holder may also exist. Under this view, the first condition appears to be a general rule that requires a demonstration of actual taxation at the level of the owner while the second and third conditions do not. If this is so, the taxpayer that wishes to rely on the second or third condition may need to be subject to specific requirements that are tighter than those under the first condition, including direct holding, in exchange for not being required to show taxation at the owner's level. This view does not seem to contradict the commentary's lack of any express statement that the holder under the first condition means a direct holder only.

Applying this direct holding requirement to the second and third condition, and possibly the first condition, to qualify for article 7.1.1 may result in some unexpected consequences. If the ultimate owners of a UPE that is a flow-through entity own their interest through multiple tiers of intermediary flow-through entities (such as domestic trusts or partnerships), there is no meaningful change to how the indirect owners are treated for U.S. tax purposes and should not, policy-wise, result in falling outside of article 7.1.1. The article 7.1.1 benefit, however, could be denied in these cases simply because the direct holding requirement is not met.

In the pillar 2 legislation recently enacted by the United Kingdom, this issue does not seem to exist; under a provision corresponding to article 7.1.1, the legislation expressly provides that the holder of an ownership interest in the UPE includes a "direct *or indirect*" holder[21] (emphasis added). Absent the OECD making a similar revision to article 7.1.1, however, it is unclear if other countries will adopt a similar approach.

Another issue relating to article 7.1.1 is the requirement under article 7.1.1(a)(i) that the holder be "subject to tax on the full amount of" the UPE's GLOBE income. It is unclear whether this simply requires showing that the partner is generally subject to U.S. tax (as would be the case with any C corporation) or whether an item-by-item comparison is required of items of the UPE's GLOBE income versus the holder's taxable income in its jurisdiction to identify any relevant GLOBE-to-tax differences. Also unclear is whether the phrase "full amount" means that any permanent differences (however immaterial, such as a small amount of tax-exempt interest income) would preclude the application of the rule.[22] A narrow reading of this requirement would make it very difficult for many companies to benefit from article 7.1.1.

[19] *See* commentary on article 7.1.1, paras. 18 and 21.

[20] For instance, article 1.4 defines the term "UPE" as, among others, an entity that owns "directly or indirectly" a controlling interest in any other entity and is not owned, with a controlling interest, "directly or indirectly" by another entity.

[21] United Kingdom, Finance (No. 2) 2023 (c. 30), Part 3, Chapter 4, section 170(2)(a) (July 26, 2023).

[22] Note that the commentary only mentions the implications of temporary timing differences, which would not cause the holder to fail the requirement. *See* commentary on 7.1.1, para. 12.

5. Possible Acceleration of the Transition Year for Some U.S. MNEs

U.S. MNEs should be mindful of U.S. PEs owned by a directly or indirectly held CFC or "hook stock" that is directly or indirectly owned by a CFC. In either case, this could accelerate the MNE group's transition year for the United States. The model rules state that:

> a Transition Year, for a jurisdiction, is the first Fiscal Year that the MNE Group comes within the scope of the GLOBE Rules in that jurisdiction.[23]

Therefore, the GLOBE rules appear to require a transition year for an MNE group to be determined on a jurisdiction-by-jurisdiction basis (and not on an entity-by-entity basis).[24] This means that the transition year for a given jurisdiction could be the first fiscal year in which the MNE group has at least one constituent entity in that jurisdiction upon whose profits a top-up tax could be charged under an IIR or UTPR imposed by another jurisdiction.[25] For U.S. MNE groups without so-called sandwich structures (no U.S. entities owned under a CFC), the transition year for the United States should be the MNE group's first fiscal year beginning on or after January 1, 2025, when other countries' UTPRs are expected to come into effect, and potentially delayed until fiscal years beginning on or after January 1, 2026, if the MNE group applies the "Transitional UTPR Safe Harbor" for the United States.[26]

However, with a sandwich structure, the transition year for the United States could be accelerated if the U.S. MNE group includes a CFC that owns a U.S. PE or owns stock in the U.S. parent. If either the CFC or one of its direct or indirect owners (such as an upper-tier CFC holding company) is located in a jurisdiction that implements an IIR for fiscal years beginning in 2024, the U.S. PE's or parent's profits would become subject to that IIR (even if no or minimal top-up tax is due),[27] causing the transition year for the United States to begin (at least) in 2024 instead of 2025. In the case of a CFC owning hook stock in the U.S. parent, this could also bring a share of the GLOBE income of other CFCs that are directly or indirectly held by the U.S. parent within scope of an IIR in 2024.

Consequently, certain rules, such as article 9.1 through 9.3, would turn off earlier than expected, because these rules apply only before the transition year begins. For example, for purposes of article 9.1.1, accelerating the transition year for a jurisdiction could mean losing the benefit of DTAs for future use of foreign tax credit carryforwards or general business credits. Article 4.4.1(e) generally excludes the generation and use of such "tax credit DTAs" from GLOBE computations, so that covered taxes are not recognized when the DTA reverses. However, article 9.1.1 applies without regard to article 4.4.1(e), and applies to DTAs, including tax credit DTAs, only if they are established before the transition year.[28] Thus, accelerating the transition year for the United States would eliminate the future GLOBE ETR benefit of deferred tax expense attributable to tax credit DTAs established in fiscal years beginning 2024. U.S. MNEs should therefore be mindful of their U.S. PEs and any risks of creating inadvertent or otherwise insignificant PEs under an IIR jurisdiction.

6. Indefinitely Long Transition Period for MNEs Below the Revenue Threshold

The definition of transition year also creates issues for MNE groups that do not meet the €750 million consolidated revenue threshold. For those groups, the transition year could be many years

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[23] Article 10.1.1 ("Transition Year").

[24] However, country legislation may take a different approach. *See, e.g.*, Canada public consultation draft of Global Minimum Tax Act, at 21 (Aug. 4, 2023) (defining "transition year" as being with respect to a specific constituent entity).

[25] *See* July 2023 Administrative Guidance, section 4, para. 46 ("A Transition Year is the first Fiscal Year that the MNE Group comes within the scope of the GloBE Rules in respect of that jurisdiction. This means that a Transition Year is the first Fiscal Year for which the MNE Group has to undertake the calculations of a jurisdiction in accordance with the GloBE Rules (i.e., the IIR or the UTPR can apply with respect to a Constituent Entity of the MNE Group in the jurisdiction).").

[26] *See* July 2023 Administrative Guidance, section 5.2. The transitional UTPR safe harbor provides transitional relief from a UTPR in the jurisdiction of an MNE group's UPE provided that the jurisdiction has a corporate income tax that applies at a rate of at least 20 percent.

[27] To the extent a top-up tax is owed for the United States, only a ratable portion (based on GLOBE income) of that tax is allocated to the U.S. PE for purposes of applying the IIR. *See* article 5.2.4.

[28] *See* February 2023 Administrative Guidance, section 4.1.3, para. 7.

later, when the group meets the threshold either through gradual growth or acquisition.

Article 9.1.3 of the model rules deals with the attributes relating to the intragroup transfer of assets between constituent entities from December 1, 2021, until the start of the transition year. Subject to certain exceptions, the rule requires the basis in the acquired assets (other than inventory) to be historic carrying value of those assets in the hands of the disposing entity, with DTAs and DTLs brought into the GLOBE period on that basis. In other words, the MNE group would ignore any basis step-up on the intragroup transfer and the incremental depreciation or amortization for GLOBE purposes.

While this rule operates as a temporary-transition-period rule that applies between December 1, 2021, and a company's first fiscal year beginning in either 2024 or 2025 (depending on when GLOBE rules would apply to the GLOBE income of the buyer entity), the period could be much longer for smaller MNE groups that do not meet the consolidated revenue threshold. Those groups could be required to indefinitely track the tax attributes associated with intragroup asset transfers, despite being outside the scope of GLOBE, in anticipation of coming within GLOBE's scope many years down the road.

7. Unexpected Non-Hybrid or Reverse Hybrid Classifications

The existing pillar 2 guidance creates potential challenges surrounding the classification of entities under the definitions for a tax transparent entity, a reverse hybrid entity, and a hybrid entity, as found in article 10.2.[29] Special rules apply to these entities, generally to align the jurisdiction in which GLOBE income is recorded with the jurisdiction in which taxes are paid on that income, such as by allocating GLOBE income or covered taxes (or both) from one constituent entity to another.[30] This can resolve differences between financial accounting standards and local tax rules if, for example, an entity records financial accounting income but its owner pays tax on that income because the entity is transparent for local tax purposes. In general, the definitions of these special entity types depend on the tax treatment of the entity in the jurisdiction in which it is located (either where it was created or where it is tax resident) and the jurisdiction in which its owner is located. The commentary explains that "owner" for this purpose means the entity's *direct* owner.[31]

Because of the U.S. check-the-box rules, numerous issues arise for U.S. companies in classifying foreign and domestic entities. For example, consider a U.S. parent corporation (USP) that wholly owns a foreign company (FDE1), which in turn owns another foreign company (FDE2). A check-the-box election has been made to treat both FDE1 and FDE2 as disregarded entities (DREs) from USP for U.S. tax purposes. Under the model rules, FDE1 is a hybrid entity, so U.S. taxes paid by USP on FDE1's income are allocated to FDE1. However, FDE2 is not a hybrid entity because its *direct* owner is FDE1, which we assume is located in a jurisdiction in which tax law does not recognize U.S. check-the-box elections. Thus, none of USP's U.S. taxes appear to be allocated to FDE2, even though the two entities are treated identically for U.S. tax purposes.

Another issue arises if a U.S. limited liability company has a foreign owner. Because most jurisdictions treat LLCs as corporations (that is, not fiscally transparent) for tax purposes, a foreign-owned U.S. LLC appears to be a reverse hybrid entity under the model rules. Accordingly, the LLC will generally be treated as a stateless entity, meaning that its jurisdictional ETR is calculated on a standalone basis (as if the LLC

[29] *See* articles 10.2.1 through 10.2.5.

[30] *See, e.g.*, articles 3.5.1 (providing rules to allocate the GLOBE income of a tax transparent entity) and 4.3.2(b) and (d) (providing rules to allocate the covered taxes of a tax transparent entity and a hybrid entity, respectively).

[31] *See* commentary on article 10, para. 160 ("An Entity is treated as fiscally transparent under the laws of a jurisdiction . . . if such jurisdiction treats the income, expenditure, profit or loss of that Entity *as if they were derived or incurred by the direct owner of the Entity* in proportion to its interest.") (emphasis added). *See also* commentary on article 3, para. 205 ("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.") (emphasis added); commentary on article 10, para. 154 ("Flow-through Entities can further be divided into two categories: Tax Transparent Entities and Reverse Hybrid Entities. The difference between these terms depends on how the *direct owners* (i.e., holders of their Ownership Interest) are treating them under their domestic tax law.") (emphasis added).

were the only entity in that jurisdiction).[32] Further, the LLC will record GLOBE income that, as a reverse hybrid entity, is *not* allocated to any other entity, and yet will incur no U.S. taxes because it is fiscally transparent for U.S. tax purposes. The result is potentially a 0 percent ETR subject to top-up tax.[33]

Surprises also occur when an entity owner is located in a jurisdiction with no income tax law. Consider a partnership, such as a U.S. limited partnership (U.S. LP), that has a partner located in a jurisdiction without a corporate income tax. Assuming U.S. LP is fiscally transparent for U.S. tax purposes, the model rules should treat it as either a tax transparent entity or a reverse hybrid entity depending on whether the partner's tax law views U.S. LP as fiscally transparent. For a partner located in a jurisdiction with no income tax, however, this determination is unclear. It appears that the U.S. LP may be a reverse hybrid entity because the partner's jurisdiction has no concept of "fiscal transparency." If so, U.S. LP's GLOBE income would not be allocated to the partner, which would in turn prevent any further allocations of GLOBE income "up the chain" if, for example, the partner is itself a partnership. This would be particularly relevant in tiered partnership structures, which are common in financing and private equity arrangements, and could lead to top-up taxes on the profits of an otherwise "true" partnership.

8. Lack of Clear Guidance on Allocations of U.S. Taxes to PEs

Another series of open issues relates to how to allocate taxes paid by a U.S. taxpayer to its foreign PE or other "foreign branch" as defined under section 904(d) (including a foreign DRE or foreign hybrid partnership). For background, article 4.3.2(a) allocates to a PE an amount of covered taxes recorded in the financial accounts of the PE's owner (the main entity or U.S. taxpayer here), if the taxes relate to GLOBE income attributed to the PE.[34] The commentary generally indicates that this allocation should follow the tax rules of the main entity's jurisdiction and should allocate the actual taxes paid by a main entity on the PE's income.[35]

A first open question is how to determine a U.S. taxpayer's income attributable to its foreign PE. As a general rule, U.S. tax rules do not distinguish between home office versus branch income for purposes of computing taxable income, given that the U.S. entity is being taxed as a resident on all of its income, including income earned by a branch. However, the GLOBE rules require determining the relevant U.S. taxable income at the PE level. There are several potential options for doing this. For example, the allocation could follow the income that the U.S. taxpayer reports on the Form 8858 filed for the foreign PE, which is closer to a pure books-and-records approach. Another possibility is an approach based on books and records but adjusted to conform to U.S. tax principles, perhaps similar to the DCL regulations.[36] Or an approach might need to reflect that U.S. taxable income as adjusted to U.S. tax principles could be overstated if there are no adjustments for disregarded payments, in which case the regulations under reg. section 1.904-4(f) could be a more appropriate approach.[37]

It is also unclear whether, and if so how, deferred tax expense should be allocated to a PE. The model rules include a total deferred tax adjustment amount in the numerator of the GLOBE ETR, effectively treating deferred tax expense as covered taxes unless certain exceptions apply.[38] While the commentary makes clear that deferred tax expense should be allocable from one constituent entity to another under article 4.3.2,[39] the most appropriate manner by which to allocate deferred tax expense is uncertain.

[32] *See* commentary on article 5 ("Stateless Constituent Entities are treated as being the only Constituent Entity in a jurisdiction.").

[33] There may be some uplift to the LLC's ETR if it is owned by a CFC, because taxes paid by the CFC's U.S. shareholders on the CFC's subpart F income or GILTI may be allocated to the CFC and its "tested units" (including branches or DREs owned by the CFC).

[34] Article 4.3.2 ("Covered Taxes are allocated from one Constituent Entity to another Constituent Entity as follows: (a) the amount of any Covered Taxes included in the financial accounts of a Constituent Entity with respect to GloBE Income or Loss of a Permanent Establishment is allocated to the Permanent Establishment.").

[35] *See* commentary on article 4, paras. 46-53.

[36] *See* section 1503(d); reg. sections 1.1503(d)-1 through -8.

[37] *See* reg. section 1.904-4(f)(2), including para. (f)(2)(vi) on adjustments for disregarded payments.

[38] *See* article 4.1.1(b) (adjusting covered taxes by the total deferred tax adjustment amount).

[39] *See* commentary on article 4, para. 42.

Consider a U.S. taxpayer that owns a PE with one asset (asset A). Asset A has book basis of $50 and U.S. tax basis of $100, meaning that there is a $50 DTA attributable to asset A. If the U.S. taxpayer then sells asset A to a third party for $100, the DTA should reverse, creating $50 of deferred tax expense that should be allocated to the PE. However, the U.S. taxpayer has no U.S. taxable income on the sale, meaning that the allocation approach described in the commentary for current tax expense would not appear to allocate any deferred tax expense to the PE. Absent further guidance, taxpayers may need to identify a reasonable approach to allocate the deferred tax expense in these circumstances.

These challenges are compounded when the U.S. taxpayer owns multiple PEs or foreign branches. The commentary addresses when a main entity has two or more PEs, explaining the need to eliminate the effect of cross-crediting between the PEs before allocating taxes. Later, the commentary under article 4.3.2(d) indicates that similar allocation rules should apply for allocating taxes from an owner to a hybrid entity in which it owns an interest (assuming both are part of the same MNE group), as would be relevant if a U.S. taxpayer owns a foreign DRE or partnership that creates a foreign branch under section 904(d). However, if a U.S. taxpayer owns both foreign PEs and foreign DREs, it could make sense for the allocations under article 4.3.2(a) and (d) to be combined into a single allocation approach, given that both are foreign branches for purposes of section 904(d) and cross-crediting is generally allowed. A combined approach would be complex but could promote certainty if built upon the existing infrastructure of the section 861 and 904(d) regulations. However, there would still be open questions, such as how to deal with deferred taxes and whether to back out any foreign branches that are neither a PE nor a hybrid entity for purposes of the GLOBE rules (which might include a second-tier DRE, as explained in the prior section). Ultimately, U.S. multinationals may be required to undertake parallel computations to allocate foreign taxes, once for ordinary U.S. tax purposes and once for GLOBE purposes.

On one hand, the lack of clear guidance on allocating taxes to PEs ought to mean that companies have latitude to choose a reasonable method. But on the other hand, there is a concern that any approach could be subject to challenge by non-U.S. tax authorities, which may disagree with the result of a particular approach. This creates significant uncertainty for companies.

9. Compliance Burden From Calculating GLOBE ETR for Safe Harbor Eligible Entities

For a constituent entity whose constituent entity-owner is subject to a CFC tax regime (such as the GILTI regime in the United States), article 4.3.2(c) of the model rules allocates to the CFC any covered tax included in the owner's financial accounts for its share of the CFC's income. The February 2023 Administrative Guidance provides special allocation rules in applying article 4.3.2(c) when the CFC tax regime constitutes a "Blended CFC Tax Regime."[40] Applying these rules to GILTI, the CFC is not allocated any CFC tax if a jurisdiction in which a CFC located has a jurisdictional ETR at or above 13.125 percent, which is the "Applicable Rate" for GILTI.

If a jurisdiction is eligible for the transitional CbC reporting safe harbor (or adopts a QDMTT regime), the general expectation may be that no GILTI tax would be allocated to that jurisdiction because it has a QDMTT or an ETR of at least 13.125 percent for purposes of the CbC safe harbor (if the simplified ETR test applies). For the following reasons, however, that may not always be the case.

The CbC safe harbor[41] is intended to ease for a certain period the compliance and administrative burdens that applying the GLOBE rules imposes on MNE groups and tax administrations. The CbC safe harbor provides three tests (de minimis test, simplified ETR, and routine profits test), the satisfaction of which can be determined based on qualifying CbC reports without the complex adjustments normally required under the model rules. If a jurisdiction meets any one of the three tests under the CbC safe harbor for a year, all the constituent entities in that jurisdiction will be

[40] *See* February 2023 Administrative Guidance, section 2.10 ("Allocation of Taxes Arising Under a Blended CFC Tax Regimes").

[41] *See* Guidance on Safe Harbors and Penalty Relief, section 1 ("Transitional CbCR Safe Harbor").

deemed to have a zero top-up tax in that year for GLOBE purposes.

Even if a jurisdiction is eligible for the CbC safe harbor, an MNE group might still need to compute its ETR in that jurisdiction under the normal GLOBE rules for purposes of GILTI tax allocations for the MNE group, which may result in significant compliance burdens. This is because the blended CFC tax regime allocation rule requires allocating tax based on the "Effective Tax Rate for a jurisdiction as computed under Article 5.1."[42]

Moreover, any GILTI tax allocated to the CbC safe harbor jurisdiction (because the jurisdiction has a GLOBE ETR of lower than the applicable rate of 13.125 percent) will basically be unused because the CbC safe harbor jurisdiction will have no top-up tax regardless of the GILTI tax allocation. Even if a jurisdiction's simplified ETR under the CbC safe harbor equals or exceeds 15 percent or any higher rate (the minimum rate to meet the simplified ETR test), its normal GLOBE ETR may still be below 13.125 percent because of the different approaches adopted to compute the two sets of ETRs.

For the QDMTT, similar implications may arise. A QDMTT is a minimum tax that is included in the domestic law of a jurisdiction and operates to increase domestic tax liability to the minimum rate of 15 percent for the jurisdiction. A QDMTT is computed without regard to the GILTI tax allocation.[43] The OECD/G-20 inclusive framework so far has introduced various rules, apart from those under the model rules and the commentary, to make sure that a QDMTT operates consistently with the GLOBE rules.[44] However, some differences are permitted; most notably, a QDMTT can be based on a local accounting standard rather than the accounting standard used for consolidated financial accounting purposes. The July 2023 Administrative Guidance deems a jurisdiction eligible for the QDMTT safe harbor to have a zero top-up tax for GLOBE purposes even if a top-up tax could have been computed under another country's IIR or UTPR.[45]

In the context of the GILTI tax allocation, like a jurisdiction eligible for the CbC safe harbor, an MNE Group may need to compute a separate GLOBE ETR for that jurisdiction to determine GILTI tax allocations for the MNE group. If the QDMTT jurisdiction's GLOBE ETR is determined to be below 13.125 percent (despite its ETR of 15 percent or above for QDMTT purposes), it would be allocated a GILTI tax from the United States. When the QDMTT jurisdiction satisfies the QDMTT safe harbor requirements, the GILTI tax so allocated would go unused because the QDMTT safe harbor jurisdiction would already be deemed to have a zero top-up tax.

10. Adoption of QDMTT Potentially Triggering U.S. DCL Rules

The GLOBE rules' concept of "jurisdictional blending" potentially creates new risks for U.S.-owned foreign branches or foreign DREs under the U.S. DCL rules.[46] The DCL rules are intended to prevent a double dip of a single economic loss in both the U.S. and a foreign jurisdiction.[47] Under those rules, a U.S. person owning a foreign branch or foreign DRE (in either case, a separate unit) generally cannot reflect any portion of a loss attributable to that separate unit in its U.S. taxable income (that is to say, cannot make a domestic use of the loss).[48] However, an exception exists for losses with no foreign use, in which case the U.S. person can elect a domestic use of the loss in the current tax year, provided that the person demonstrates or certifies for each of five years that the loss indeed has no foreign use.[49]

Commonly, a foreign use arises — and prevents a domestic use election — when the foreign jurisdiction has a tax consolidation or similar regime through which the separate unit's

[42] *See* February 2023 Administrative Guidance, section 2.10.3, para. 8, para. 58.6 to be added to the commentary to article 4.3.2.

[43] *See* February 2023 Administrative Guidance, section 5.1.3, para. 11, para. 118.30 to be added to the commentary to article 10.1.

[44] *See* February 2023 Administrative Guidance, section 5 ("Qualified Domestic Minimum Top-up Taxes"); July 2023 Administrative Guidance, section 4 ("Qualified Domestic Minimum Top-Up Taxes").

[45] *See* July 2023 Administrative Guidance, section 5.1 ("QDMTT Safe Harbor").

[46] *See* section 1503(d); reg. sections 1.1503(d)-1 through -8.

[47] *See, e.g.*, S. Rep. No. 99-313, at 420 (1986).

[48] Reg. section 1.1503(d)-4(b).

[49] *See* reg. section 1.1503(d)-6(d).

loss is effectively shared with a corporation located in the same country. However, many countries lack any tax consolidation or similar regime, or have strict ownership or grouping rules that limit the circumstances in which a loss could be shared (for example, consolidation is only allowed in a direct parent-subsidiary relationship). In those cases, it is possible that no foreign use is made of the loss, so the domestic use election can be made. Many potential DCL issues are eliminated through careful planning and monitoring to ensure that a separate unit does not or cannot enter into a tax consolidation or other loss-sharing regime, because this could both prevent a domestic use election and cause recapture of prior years' DCLs.

A GLOBE top-up tax, and in particular a QDMTT, imposed on a jurisdictional basis would potentially upend this by combining the GLOBE loss of one MNE group entity (a separate unit for DCL purposes) with the GLOBE income of another MNE group entity in that same jurisdiction.[50] Assuming one or more items that compose the GLOBE loss also compose the DCL, the QDMTT would potentially create a foreign use, thus preventing a domestic use of the DCL. Moreover, a book-tax difference could cause a previously certified DCL to be recaptured if an item that composed the DCL in one year is later reflected in a GLOBE loss in a subsequent year within the five-year period. This would threaten recapture of DCLs that were certified even before the GLOBE rules ever took effect. Treasury and the IRS are aware of this issue[51] and may consider future guidance,[52] though the scope and timeline for that guidance is uncertain.

Conclusion

As a result of these unexpected issues, companies may find that their ETR computation leads to surprising results. Considering many of the issues may lead to unintended outcomes, the OECD/G-20 inclusive framework could address some of these issues in future rounds of guidance. In the meantime, careful analysis of these issues sooner, rather than later, is recommended to determine whether some issues can be mitigated. ■

[50] QDMTTs appear to create the most risk of foreign use of a DCL. The DCL regulations define foreign use as occurring when an item of deduction or loss composing the DCL is made available under the income tax laws of a foreign country. While questions may exist as to whether an IIR or UTPR is an income tax, a QDMTT appears likely to be an income tax in the traditional sense — including, for example, for FTC purposes.

[51] *See, e.g.*, Jeff Maydew, Meaghan A. Wolfe, and Jonathan D. Lockhart, "Guidance Requested That the Pillar 2 Jurisdictional Blending Rules Do Not Constitute the Foreign Use of Dual Consolidated Losses," *Tax Notes Int'l*, Aug. 14, 2023, p. 845 (comment letter sent to the IRS by practitioners from McDermott Will & Emery).

[52] *See, e.g.*, Andrew C. Velarde, "IRS Plans on Refining Excise Tax Funding Rule," *Tax Notes Int'l*, Sept. 18, 2023, p. 1617 (quoting an IRS official's comments on a Practising Law Institute panel that the IRS is considering examining how the DCL rules interact with the OECD's pillar 2 rules).