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Legislation

Congress returns amid speculation over limited budget reconciliation

The US Congress returned to Washington at the end of April from its spring recess with Democrats questioning whether limited budget reconciliation legislation is possible and, if so, what would be its parameters. Senator Joe Manchin (D-WV) has expressed some interest in a climate-focused reconciliation bill that also addresses tax changes and deficit reduction.

Senator Manchin is now also separately holding meetings to explore whether some version of an energy bill could be enacted on a bipartisan basis, outside of the reconciliation process.

Among the complicating factors in regard to possible future budget reconciliation legislation this year are differences between Senator Kyrsten Sinema's (D-AZ) and Senator Manchin's tax positions – Senator Sinema opposes tax rate increases and Sen. Manchin supports them – and uncertainty over whether both Senators Manchin and Sinema want a budget agreement.

While there is no new budget legislation or even the outline of a deal as yet, Senator Manchin offered some high-level clarity on 26 April when he outlined what he could support in terms of a scaled-back bill. Following a meeting with Senate Majority Leader Chuck Schumer (D-NY), Senator Manchin was quoted as saying that any future budget reconciliation bill should be focused on reducing inflation, reducing the debt, and “getting a handle on what’s going on.”

To that end, Senator Manchin indicated he supports changes to the tax code, including increasing the corporate tax rate to 25%, setting the capital gains rate at 28% and eliminating “loopholes” and “making sure everyone pays their fair share.” The prospects for any budget deal, however, remain uncertain.

Although there reportedly are discussions taking place among the Biden Administration and Congressional Democrats, Senator Manchin indicated there are no ongoing formal reconciliation negotiations at the present time.

A senior Treasury official in April also offered up that the Biden Administration views both the Treasury Greenbook's repeal of the base erosion and anti-abuse tax (BEAT) and replacement with an undertaxed profits rule (UTPR) and the House-passed *Build Back Better Act's* (HR 5376) BEAT corrections as furthering the OECD's BEPS 2.0 Pillar Two global minimum tax proposal.

The official was quoted as saying the Administration “fully supports the BEAT reforms in the House-passed bill.” According to the official: “Both the green book UTPR proposal and the House BEAT reforms would create powerful incentives for other countries to join and comply with the new global regime, and both further the goals of it.”

The Treasury official also confirmed the Administration remains confident that Congress will pass international tax reform and that the US will meet its commitment to reform the global intangible low-taxed income (GILTI) and BEAT “which remains a top priority for the Administration.”

Senate proposal would disallow foreign tax credits, other US tax benefits connected with operations in Russia or Belarus

Senate Finance Committee Chairman Ron Wyden (D-OR) and Senate Finance Committee Member Rob Portman (R-OH) on 7 April 2022 released a discussion draft of proposed legislation that would disallow foreign tax credits for taxes paid to Russia or Belarus and would also disallow certain other US tax benefits.

In particular, the proposal would amend Section 901(j) to deny foreign tax credits for taxes paid or accrued to Russia or Belarus. The proposal would also eliminate other US tax benefits for persons within the proposal's scope, including tax treaty benefits, benefits under Section 892, the trading safe harbor under Section 864(b) and the shipping exemption under Section 883.

US suspends tax information exchange with Russia

In another sign of deteriorating relations with Russia, the press reported that the US Treasury officially suspended the exchange of tax information with the Russian Government “to bring additional pressure to bear on Russia.” Treasury reportedly ceased exchanging tax information on 24 February 2022.

According to Senators Wyden and Portman, the proposal is aimed at denying US tax benefits to persons that are “choos[ing] to keep doing business in Russia.”

The proposal grants the Secretary of the Treasury considerable authority in the implementation of the rules. For example, the proposal does not provide any indication of the criteria to be used in determining whether the loss of US tax benefits is merited, leaving it to the Secretary to identify such persons.

Further guidance would also be required in order to determine those persons impacted by the proposal, as the draft language does not define some key terms used, including “control,” “affiliate” and “related to.” Depending on how these terms are defined, the scope of persons affected by the denial of the listed US tax benefits could be extensive.

Taxpayers should consider how the proposal might impact their structures and whether to engage with the legislative process, considering the uncertainty over whether and how quickly the proposal might progress and how it may be modified.

IRS news

IRS issues annual APA report for 2021

The IRS Advance Pricing and Mutual Agreement (APMA) Program issued the 23rd annual Advance Pricing Agreement (APA) report on 22 March 2022, in [Announcement 2022-7](#). The report discusses APMA, including its activities and structure for calendar year 2021, and gives useful insights into the operation of the APA Program.

The number of APA filings increased in 2021, with taxpayers filing 145 APA requests (up from 121 in 2020). The total number of APAs concluded, however, decreased from 127 to 124 and the median of time to finalize an APA increased from 32.7 months in 2020 to 35.1 months in 2021.

APAs with Japan represent more bilateral APAs than any other country at 40% of bilateral APAs executed in 2021. This is attributable to the maturity of the APA Programs in the United States and Japan and the negotiating experience of the APMA team and the competent authority team representing the National Tax Administration of Japan.

Canada is the third most frequently involved treaty partner in executed APAs in 2021 at 7%, as a result of its role as the third largest trading partner with the US (following China and Mexico) and the fact that it has been a US tax treaty partner for almost 80 years.

In addition, the number of India APA requests filed continues to increase steadily, in part as a result of the improved relationship between the IRS and India’s tax authorities during the last several years. In 2021, India represented 16% of bilateral APAs filed, 22% of pending bilateral APAs and 5% of executed bilateral APAs (second only to Japan in all three categories).

New Schedules K-2 and K-3 FAQs released

The IRS in April released eight new Schedules K-2 and K-3 Frequently Asked Questions (FAQs) (Forms 1065, 1120S, and 8865). The FAQs add to previously issued FAQs issued in February. Schedules K-2 and K-3 are new reporting forms that pass-through entities generally must complete, beginning in the 2021 tax year. According to the IRS, the new schedules K-2 and K-3 “improve reporting by standardizing international tax information to partners and flow-through investors, making it easier for them to report these items on their tax returns.”

OECD developments

OECD holds public consultation meeting on Implementation Framework for Pillar Two GloBE Rules

On 25 April 2022, the OECD held a [public consultation](#) meeting on the Implementation Framework for the Pillar Two Global Anti-Base Erosion (GloBE) Rules (the Implementation Framework). The four questions on which the OECD/G20 Inclusive Framework on BEPS was seeking input were outlined in the invitation to provide comments, which was released on 14 March 2022.

The meeting focused on the mechanisms necessary to ensure that tax administrations and Multinational Enterprises (MNEs) can implement and apply the GloBE Rules in a consistent and coordinated manner. Additionally, at the end of the session, the OECD Secretariat addressed some technical questions related to the GloBE Rules.

In total, 75 [comments](#) were provided by professional service providers, businesses, industry associations, and individuals. The EY comment letter submitted to the OECD can be found [here](#).

The consultation meeting highlighted how complex the GloBE Rules are and the importance of a detailed Implementation Framework including simplifications, processes for coordinated interpretations and mechanisms to provide tax certainty. The Inclusive Framework is expected to present the Implementation Framework by the end of this year, which provides only a short timeframe for its development. The OECD Secretariat indicated during the consultation meeting that further refinements to the Implementation Framework will need to continue to be made after the implementation of the GloBE Rules by Inclusive Framework member jurisdictions.

It is important for businesses to evaluate the potential impact of the global tax changes both on their tax positions and on their data and compliance processes and systems. Businesses should also monitor activity in relevant jurisdictions related to the implementation of the global minimum tax rules into their domestic tax legislation.

OECD releases public consultation document on draft rules regarding scope under Amount A for BEPS Pillar One

On 4 April 2022, the OECD Secretariat released a [public consultation document](#) with draft rules regarding scope under Amount A for Pillar One of the OECD/G20 project on *Addressing the Tax Challenges Arising from the Digitalisation of the Economy* (the BEPS 2.0 project).

The document includes draft model rules that once finalized will be the basis for the substantive provisions of the Multilateral Convention, as well as a template for domestic legislation, through which Amount A will be implemented. The document also includes footnotes with descriptions of additional information that will be included in the Commentary that will support the model rules.

The new taxing right established through Amount A only applies to those Multinational Enterprise Groups that fall within the defined scope of Amount A. The scope of Amount A is based on two threshold tests: (i) a global revenue test; and (ii) a profitability test. Both of these tests are to be met for a Group to be considered a Covered Group under the Amount A rules.

Based on the consultation document, the global revenue test requires a Group to have Total Revenues greater than €20 billion. The profitability test is a three-pronged test that is met if the Group's Pre-Tax Profit Margin is: (i) greater than 10% in the Period; (ii) in two or more of the four periods preceding the Period; and (iii) on Average across the Period and the four periods immediately preceding the Period.

The agreement by the Inclusive Framework on BEPS excludes extractives (see article below) and regulated financial services. Furthermore, it has been agreed that segmentation will occur only in exceptional circumstances where, based on the segments disclosed in the financial accounts, a segment meets the scope rules. The consultation document does not include the rules for the industry exclusions or for segmentation. These rules will be released for public consultation later as standalone documents.

The consultation document is a working document released by the OECD Secretariat to obtain input from stakeholders. It was released without prejudice to the final agreement and does not reflect consensus of the Inclusive Framework member jurisdictions on the substance of the document.

If adopted, the application of the draft model rules would have significant implications for companies that are in scope of Pillar One Amount A, affecting the amount of profits to be re-allocated to market jurisdictions and leading to new compliance requirements including requiring a new calculation of a tax base separate from the entity-based domestic tax base calculations.

OECD releases public consultation document on Extractives Exclusion under Amount A for Pillar One

On 14 April 2022, the OECD Secretariat released a [public consultation document](#) regarding the Extractives Exclusion under Amount A for Pillar One of the OECD/G20 project on *Addressing the Tax Challenges Arising from the Digitalisation of the Economy*.

The new taxing right established through Amount A only applies to those Multinational Enterprise Groups that fall within the defined scope of Amount A. The Extractives Exclusion will exclude from the scope of Amount A the profits from Extractive Activities. The definition of Extractives Activities contains two elements: (i) a product test; and (ii) an activities test. Both of these tests must be met for the revenues and profits to be excluded from the Amount A scope determination. This means that the exclusion applies where the Group derives revenue from the sale of Extractive Products *and* the Group has carried out the relevant Exploration, Development or Extraction.

This consultation document covers Schedule [F] of the Model Rules that will govern the Extractives Exclusion. Other parts of the Model Rules on Amount A, on which the corresponding provisions for the Extractives Exclusion would be based, are pending finalization and therefore the Schedule for the Extractives Exclusion provides a preliminary description and explanation of the envisaged draft rules. The consultation document does not include the Schedule on Segmentation or the Schedule that will govern the exclusion for Regulated Financial Services. These Schedules, as well as draft rules on other aspects of Amount A, will be released for public consultation later.

The consultation document is a working document released by the OECD Secretariat to obtain input from stakeholders.

OECD releases ninth batch of Stage 2 peer review reports on dispute resolution

The OECD on 14 April 2022 released the [ninth batch of Stage 2 peer review reports](#) relating to the outcome of the peer monitoring of the implementation by Andorra, Bahamas, Bermuda, British Virgin Islands, Cayman Islands, Faroe Islands, Macau (China), Morocco, and Tunisia (the assessed jurisdictions) of the BEPS Action 14 minimum standard on dispute resolution.

The outcomes of this batch of Stage 2 peer review reports generally demonstrate positive changes across the assessed jurisdictions. According to the peer review reports, Andorra, Bermuda, Faroe Islands, Macau (China), and Morocco have addressed most of the deficiencies identified in the Stage 1 peer review. Bahamas, British Virgin Islands, Cayman Islands, and Tunisia addressed some of the identified deficiencies. The assessed jurisdictions have committed to continue working to resolve the remaining deficiencies identified during the peer review process.

OECD releases fourth annual peer review report on BEPS Action 6 relating to prevention of treaty abuse

The OECD recently released the fourth annual peer review report (the [Report](#)) on the implementation of the BEPS Action 6 minimum standard relating to prevention of treaty abuse.

The main findings show that compliant agreements concluded between members of the Inclusive Framework and covered by the Multilateral Instrument (MLI) have almost doubled from 350 to more than 650 between 2020 and 2021. Also, more than 960 additional agreements will become compliant under the MLI once all relevant signatories have ratified it. Moreover, nearly 70% of the agreements concluded among the members of the Inclusive Framework are being brought into compliance through the MLI.

Finally, under the revised methodology, recommendations were made in this year's peer review to jurisdictions that were requested to formulate a plan for the implementation of the Action 6 minimum standard in agreements which on the assessment date were not yet compliant or subject to a complying instrument, and to those that have signed the MLI but have not yet completed the steps for the entry into effect of its provisions.

EY Member Firm US Tax Desks

Australia	Scott Hes, <i>Sydney</i>	scott.hes@au.ey.com
Bahrain	Joe Kledis, <i>Manama</i>	joe.kledis@bh.ey.com
Canada	George Guedikian, <i>Toronto</i>	george.b.guedikian@ca.ey.com
	Emad Zabaneh, <i>Toronto</i>	emad.m.zabaneh@ca.ey.com
	Asif Rajwani, <i>Toronto</i>	asif.rajwani@ca.ey.com
	Ryan Coupland, <i>Calgary</i>	ryan.coupland@ca.ey.com
	George Tsitouras, <i>Montreal</i>	george.tsitouras@ca.ey.com
	Denis Rousseau, <i>Montreal</i>	denis.rousseau@ca.ey.com
	Richard Felske, <i>Vancouver</i>	richard.e.felske@ca.ey.com
China	Jeremy Litton, <i>Hong Kong</i>	jeremy.litton@hk.ey.com@hk.ey.com
	Lipeng He, <i>Shanghai</i>	lipeng.he@cn.ey.com
	Peter Kao, <i>Shanghai</i>	peter.kao@cn.ey.com
France	Paula Charpentier, <i>Paris</i>	paula.charpentier@ey-avocats.com
Germany	Thomas Day, <i>Munich</i>	thomas.day@de.ey.com
	Dmitri Bordeville, <i>Frankfurt</i>	dmitri.bordeville@de.ey.com
	Ann-Kristin Kautz, <i>Frankfurt</i>	ann-kristin.kautz@de.ey.com
	Lee-Bryan Serota, <i>Frankfurt</i>	lee.b.serota@de.ey.com
Israel	Amir Chenchinski, <i>Tel Aviv</i>	amir.chenchinski@il.ey.com
	Tal Levy, <i>Tel Aviv</i>	tal.levy@il.ey.com
	Itai Ran, <i>Tel Aviv</i>	itai.ran@il.ey.com
Japan	Takayuki Ohta, <i>Tokyo</i>	takayuki.ohta@jp.ey.com
Mexico	Alberto Lopez, <i>Mexico City</i>	alberto.r.lopez@mx.ey.com
	Manuel Solano, <i>Mexico City</i>	manuel.solano@ey.com
Singapore	Michael Xiang, <i>Singapore</i>	michael.xiang@sg.ey.com
Sweden	Russell Antonevich, <i>Stockholm</i>	russell.antonevich@se.ey.com
Switzerland	Michael Parets, <i>Zurich</i>	michael.parets@ch.ey.com
United Kingdom	Noah Lewis, <i>London</i>	noah.lewis1@uk.ey.com
	Joseph Toce, <i>London</i>	jtoce@uk.ey.com
	Sean Trahan, <i>London</i>	sean.trahan@uk.ey.com
	Leif Jorgensen, <i>London</i>	ljorgensen@uk.ey.com
	Jillian Symes, <i>London</i>	jsymes@uk.ey.com

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