

# NEWS REPORT: THE RELEVANCE OF A QDMTT FOR CURAÇÃO

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## 1. INTRODUCTION

The profound impact of rapid digital transformation on economies and societies has sparked global discussions across legal and regulatory sectors, including international tax. In the current global economy, traditional income tax rules, initially designed for conventional physical businesses, face challenges in addressing the complexities of the digital era. While these rules were established to ensure tax certainty and prevent double taxation, digitalization has led to challenges due to intangible value creation and remote market access. This has enabled multinational enterprises (MNEs) to exploit loopholes and shift profits to low-tax jurisdictions.

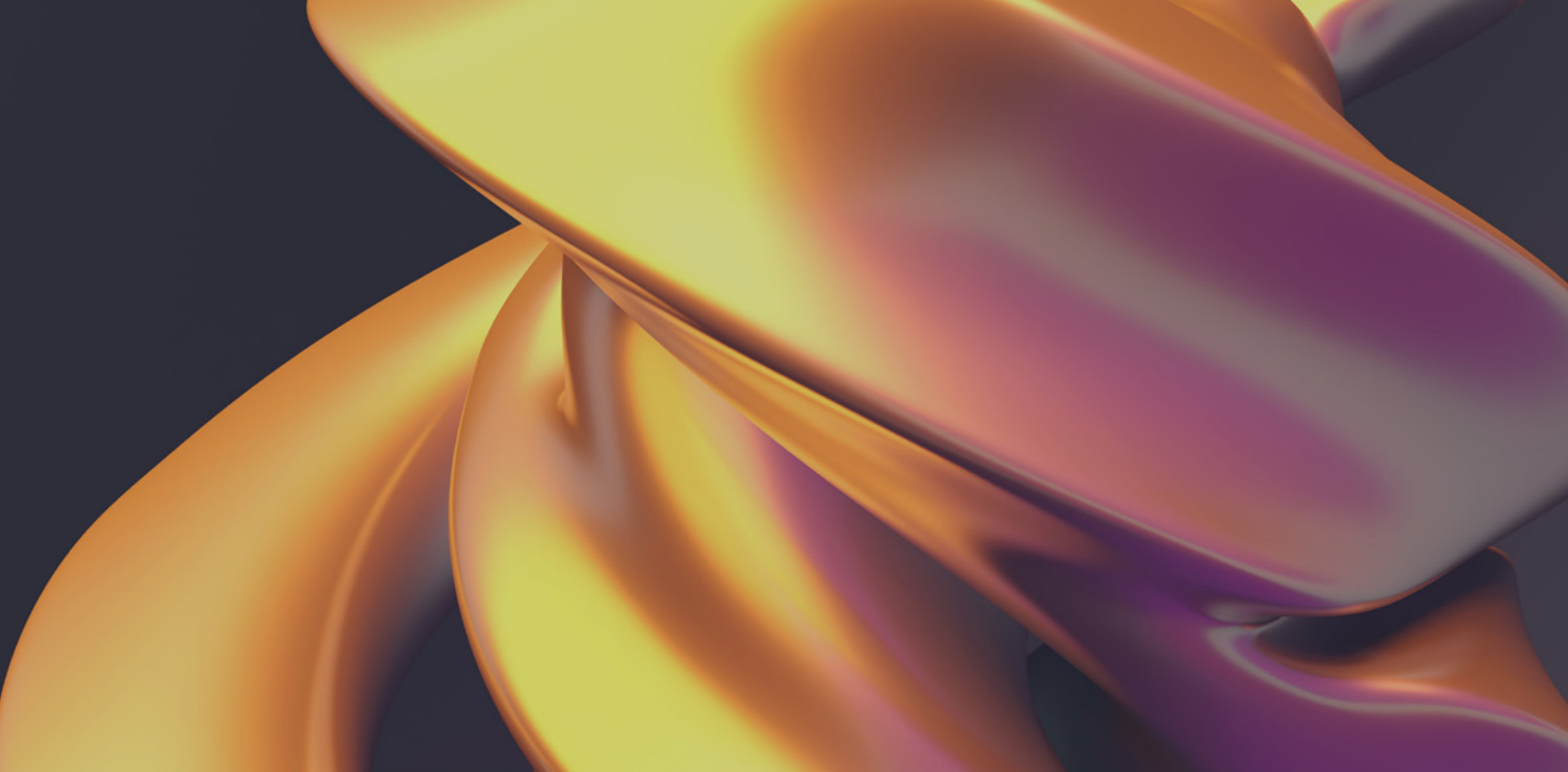
In response to these challenges, the Organization for Economic Cooperation and Development (OECD) has taken a proactive approach by introducing Pillar Two, a groundbreaking initiative to reform international tax frameworks to adapt to the realities of the digital economy. The Pillar Two model rules, unveiled in December 2021 as part of the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS) project, represents a crucial step towards limiting worldwide tax avoidance by imposing a global minimum effective tax rate on excess profits generated by MNEs across jurisdictions.

As a member of the OECD/G20 Inclusive Framework, Curaçao also agreed to a coordinated system of Global Anti-Base Erosion (GloBE) Rules that are designed to ensure the MNEs pay at least 15% tax on the profits arising in each jurisdiction where they operate.<sup>1</sup>

This news report discusses the content of Pillar Two, specifically the Qualified Domestic Top-Up Tax (QDMTT) and its relevance for Curaçao.

## 2. QDMTT

Pillar Two ensures a minimum Effective Tax Rate (ETR) of 15% in each jurisdiction. If the ETR calculated based on the GloBE Rules (GloBE ETR) is less than the 15% global minimum rate, the calculation of top-up tax is required. Top-up tax differs from taxes imposed by traditional income tax regimes. Traditional income taxes are generally based on specified tax rates applied to the taxable profit of an entity. In contrast, the top-up tax becomes applicable only when MNE group entities pay insufficient income taxes in a specific jurisdiction. This top-up tax may be enforced through the Income Inclusion Rule (IIR) or the Undertaxed Profits Rule (UTPR) based on the GloBE Rules. Countries also have the option to introduce a QDMTT in their jurisdiction. Based on the IIR and the UTPR, a jurisdiction other than the one with a GloBE ETR of less than 15% is given the authority to levy up to 15%. The jurisdiction with a GloBE ETR of less than 15% can prevent the imposition of a top-up tax under the IIR or UTPR by implementing a QDMTT.



The QDMTT is a minimum tax implemented into the domestic law of a jurisdiction. It is intended to assess the excess profits of entities that fall within the scope of Pillar Two (Constituent Entities) in a manner consistent with the GloBE Rules. For a QDMTT to be recognized, it must reflect the calculation and assessment methods of the GloBE Rules without additional benefits. In the situation that the domestic minimum tax qualifies as a QDMTT within the meaning of the GloBE Rules, all payments made under it will be fully credited against the obligations under Pillar Two. If the QDMTT is equal to the top-up tax (as it is intended to be), there will be no top-up taxes imposed in other jurisdictions. Therefore, levying QDMTT rearranges the order in which jurisdictions can impose the top-up tax if a jurisdiction's ETR falls below the global minimum rate of 15%.

A jurisdiction with a QDMTT has priority in receiving this additional tax income from entities within its borders, diverting income that would otherwise go to other countries under the IIR and the UTPR.

For MNEs, this means that the QDMTT determines where the top-up tax is paid without changing the amount of the top-up tax.

### **3. SHOULD CURAÇAO IMPLEMENT A QDMTT?**

The Pillar Two GloBE Rules will apply to MNEs with a consolidated group turnover of EUR 750 million or more in at least two of the last four consecutive fiscal years.<sup>2</sup> This concerns the turnover in accordance with the consolidated annual accounts of the Ultimate Parent Entity (UPE). Companies based in Curaçao that currently submit a Country-by-Country notification will most likely fall within the scope of Pillar Two, requiring them to have a GloBE ETR of at least 15%.

The GloBE ETR is calculated by dividing the Adjusted Covered Taxes by the GloBE Income (or Loss).<sup>3</sup> The Adjusted Covered Taxes and the GloBE income are calculated based on the GloBE Rules, which may not be necessarily the same as the tax accounting principles currently applicable in Curaçao for determining the

ETR. Due to the discrepancies between the two calculation methods, the GloBE ETR in Curaçao can be lower than 15% even if, the effective tax rate is 15% according to the tax accounting standards applicable. For example, since the tax year 2023, Curaçao has implemented a profit tax rate of 15% on taxable income up to NAf. 500,000 (22% rate on income exceeding NAf. 500,000). Consequently, it is likely that the GloBE ETR will be less than 15% in Curaçao. Moreover, based on the territoriality regime of Curaçao only the domestic profit is taxed, with a starting profit tax rate of 15%. Plus, Curaçao has several tax regimes that qualify for a profit tax rate of 3%, along with other regimes such as the innovation box (0%). In sum, the GloBE ETR in Curaçao is quite likely to fall below 15%. Currently, Curaçao lacks specific legislation in the context of Pillar Two. Therefore, only the additional tax methods outlined in the GloBE Rules, namely the IIR and the UTPR, apply. In other words, the jurisdiction of the UPE has the right to impose the top-up tax under the IIR. In such cases, the top-up tax is levied in other jurisdictions on the excess profits of the MNE group entities based in Curaçao. In this context, the question arises as to why Curaçao does not introduce a QDMTT. In cases where the GloBE ETR of Constituent Entities is less than 15% within Curaçao, potential tax income from Curaçao will flow abroad if there is no QDMTT in Curaçao. Therefore, if Curaçao chooses to implement a QDMTT, it is crucial to have comprehensive knowledge of the calculations involved in determining the GloBE ETR and the top-up tax amount.

#### **4. QDMTT AND CURAÇAO'S COMPETITIVENESS**

Prior to Pillar Two, jurisdictions could compete without any restrictions regarding their tax rate, which is the so called "race to the bottom." For example, in a competition for inbound investments from an MNE, it was possible that this type of tax competition could lead to zero tax on profits. With Pillar Two, profit tax competition of MNEs is effectively limited to 15% of excess profit as defined by the GloBE Rules. Still, it is not expected that implementing a QDMTT will put Curaçao in a more disadvantageous competitive position than by not implementing it. In this regard, if Curaçao does not locally calculate and levy the top-up tax, the jurisdiction of the UPE will levy based on the IIR or the jurisdiction of another MNE group entity will levy based on the UTPR. That said, it remains essential to have a QDMTT in place that is calculated under the GloBE Rules. If a calculation leads to a higher ETR than 15%, Curaçao will be in a disadvantageous competitive position. Moreover, introducing a QDMTT will not put an end to tax competition of Curaçao. For instance, entities that do not fall within the scope of Pillar Two, will still have access to tax incentives offered by Curaçao. Therefore, an appealing fiscal environment for business establishments will remain pertinent.

#### **5. CHALLENGES AND CONSIDERATIONS**

Introducing QDMTT for profit tax entails administrative complexity. This will put a burden on the tax authorities, particularly when applying the calculation methodology under the GloBE Rules. To comply effectively with Pillar Two and the GloBE Rules will not only require a comprehensive understanding of these rules, but the expertise of specialists in this area is very much needed.

This need may incur additional costs, such as training costs, for a better understanding of the GloBE Rules. Moreover, implementing a QDMTT also entails IT adjustments in the tax return portal. The tax authorities will have to adjust the tax return portal in such a way that it automatically calculates the GloBE ETR of a Constituent Entity established in Curaçao and it must also automatically calculate the QDMTT or the top-up tax in case the GloBE ETR is lower than 15%. IT adjustments in this regard can take quite a long time. Additionally, the costs in this regard may sum up to a substantial amount. MNEs are already expected to pay a minimum tax of 15% and must, therefore, calculate the GloBE ETR in all jurisdictions where they operate. In essence, the MNE must comply with GloBE Rules, regardless of a QDMTT implementation in Curaçao.

## **6. BENEFITS OF IMPLEMENTING A QDMTT IN CURAÇAO**

Implementing the QDMTT in Curaçao offers significant benefits beyond mere financial gains. As already pointed out, it has the potential to generate additional tax revenue by effectively taxing profits that would otherwise be shifted to different jurisdictions, thereby strengthening the financial resources of Curaçao. However, implementing the QDMTT also ensures a fair distribution of tax burdens, in line with global efforts to combat tax avoidance and to promote tax fairness by taxing MNEs based on the location of economic activities rather than where they file their tax returns. This approach prevents profit shifting and sets a minimum tax threshold, discouraging practices that undermine the tax base. Furthermore, the introduction of the QDMTT in Curaçao signals a critical step to fulfill its international tax commitment

and strengthens Curaçao's international reputation as a transparent and compliant tax jurisdiction. To that end, the implementation of the QDMTT can lead to increased international cooperation by conforming to global standards, positioning Curaçao as a reliable player in the international tax landscape, and promoting collaboration with other jurisdictions, which in turn can result in mutual benefits in the field of trade, investment, and economic development. In contrast, the non-implementation of Pillar Two, particularly the QDMTT, may not necessarily benefit Curaçao directly. Without a mechanism to address profit shifting and ensure a minimum level of taxation, the jurisdiction could face challenges in maintaining a level playing field and preventing erosion of its tax base.



## 7. CURRENT DEVELOPMENTS

On October 30, 2023, an 'International Compliance Task Group' (the task group) was established by the Minister of Finance of Curaçao to map out the consequences for Curaçao of whether to implement Pillar Two and the possible alternatives for Pillar Two. On January 17, 2024, the task group held a first consultation meeting where various stakeholders were able to put forward their views on the introduction of Pillar Two. During the consultation round, the central question was what the possible consequences for Curaçao and the international financial sector would be if this international tax standard is introduced into Curaçao legislation. The task group will advise the Minister on taking a position on this matter. On a separate note, in the Dutch Caribbean (Bonaire, Saba, Sint Eustatius), new legislation on the minimum tax came into force on January 1, 2024. This new legislation introduces a new minimum taxation of 15% on the profits of a Constituent Entity in the Dutch Caribbean.

## 8. FINAL REMARKS

The decision to implement a QDMTT in Curaçao requires careful consideration of its potential impact on competitiveness, administrative efficiency, and overall economic well-being. Balancing the benefits of additional revenue and fair taxation against compliance costs and increased administrative complexities is crucial for making an informed decision aligned with Curaçao's financial goals and international tax standards. By implementing a QDMTT, Curaçao will demonstrate its commitment to international tax standards, whilst strengthening its position in the global economy, and contributing to combating tax avoidance and promoting tax fairness worldwide.



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<sup>1</sup>OECD (2021), Tax Challenges Arising from the Digitalisation of the Economy – Global Anti-Base Erosion Model Rules (Pillar Two): Inclusive Framework on BEPS, OECD, Paris, page 60 <https://www.oecd.org/tax/beps/tax-challenges-arising-from-the-digitalisation-of-the-economy-global-anti-base-erosion-model-rules-pillar-two.htm>.

<sup>2</sup>OECD (2021), Tax Challenges Arising from the Digitalisation of the Economy – Global Anti-Base Erosion Model Rules (Pillar Two): Inclusive Framework on BEPS, OECD, Paris, page 60 <https://www.oecd.org/tax/beps/tax-challenges-arising-from-the-digitalisation-of-the-economy-global-anti-base-erosion-model-rules-pillar-two.htm>, article 1.1

<sup>3</sup>In this article, we will not go into the calculation of the Adjusted Covered Taxes and the GloBE Income.