A NOTE FROM THE

EDITOR-IN-CHIEF

What Is My Basis? New OECD Guidance Clarifies GloBE Carrying Value Determinations

By Brian Jenn

One of the most vexing questions taxpayers have faced since the Organization for Economic Cooperation and Development ("OECD") issued the Global Anti-Base Erosion ("GloBE") Model Rules in December 2021 is how to determine the GloBE "carrying value" of their assets. Knowing GloBE carrying value, which is GloBE parlance for "tax basis," of a constituent entity's assets is essential since amortization and depreciation of such assets are taken into account in determining GloBE income and loss. Differences between amortization taken into account for GloBE purposes and regular tax purposes can contribute to a multinational enterprise ("MNE") Group having a jurisdictional effective tax rate ("ETR") below 15% and resulting in Top-Up Tax liability, unless utilization of a GloBE deferred tax asset ("DTA") results in the constituent entity being deemed to pay additional Covered Taxes that offset the impact of amortization or depreciation on the jurisdictional ETR.

The GloBE Model Rules provide some basic guidance on the determination of GloBE asset carrying value at the beginning of the Transition Year[1] and following certain asset and stock acquisitions. As a general matter, under Articles 3.1.2 and 3.1.3, the starting point for determining GloBE income or loss is the relevant financial accounts of the MNE Group,[2] with the consequence that the asset carrying value in those financial accounts is also the starting point for determining GloBE carrying value, although for GloBE purposes purchase accounting adjustments in those financial accounts are disregarded. Articles 6.2–6.3 provide rules for determining asset carrying value after a stock or asset acquisition.

Although the GloBE Model Rules provide a starting point for determining GloBE carrying value, they also leave questions unanswered or with seemingly unsatisfactory answers that could lead to double taxation. In particular, Article 6.3.1 provides that following an asset acquisition (which would require the inclusion of gain or loss in the seller's GloBE income), the acquiror takes a GloBE

BRIAN JENN is a Partner in the Chicago office of McDermott Will & Emery LLP.

carrying value based on the acquiror's carrying value of the assets under the Ultimate Parent Entity's ("UPE's") consolidated financial statements. Because an asset transfer within a consolidated group may be accounted for *at cost* under U.S. generally accepted accounting principles ("GAAP") "common control" rules or other financial accounting standards, Article 6.3.1 presented the possibility that the disposing entity would recognize gain in GloBE income, but the acquiring entity would not enjoy a step-up in GloBE carrying value.

For acquisitions during and after the Transition Year, the full suite of rules under Articles 6.2 and 6.3 will apply to address GloBE carrying value in, among other transactions, stock acquisitions treated as asset acquisitions, GloBE reorganizations, and certain situations where a local tax step-up is allowed or required.

GloBE Administrative Guidance issued in June 2024 ("June 2024 AG") finally addresses the issues related to double taxation in intra-group asset transfers and also clarifies issues related to the determination of GloBE carrying value, as well as GloBE DTAs and deferred tax liabilities ("DTLs"), for assets acquired before the Transition Year. The remainder of this column describes the current state of play in the determination of GloBE carrying value for assets acquired (1) before December 2021, (2) after November 2021 and before the Transition Year, and (3) in the Transition Year or thereafter.

Assets Acquired Before December 2021

Articles 6.2 and 6.3 provide a host of rules for determining GloBE carrying value in the context of stock and asset dispositions and acquisitions. These include Article 6.2.2 (stock acquisitions treated as asset acquisitions for local tax law), Articles 6.3.2 and 6.3.3 (GloBE Reorganizations), and Article 6.3.4 (election to align carrying value under the GloBE rules with outcomes under local tax law). Significantly, the June 2024 AG clarifies that none of the rules in Articles 6.2 and 6.3, save one, applies to acquisitions prior to the Transition Year.

Because Articles 6.2 and 6.3 are generally disregarded for assets acquired before November 30, 2021, the GloBE carrying value of such assets generally will correspond to the historic carrying value of the assets in the UPE's consolidated financial statements.[3] Further, the June 2024 AG clarifies that where the assets were acquired by the MNE Group in a stock acquisition, Article 6.2.1(c) applies with the result that the target will determine its GloBE income or loss and Adjusted Covered Taxes using its historical carrying value of its assets—*i.e.*, the historical carrying value the target had in its consolidated financial accounts at the time the entity was acquired.[4]

Using the historic carrying value of assets in the MNE Group's financial accounts may be disadvantageous where the asset has been transferred within the MNE Group in a transaction in which gain was recognized for local tax purposes, but the transaction was accounted for at cost under the MNE Group's financial accounting standard. Nonetheless, if the acquiror obtained a basis step-up for local tax purposes, there likely would have been a DTA for financial accounting purposes that would become a GloBE DTA that ultimately increases Covered Taxes as the local tax amortization is taken into account.

In particular, under Article 9.1.1, if there is a DTA or DTL in the financial accounts of a constituent entity for the Transition Year based on the difference between the local tax basis of an asset and the financial accounting carrying value (which will equal the GloBE carrying value), then the DTA or DTL becomes a GloBE DTA or DTL. That GloBE DTA or DTL will be taken into account in determining the Deferred Tax Adjustment Amount under Article 4.4 for the relevant jurisdiction. That is, as the DTA or DTL "reverses" or is utilized, the constituent entity will be deemed to pay additional Adjusted Covered Taxes so that, for instance, tax amortization that exceeds book amortization (and thus GloBE amortization) in a particular year will not have the effect of lowering the GloBE ETR.

Assets Acquired After November 2021 and Before the Transition Year

As in the case of assets acquired before December 2021, Articles 6.2 and 6.3 (except for Article 6.2.1(c)) do not apply for determining the carrying value of assets acquired after November 2021 and before the Transition Year. Accordingly, the GloBE carrying value of such assets will generally correspond to the historic carrying value in the UPE's consolidated financial accounts or in the financial accounts of an entity acquired by the MNE Group during this period.

As in the case of a pre-December 2021 asset acquisition, the lack of a step-up in carrying value in a taxable asset acquisition occurring after November 2021 and before the Transition Year could have a negative impact on the MNE Group's GloBE ETR for the relevant jurisdiction. Although there is also the possibility of a GloBE DTA to offset this negative impact, the availability of a GloBE DTA is subject to Article 9.1.3, which limits the ability of an MNE Group to import a financial accounting DTA into the GloBE system in an acquisition occurring during such period.

Although Article 9.1.3 provides without qualification that an acquiror of assets between December 2021 and the Transition Year takes the *transferor's* financial accounting carrying value as its GloBE carrying value, Administrative Guidance under Article 9.1.3—as clarified by the June 2024 AG—allows the MNE Group to take into account a GloBE-only DTA to the extent the seller paid local tax on the transfer or utilized a DTA.[5] The June 2024 AG also clarifies that the GloBE DTA under Article 9.1.3 arises regardless of whether there would be a DTA under the relevant financial accounting standard.

Assets Acquired During and After the Transition Year

For assets acquired during and after the Transition Year, the June 2024 AG includes the important guidance—noted in the introduction—that the acquiring constituent entity will take a GloBE carrying value determined in accordance with Article 3.2.3, which provides that transactions must be consistent with the arm's length principle.[6] As a result, the acquiring entity generally will take a GloBE carrying value that is stepped up to the arm's length value/acquisition price, thereby avoiding the potential for double tax on a future disposition of the asset (or as a result of local tax amortization or depreciation exceeding that allowed for GloBE purposes).

In light of the special rule allowing stepped-up GloBE carrying value, the June 2024 AG also provides corresponding rules regarding the calculation of a GloBE DTA or DTL for an asset acquisition during or after the Transition Year. In particular, under these circumstances, any GloBE DTA or DTL taken into account in determining the Deferred Tax Adjustment Amount under Article 4.4 must be determined based on the difference between the GloBE carrying value and local tax basis, rather than between the financial accounting carrying value and local tax basis.[7]

For acquisitions during and after the Transition Year, the full suite of rules under Articles 6.2 and 6.3 will apply to address GloBE carrying value in, among other transactions, stock acquisitions treated as asset acquisitions, GloBE reorganizations, and certain situations where a local tax step-up is allowed or required. The application of these rules in certain transactions where a step-up is allowed for U.S. tax purposes (*e.g.*, an election under Code Sec. 338 or 754) can be uncertain and may be the subject of a future column.

ENDNOTES

1 Generally speaking, the Transition Year for a constituent entity with respect to a particular jurisdiction is the first year that the MNE Group is subject to the GloBE rules with respect to that jurisdiction. For a jurisdiction with respect to which the MNE Group satisfies the country-by-country reporting safe harbor, the Transition Year is the first year in which the MNE Group no longer qualifies for that safe harbor with respect to that jurisdiction.

2 The consolidated financial accounts prepared by the Ultimate Parent Entity ("UPE") on behalf of the MNE Group will generally be the relevant financial accounts for this purpose, although a jurisdiction implementing a QDMTT may choose under some circumstances to utilize a local financial accounting standard for purposes of determining the QDMTT base.

3 June 2024 AG, section 2.1, paragraphs 4 and 5.

4 June 2024 AG, section 2.1, paragraph 39.

5 June 2024 AG, section 2.1, paragraph 50. No DTA is created if the acquiring entity is permitted under paragraph 10.9 of the Commentary to Article 9.1.3 to use its own accounting carrying value for GloBE purposes.

6 June 2024 AG, section 2.1, paragraph 43.

7 June 2024 AG, section 2.1, paragraph 35.