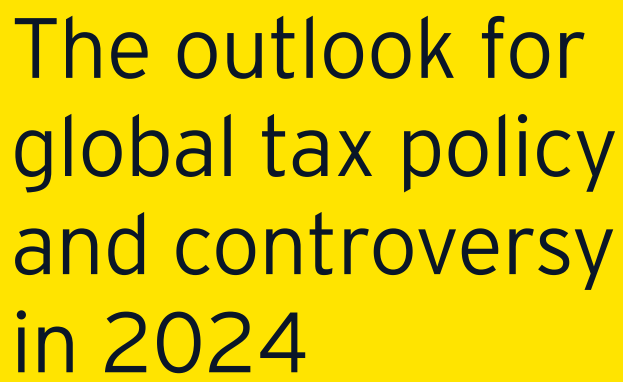

The outlook for global tax policy and controversy in 2024

How to find certainty amid tax policy transformation

With so much tax change unfolding, the 2024 EY Tax Policy and Controversy Outlook explores what you should act on now and what you should keep your eye on next.

Is a more stable international tax system on the horizon as governments coordinate more than ever before? How will Pillar Two[1] affect tax incentives, even for companies not subject to its rules? How will increasing transparency influence the development of new tax policies?

Around the world, governments are actively evaluating and implementing tax reforms developed in global discussions. "Companies cannot wait for these interconnected provisions to be finalized everywhere before addressing the implications for their businesses. Complying with BEPS 2.0 Pillar Two rules, satisfying new transparency requirements and preparing for future controversy require action now," says Barbara Angus, EY Global Tax Policy Leader.

Further transformation is ahead as governments consider digital taxes, modification of other tax rules in light of Pillar Two, and broader tax reforms to further their policy objectives and meet their revenue needs. All this activity will have long-term implications for the international tax environment and the global economy.

"Major intertwined tax developments continue to evolve and it's the companies that see the whole picture in real time that will navigate successfully," says Marna Ricker, EY Global Vice Chair of Tax. "Both businesses and tax authorities value certainty, especially in a time when not only tax policy and administration, but also business and technology, are changing rapidly. Putting the people and systems, particularly around data and technology, in place to anticipate and adapt to this new environment will be key to realizing that certainty."

These and other developments are addressed in this article, reflecting observations by EY Tax professionals in 75 jurisdictions gathered in the annual EY *Tax Policy and Controversy Outlook* survey at the start of 2024. This article examines the trends found in the contributors' projections for 2024 at the global, regional and national levels. Detailed reports for all 75 jurisdictions are available for those interested in more information.

[1] Formally, the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS) project on addressing the tax challenges of the digitalization of the economy.

On today's tax agenda

Pillar Two is live

Pillar Two is intended to create a coordinated system of taxation requiring large multinational entities (MNEs) to pay a minimum level of tax (an effective tax rate (ETR) of 15%) on the income arising in each of the jurisdictions where they operate. Many jurisdictions have now incorporated Pillar Two rules into their domestic law, and many more are working toward implementation.[2] With Pillar Two legislation enacted, governments are continuing to flesh out technical details and developing the administrative procedures for compliance. Additional administrative guidance clarifying and expanding upon the agreed Pillar Two model rules and commentary is being developed in the Inclusive Framework for incorporation by jurisdictions into their domestic law and guidance. In addition, the Inclusive Framework will conduct peer reviews of each jurisdiction's enacted Pillar Two rules to determine their alignment with the agreed rules and then turn its attention to how jurisdictions are applying the rules in practice. Even as these ongoing developments continue to unfold, there are actions for companies to take now to prepare.

"Perhaps the most significant action businesses can take today is to evaluate and prepare for potential use of the transitional safe harbor based on country-by-country reporting (CbCR). This safe harbor allows for more simplified calculations and adjustments to financial income and taxes than would be required under the Pillar Two rules, and thus reduces administrative complexity in the jurisdictions where a company meets the conditions for its application," says Matt Andrew, EY Asia-Pacific Tax Policy Leader. The CbCR safe harbor is available for three years, but businesses must use it for a jurisdiction in the first year or they lose the option for that jurisdiction permanently, so action now is critical.

Determining the availability of and applying the safe harbor requires a data exercise distinct from what is required for application of the Pillar Two rules beyond the safe harbor. "Starting now with full Pillar Two calculations for the subset of jurisdictions where the conditions for the safe harbor are not met will highlight the types of data that ultimately will be needed for all jurisdictions," says Kevin Flynn, EY Americas Tax Leader. "This will enable companies to scope out the process and systems changes that will be necessary for Pillar Two reporting and compliance and determine the personnel outside the tax department who will need to be part of the Pillar Two project team."

This wave of global tax change further heightens the need for tax certainty. "Achieving tax certainty is an ongoing process," says Luis Coronado, EY Global Tax Controversy Leader. "What we are seeing occur today is a move away from exclusively fire-fighting individual disputes, toward a more proactive approach where risks are identified, assessed and managed earlier in the controversy lifecycle to reduce the occurrence and lessen the magnitude of future disagreements."

Transparency cascades

Not only is CbCR data taking on new relevance under Pillar Two, but the data is now subject to public disclosure requirements in the European Union (EU). Australia is also planning to require public CbCR as of 1 July 2024.

According to the 2024 *EY International Tax and Transfer Pricing Survey*, 96% of the senior tax and finance executives surveyed expect additional work to prepare their CbCR data for public disclosure. "The information found in the reports can be difficult to understand and easy to misinterpret. Accuracy and completeness of data in the CbCR is paramount, and businesses need to be ready to explain what those numbers mean," says Rocio Reyero Folgado, EY EMEIA Tax Leader. "As considerable time goes into preparing these reports, businesses should also think about how else they can use the information gathered," she continued.

The data required for reports may be used by businesses to glean new insight into their operational profile, which can be leveraged to make structural and process improvements. Businesses also can use the information proactively in communications with external stakeholders about their role in and contribution to local economies.

Tax administrations are increasing their own transparency, too, revealing more about their expectations and priorities. Businesses can use this information to be more proactive in getting ahead of potential controversy. Examples include the publication by many countries of annual audit strategy documents or the use of compliance guidelines, such as the Australian Practical Compliance Guidelines and the UK's new Guidelines for Compliance program.

[2] Track all the latest legislative updates with the EY BEPS 2.0 – Pillar Two Developments Tracker.

Growing emphasis on tax governance and cooperative compliance

"How a business invests in and manages its global and local tax governance is increasingly critical as more tax administrations consider governance as a way to risk-rate taxpayers and determine the level of review and intervention," says Martin Caplice, EY Asia-Pacific Tax Controversy Leader. This approach – which is sometimes described as compliance assurance or justified trust – helps tax administrations meet several related objectives aimed at reducing the overall number of tax issues that ultimately turn into disputes.

A resurgence in cooperative compliance arrangements is expected in 2024, particularly as companies seek additional certainty with respect to new Pillar Two rules. These programs involve the taxpayer and tax administration working in a collaborative way throughout the year to review transactions that will eventually flow through to the tax return. Such transactions are then excluded from audit, streamlining the compliance process and, in theory, reducing the amount of time it takes to close a tax year. While these programs have been around for some time, many tax administrations are now looking at their adoption or expansion. For example:

- Italy is radically overhauling and expanding its program.
- Japan is piloting a new compliance assurance program.
- Several tax administrations in Latin America are exploring pilot programs.

What to keep your eye on next

Adapting to the new Pillar Two environment

The full effects of Pillar Two will continue to build over the next several years, with additional jurisdictions acting on implementation, the transitional safe harbors scheduled to phase out and broad application of the Under-taxed Profits Rule (UTPR) set to begin in 2025.

Rolling implementation

It will be important for companies to monitor Pillar Two developments in all jurisdictions that are relevant to their businesses. They will be subject to rules that come online at different times and that reflect technical differences – potentially significant differences. Moreover, the interconnectedness of the global minimum tax framework means that Pillar Two implementation in one country will affect a company's Pillar Two outcomes in other countries. This will need to be factored into supply chain structuring, acquisition due diligence and broader business planning. Tax policymakers and tax administrations similarly will need to follow developments in other jurisdictions because of the effects on the operation of their own Pillar Two rules and the revenue that their rules will bring in.

Rethinking incentives

The implications of Pillar Two for tax incentives will be a significant consideration for companies and for governments. "Tax incentives are a powerful government policy lever, but the effectiveness of many tax incentives will be eroded by the potential application of other jurisdictions' Pillar Two rules to impose top-up taxes that reduce or eliminate the benefit provided. As governments look at other policy approaches for encouraging the investment they seek and companies evaluate the shifting global environment in which they operate, constructive engagement between policymakers and business representatives will be invaluable," says Eng Ping Yeo, EY Asia-Pacific Tax Leader.

Bolstering sustainability

Pillar Two has particular ramifications for sustainability, as tax incentives have been a key tool for governments in encouraging green behavior. Governments may instead place more emphasis on new or increased use of targeted taxes to meet their sustainability goals. Windfall taxes on the energy sector, plastic packaging taxes and carbon border adjustments (CBAMs) have burgeoned in recent years and new climate-focused taxes could continue to emerge. This kind of shift affects companies' plans for achieving their own sustainability commitments, which underscores the importance of continuing dialogue in this policy area.

New controversy

The technical complexity of the Pillar Two rules, combined with the way the rules of multiple countries can apply to the same income, compels companies and tax administrations to anticipate future controversy. Because Pillar Two rules are being implemented through domestic legislation without any overarching multilateral instrument, discussion in the Inclusive Framework on dispute prevention and resolution has focused largely on how existing mechanisms could be used. Companies are prudently looking at how putting advanced pricing agreements (APAs) in place now can create a foundation that will help reduce Pillar Two issues in the future. "As well as APAs and other advance certainty procedures, companies may want to look at the Organisation for Economic Co-operation and Development (OECD) International Compliance Assurance Program (ICAP) as a tool that could potentially provide some Pillar Two certainty on a multilateral basis by proactively identifying and resolving potential tax issues. And it can help build relationships with tax authorities along the way," says Joel Cooper, EY Global International Tax and Transaction Services Controversy Leader.

The repercussions of Pillar One

Pillar One has advanced more slowly than Pillar Two, with 2024 expected to be a pivotal year for this work on new profit allocation rules for MNEs.

Amount A and digital services taxes (DSTs)

The centerpiece of Pillar One is a formulaic approach designed to increase the share of taxing rights over global business income assigned to market jurisdictions, which is known as Amount A. This is coupled with elimination of DSTs and similar measures. Although the original Amount A concept focused on digital business activity, it is now structured to apply to MNEs that meet the specified revenue and profitability thresholds generally without regard to industry or business activity. In contrast, while the commitment not to impose DSTs is conditioned on Amount A entering into effect, it applies to all MNEs.

The Inclusive Framework has developed a Multilateral Convention (MLC) through which Amount A is to be implemented, but there are specific areas where jurisdictions have differing views that must be resolved for the MLC to be finalized. The Inclusive Framework is now aiming to have a signing ceremony for an agreed MLC by the end of June 2024. Amount A (and, therefore, the requirement to eliminate DSTs) is to enter into force only when a critical mass of jurisdictions have completed all the necessary steps to ratify the MLC and have made any necessary changes to their domestic law. As defined in the MLC, these conditions cannot be met without the United States, which is headquarters for a preponderance of the MNEs in scope of Amount A. US implementation would require action by both the Presidential administration, which has been actively involved in advancing Amount A, and Congress, where opposition has been strongly voiced by some. Moreover, Amount A is not likely to be ripe for action beyond the MLC signature stage until after the 2024 US elections, further complicating predictions on US participation.

"The technical, procedural and political hurdles that remain are extremely challenging, and pressure is mounting for a reckoning on Amount A, which could come this year," says Angus. The Inclusive Framework's standstill agreement on enactment of new DSTs expired as of the end of 2023. Canada is moving forward with announced plans to implement a DST in 2024 with potential retrospective effect from 2022. New Zealand has proposed a DST, and other countries are exploring their options in this area. More broadly, jurisdictions that are dissatisfied with the current rules for allocating global business income and are growing increasingly impatient with progress in the Inclusive Framework may resort to unilateral approaches for imposing tax on additional income, including by incorporating concepts from the global discussions. These kinds of potential responses have far-reaching implications for MNEs, regardless of industry or whether they would be in scope of Amount A.

The other element of Pillar One

Pillar One's Amount B provides for a system of fixed returns on baseline marketing and distribution activities, intended to operate within the traditional transfer pricing framework through incorporation in the OECD Transfer Pricing Guidelines. In contrast to Amount A, Amount B is not subject to scope thresholds and its rules apply to the covered transactions of any MNE.

As of February 2024, Amount B has moved ahead of Amount A, with the Inclusive Framework's release of an agreed report on the Amount B approach and its incorporation into the Guidelines. Although the report describes some work that is still ongoing, the Amount B approach can be applied by jurisdictions beginning in 2025. Jurisdictions can choose whether to apply Amount B, and the pricing results under Amount B will not be binding on a non-adopting jurisdiction. Those jurisdictions that choose to apply it have a further option to treat it as a taxpayer safe harbor election or as mandatory for transactions in scope. The level of enthusiasm for Amount B has varied widely across jurisdictions, so it remains to be seen whether, when and how individual jurisdictions apply Amount B. Although its objective is to reduce disputes over marketing and distribution returns, the optionality that is built into Amount B could mean that it becomes a new source of controversy.

The future of tax controversy

Around the world, audit activity is expected to intensify in 2024. Disputes will continue to be increasingly granular, calling for more voluminous documentation and involving more specialized teams and technologies within tax administrations.

The focus of tax authorities on cross-border tax issues will continue to grow, including particular focus on transfer pricing for intangible property, embedded royalties, intra-company financial transactions, and deductible payments to low- or no-tax jurisdictions. And even with the advent of a new global minimum tax, there is not yet any sign of a significant move toward jurisdictions' reducing their use of specific anti-abuse rules.

Tax compliance will continue to require businesses to produce more detailed documentation, to be delivered in shorter timelines. That information will be combined with information exchanged with other tax administrations and other governmental departments. "We are seeing the exchange of information having a tangible effect in tax enforcement," says Jean-Pierre Lieb, EY EMEIA Tax Policy and Controversy Leader. "Businesses are seeing information or arguments put forward during the course of an audit that could only have come to the tax administration from outside sources."

Even as tax authorities are conducting more detailed tax audits and applying penalties more frequently, many are seeking to create more open and collaborative relationships with businesses. We see several trends in cooperative compliance approaches that are likely to expand or accelerate in 2024:

- Voluntary tax governance programs will likely move, over time, to a mandatory basis, particularly for the largest businesses in an economy.
- Both mandatory compliance assurance programs and voluntary cooperative compliance programs will start to encompass a greater number of businesses within their scope.
- Stronger links will form between tax governance and penalty treatment — with tax administrations potentially offering more lenient treatment to taxpayers demonstrating otherwise strong governance in tax.

Regional tax trends and expectations

Local tax reforms in the Americas

Governments in the Americas are discussing Pillar Two and related policies, but few have announced firm intentions. In the region, a wide variety of tax reforms have been recently enacted or are currently underway. In a novel move, Ecuador enacted an optional tax increase for taxpayers seeking tax stability. Taxpayers that increase their effective income tax rate by two percentage points will not be affected by any future tax reforms for up to five years. Additionally, Ecuador enacted a variety of investment and employment incentives and tax debt penalty and interest amnesty, with a VAT increase under debate.

Chile is considering a new tax reform package (after the 2022 bill was rejected), including transparency reform, a corporate tax rate decrease (from 27% to 25%), implementation of Pillar Two rules, R&D and small and medium-sized entity investment incentives and measures to address tax evasion and avoidance.

The first phase of Brazilian tax reform was approved in 2023, including replacement of the existing five VAT taxes with two main taxes after a transition phase. An increase in litigation at the outset is anticipated, until the understanding of the new concepts and procedures in this legislation becomes settled. A second phase of tax reform is expected in early 2024, with details that flesh out previously approved measures and a corporate income tax proposal that may include Pillar Two provisions.

The US is still addressing implementation of the 2022 *Inflation Reduction Act*, including the development of detailed guidance on the green energy tax credits and the corporate alternative minimum tax. The upcoming expiration of major provisions of the 2017 *Tax Cuts and Jobs Act* is expected to be a focus of discussion, in preparation for potential legislative action beyond the 2024 elections.

Policy and enforcement innovation continue in Asia-Pacific

Jurisdictions in Asia-Pacific were some of the first to adopt Pillar Two and many are now considering options for changing tax incentives and adopting nontax incentives to remain competitive in a Pillar Two world.

Many jurisdictions in the region are under pressure to collect tax shortfalls or reduce debt. Accordingly, several jurisdictions are expected to increase audit activity. Transfer pricing is expected to remain the leading tax risk in the region in 2024. Jurisdictions also continue to invest heavily in tax administration technology, including e-invoicing and other digital tax administration enhancements.

Asia-Pacific jurisdictions continue to be at the forefront of factoring tax governance into classification of taxpayers by risk level. Several jurisdictions are adopting new programs or expanding existing programs. Singapore and Malaysia are encouraging taxpayers to participate in their relatively new voluntary programs, and New Zealand is expanding its focus on governance in 2024.

Change rippling through Europe, the Middle East and Africa

There was a flurry of legislative activity at the end of 2023 as most EU Member States transposed the EU Minimum Tax Directive into domestic legislation. Several other jurisdictions in the region have also enacted Pillar Two legislation. And across the region, there are additional jurisdictions that have legislation moving through the process or have announced their intention to implement the Pillar Two rules.

The European Commission has stated that agreement on VAT in the Digital Age is a top priority and agreement is expected soon. Negotiations are continuing on the Faster and Safer Relief of Excess Withholding Taxes (FASTER) proposal and may reach conclusion in the first half of 2024. Public consultations on the Transfer Pricing Directive and the Business in Europe: Framework for Income Taxation (BEFIT) proposals closed in January 2024 with extensive comments received; for each of these proposals, the path forward remains unclear. While there have been extensive negotiations around the Unshell proposal, no agreement has been reached.

Windfall taxes are still a topic of discussion in the region, with several energy and bank windfall taxes in effect. Ukraine has newly adopted a 50% tax on the windfall profits of banks in the 2023 tax year (i.e., retrospectively).

The transitional phase of the EU CBAM began in October 2023, with importers of goods now required to submit quarterly reports on "embedded emissions" in imported goods. The United Kingdom has confirmed that it will also implement a CBAM by 2027.

In an effort to attract business, Saudi Arabia is offering a 30-year tax relief package, including a 0% rate on corporate income tax and on withholding tax, for approved regional headquarters activities in Saudi Arabia.

South Africa is conducting a comprehensive review of all corporate tax incentives, with a view to broadening the tax base. However, in the short term, increased revenue is expected from stronger enforcement and enhanced compliance, rather than significant structural tax changes.

Looking ahead

As companies and tax administrations work through this current period of tax change, it is important to continue to look ahead as experience gained now can help shape what will follow. There are plans to follow the Pillar Two work with a project to identify complexities in the international tax system that can be eliminated as unnecessary in a global minimum tax world. At the jurisdiction level, policymakers will focus on how best to meet their revenue needs and achieve their policy objectives within the new global tax framework that is built on unprecedented coordination. And tax authorities will need to harness new technology while broadening and deepening their cooperative relationships in order to do the job of tax administration as effectively and efficiently as possible. Across all of these dimensions, constructive involvement by businesses will be invaluable.

As we look ahead, there is ongoing focus on making sure that the global dialogue about tax is one that captures the full range of perspectives. The Inclusive Framework has extensive plans for future work. The United Nations is developing a framework convention for international tax cooperation. Regional tax organizations are becoming more active as well. All of these discussions will be enhanced with the inclusion of business input. Ensuring that the discussions are brought together in a collaborative way will enrich the outcomes for the global economy.

"We are reaching the point where businesses and governments alike need to shift from preparing for change to the practical aspects of applying and administering the new rules," says Ricker. "Businesses should continue to engage with policy makers and tax authorities as the technical details are fleshed out and procedural requirements are established," agreed Angus. "And as always, keep the horizon within your sights as the actions you take today position you to tackle the further tax change yet to come," Ricker concluded.

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