

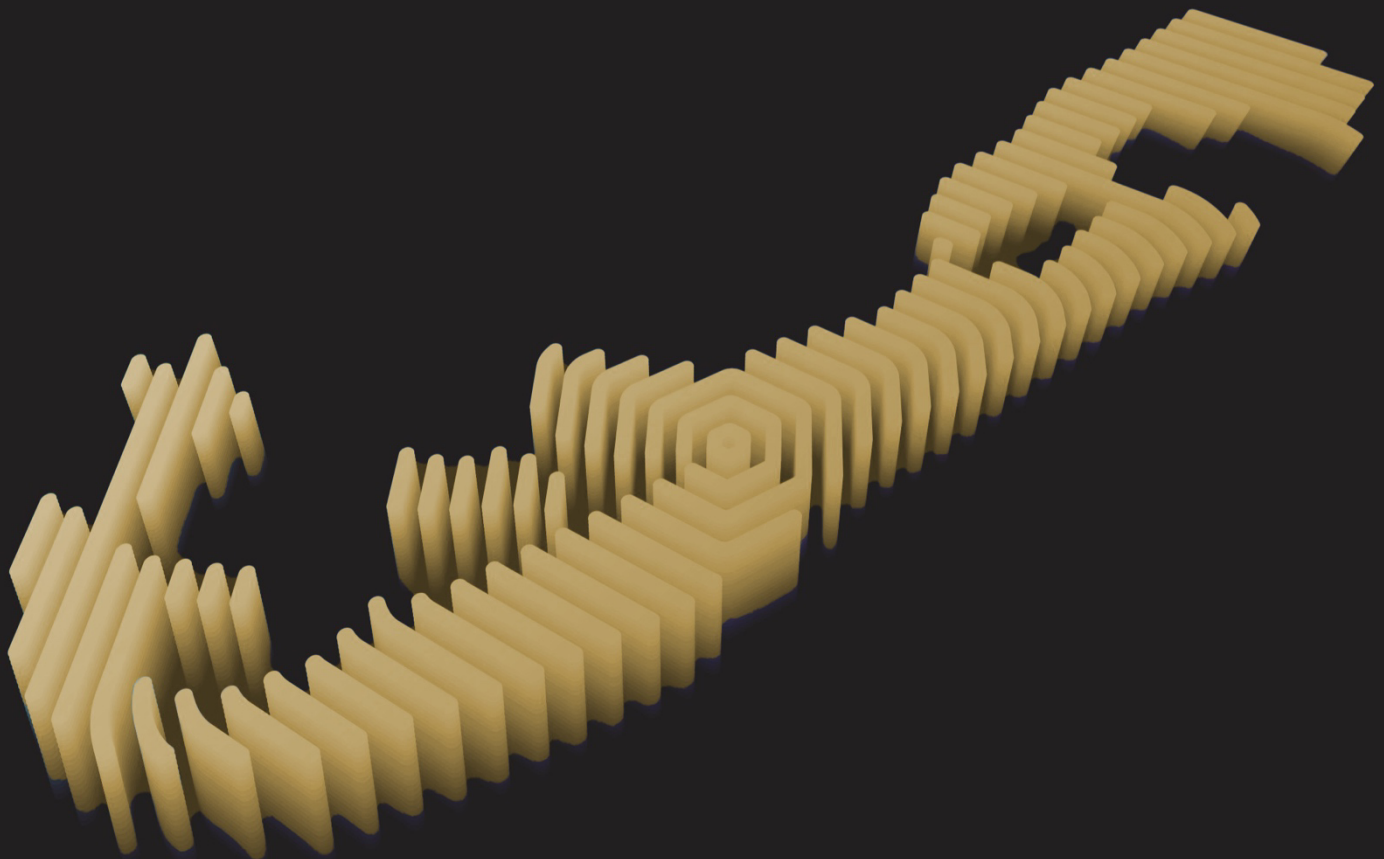


GOVERNMENT OF BERMUDA
Ministry of Finance

SECOND PUBLIC CONSULTATION

Introduction of
Corporate Income Tax in Bermuda

Published October 5, 2023





Government of Bermuda
Ministry of Finance
Second Public Consultation

Introduction of Corporate Income Tax in Bermuda

Table of Contents

1. Introduction	3
2. Policy Considerations	4
3. Corporate Income Tax Outline and Further Consultation.....	6

1. Introduction

Following the First Public Consultation conducted between August 8 and September 8, the Government of Bermuda has reviewed the responses, comments and submissions made as part of that process. That review has enabled this Second Public Consultation to be undertaken.

This Second Public Consultation is in three parts. Following the Introduction, Part 2 addresses certain overarching policy considerations which have formed the basis of certain measures in the proposals. Part 3 outlines the framework of the proposed Bermuda Corporate Income Tax, with focus on the key technical components of the proposals, and seeks further input from stakeholders. It will also address some of the comments received during the First Public Consultation.

This Second Public Consultation period will run from October 5, 2023 to October 30, 2023. Submissions received after this date may not be considered.

A Third Public Consultation document, including full draft legislation, is expected to be released on or about November 10, 2023, with the Consultation to run until November 24, 2023. It is the Government's intention to table the Corporate Income Tax Bill for debate with a view to enactment prior to December 31, 2023.

Consultation Paper Responses and Comments should be submitted by email to: cjanderson@gov.bm. Respondents should include "*Introduction of Corporate Income Tax in Bermuda*" in the subject box.

Media Enquiries should be addressed to: hsadams@gov.bm.

2. Policy Considerations

Design Principles

As set out in the First Public Consultation, several important policy factors influence the design of the corporate income tax. A primary objective in developing the corporate income tax is to ensure to the greatest extent possible that it is not a material incremental expense by ensuring that it qualifies as a Covered Tax for the purposes of the GloBE Rules. This should reduce the amount, if any, of Top-Up Tax payable to other jurisdictions and prevent the double taxation of profits earned in Bermuda. The second overarching objective is the desire to remain aligned so far as is practicable with the GloBE Rules. This should simplify the corporate income tax and support consistent, predictable and manageable tax outcomes on profits earned in Bermuda, reducing the disruption that may otherwise arise upon adoption.

Many respondents to the First Public Consultation expressed support for these objectives. Equally, strong support was expressed for the inclusion within the corporate income tax regime of features to support wider policy initiatives of the Government. At the highest level, these policy initiatives involve the maintenance and furthering of the competitiveness of Bermuda as an international business centre, and reinforcing the reputation of the island for transparency and co-operation. Further, these initiatives enable the continued reshaping of Bermuda as the leading mid-shore jurisdiction for international business.

The Government also believes it is critical to ensure that the cost of living, doing business and the ability to work in Bermuda are properly managed and that it seizes opportunities to increase the highly skilled jobs resident in Bermuda necessary to stimulate the wider economy in the future.

Careful consideration must be given to appropriate transition rules so that Bermuda businesses are not disadvantaged when compared to those operating in other jurisdictions. By enacting legislation in 2023 with the tax to become effective in 2025 and including appropriate transition measures, there should be a fairer transition into the new regime. The Government continues to monitor the ongoing tax developments globally, so that any changes in policy or implementation timelines are properly reflected in the process being undertaken in Bermuda.

Tax Assurance Certificates

The international tax landscape has changed considerably since 1966 when the Exempted Undertakings Tax Protection Act came into force. The development of what was to become the European Union and the increase in the level of interest related to global tax policy in groups like the Organisation for Economic Co-operation and Development (“OECD”) have given rise to an interest in significant cross-border tax protection measures, most recently in the form of the Base Erosion and Profit Shifting initiatives in 2015 and 2019. These measures include the requirement for jurisdictions including Bermuda to maintain adequate economic substance for activities that involve mobile income and mandate increased transparency, disclosure and international tax co-operation.

The most recent of these measures is the Pillar Two initiative, otherwise known as the Global Minimum Tax. The stated policy aim of this measure is to subject profits of a multinational group, regardless of the jurisdiction in which they are earned, to an effective tax rate of at least 15%.

As a result, many if not all multinational groups (within the scope of Pillar Two) that have business operations in Bermuda will have jurisdictions outside Bermuda seeking to collect Top-Up Tax on profits earned in Bermuda which may not have been taxed at an effective rate of at least 15%. This Top-Up Tax could be collected either from the shareholder under the Income Inclusion Rule (IIR) or from an affiliate under the UTPR¹. For these groups, the tax on Bermuda profits may be payable to other jurisdictions if not collected by Bermuda. There is little economic difference between paying tax in Bermuda or paying that same tax to foreign jurisdictions. In fact, for groups headquartered in Bermuda, there may be incremental cost associated with not paying tax in Bermuda as a result of the UTPR.

As discussed further below, there are additional advantages that may flow from collecting the tax in Bermuda rather than allowing it to be paid to foreign jurisdictions. Restructuring the existing tax regime in Bermuda, potentially reducing consumption and payroll taxes, would reduce the cost of living and doing business in Bermuda. Furthermore, the introduction of meaningful qualified refundable tax credits in the proposed corporate income tax regime presents an opportunity for groups that have Bermuda entities to invest in the jurisdiction in a manner consistent with the Government’s policy objectives.

In this context, Government believes it is reasonable and proportionate for any new Bermuda corporate income tax regime to supersede any existing tax assurance held by entities within the scope of the new Bermuda corporate income tax. Notably, such assurances would continue to

¹ These terms are drawn from the OECD Publications *Tax Challenges Arising from the Digitalisation of the Economy: Global Anti-Base Erosion Model Rules (Pillar Two)*, together with related Commentary and Administrative Guidance as updated from time to time, hereafter the “GloBE Rules”.

apply for entities outside the scope of the Bermuda corporate income tax, and would continue to be issued going forwards, although new assurances issued following the enactment of the corporate income tax would be adjusted to ensure consistency with the provisions of the new regime.

3. Corporate Income Tax Outline and Further Consultation

The following is an outline of the Bermuda Corporate Income Tax (“CIT”) currently being considered by the Government. The Effective Date for the legislation is expected to be January 1, 2025, meaning that Bermuda Constituent Entity Groups will be subject to CIT for Fiscal Years beginning on or after January 1, 2025.

1. Scope

Key foundational definitions in the GloBE Rules (e.g., Group, MNE Group, Constituent Entity, Ultimate Parent Entity, Main Entity etc.) will be included in the CIT rules. As a general rule, terms defined in the GloBE Rules which are also used in the CIT rules will be drafted to follow the same definitions contained within the GloBE Rules. Certain terms are specific to the CIT rules and are defined below.

Consistent with the GloBE Rules, the CIT will only apply to MNE Groups which have consolidated revenue of at least €750M in at least two of the four Fiscal Years immediately preceding the Fiscal Year in question (an “In Scope MNE Group”). For MNE Groups that meet the revenue threshold, CIT will generally apply to each Tax Resident Entity and Bermuda permanent establishment (“PE”) that is a Constituent Entity of such MNE Group (a “Bermuda Constituent Entity”).

1.1 Tax Resident Entity and Bermuda Permanent Establishment

For the purpose of the CIT, Tax Resident Entity and Bermuda PE will be defined as follows:

- Tax Resident Entity - An Entity created or organised in Bermuda, unless the Entity provides sufficient evidence that it is tax resident in another jurisdiction based on the location of its management and control.

- Bermuda PE - A PE, as such term is defined in Article 5 of the OECD Model Tax Convention, located in Bermuda.

1.2 Exempt and Excluded Entities

The following Tax Resident Entities and Bermuda PEs are exempt from the CIT and are not considered Bermuda Constituent Entities:

- 1.2.1 Excluded Entities as defined in Article 1.5 of the GloBE Rules (e.g., governmental entities, not-for-profits, pension funds, investment funds etc.).
- 1.2.2 Entities and PEs that are Constituent Entities of an MNE Group that are less than 80% owned, directly or indirectly, by the Ultimate Parent Entity (by value) (see section 1.4 below).
- 1.2.3 Entities and PEs that are Constituent Entities of an MNE Group with Limited International Presence (as defined in section 1.5 below).

An Entity for these purposes is any legal person (other than a natural person) or an arrangement which prepares separate financial statements regardless of whether it has separate legal personality.

1.3 Bermuda Constituent Entity Groups

A “Bermuda Constituent Entity Group” is a group comprised of one or more Bermuda Constituent Entities that are Constituent Entity members of an In Scope MNE Group. An In Scope MNE Group may include more than one Bermuda Constituent Entity Group, as follows:

- 1.3.1 Each Bermuda Constituent Entity that is a Flow-through Entity, but is not the Ultimate Parent Entity of the In Scope MNE Group, shall be treated as a separate and distinct Bermuda Constituent Entity Group comprising only such Bermuda Constituent Entity;
- 1.3.2 All Bermuda Constituent Entities that are Constituent Entity members of an In Scope MNE Group and that
 - are Investment Entities or Insurance Investment Entities,
 - are not Tax Transparent Entities, and

- are not subject to an Investment Entity Tax Transparency election or a Taxable Distribution Method election

shall be combined in a single Bermuda Constituent Entity Group (separate from the Bermuda Constituent Entity Groups described in sections 1.3.1 and 1.3.3).

1.3.3 All remaining Bermuda Constituent Entities that are Constituent Entity members of an In Scope MNE Group shall be combined in a single Bermuda Constituent Entity Group.

At the election of the Filing Bermuda Constituent Entity, one or more Bermuda Constituent Entities that would otherwise be included in a single Bermuda Constituent Entity Group may elect to apply alternative groupings in determining the composition of a Bermuda Constituent Entity Group.

A “Filing Bermuda Constituent Entity” means the Entity filing the CIT return for a Bermuda Constituent Entity Group.

Entities which are tax resident in Bermuda but also subject to tax in another jurisdiction will be subject to tax in Bermuda as Bermuda Constituent Entities, but credit will be given against CIT for any foreign taxes on income borne by the Entity (see section 3.3 below).

1.4 Exclusion of Certain Partially-Owned Entities

As stated in the First Public Consultation, a general design principle advanced was that the CIT would not leave any group owing more tax than would otherwise be owed under Pillar Two. Because of the way in which the Effective Tax Rate of a jurisdiction is calculated under the GloBE Rules, this design principle advanced cannot be accomplished where a CIT is imposed on the income of certain partially owned entities. This is because either the owners of the entity would bear the economic burden of the CIT which they would not otherwise bear, or the MNE Group would owe additional Top-Up Tax above what would be paid if there were no CIT because the CIT is diluted in the calculation of the Effective Tax Rate. As an example, assume an MNE Group has a Constituent Entity in Bermuda which earns 100 of GloBE Income and in which the MNE Group owns a 15% interest. If the Constituent Entity is subject to CIT, then 15 of CIT is payable. The GloBE ETR is then 15% and there is no Top-Up Tax, but the other owners of the Constituent Entity which are not members of the MNE Group bear the economic burden of 12.75 of CIT which would not have been owed by those owners under Pillar

Two. If Bermuda were to tax the UPE or intermediate owner on its pro-rata share of the profits of the Constituent Entity, then 2.25 of Bermuda CIT is payable which is then allocated to the Bermuda entity. The GloBE ETR takes into account all of the entity's income so the ETR is 2.25% and some further Top-Up Tax arises under Pillar Two. The threshold of 80% was determined on the basis that a 20% ownership interest represented a meaningful threshold for a substantive ownership interest versus a smaller number, which might create restructuring opportunities to avoid the application of the CIT.

In some instances, entities may not wish to be excluded from the application of the rules, so an election will be available to disapply this specific provision and allow for such partially-owned entities to be Bermuda Constituent Entities.

1.5 Exclusion for Groups with Limited International Presence

As noted in the First Public Consultation, Bermuda Constituent Entities and Bermuda PEs which are members of MNE Groups which satisfy the requirements of Article 9.3.2 of the GloBE Rules (referred to in the CIT as "Groups with Limited International Presence") are not considered to be within the scope of the CIT. This exclusion is based on similar principles applicable to the exclusion from the UTPR of MNE Groups in the initial phase of their international activity contained in Article 9.3 of the GloBE Rules. However, here it is an exclusion from scope rather than a reduction in tax payable.

The GloBE Rules provide that the reduction in Top-Up Tax under Article 9.3 no longer applies for Fiscal Years beginning more than five years from the first Fiscal Year when the MNE Group originally came within the scope of the GloBE Rules. For Groups within the scope of the GloBE Rules when they come into effect, the period of five years begins at the time the UTPR rules come into effect and thus the period of exclusion ends for any Fiscal Year beginning on or after December 31, 2029.

The Limited International Presence exclusion will therefore mirror this provision and will provide that Bermuda Tax Resident Entities and Bermuda PEs that are members of MNE Groups which fall within the criteria for the Limited International Presence exclusion will be regarded as out of scope of CIT for periods up to the first Fiscal Year ending on or after December 31, 2029.

The Commentary to the GloBE Rules notes that OECD Inclusive Framework Members agreed that the earliest that the UTPR could come into effect was 2024 and therefore suggests that the period of the Article 9.3 exclusion would only apply for periods up to the

first Fiscal Year ending on or after December 31, 2028 irrespective of when UTPR is actually applicable. Government will continue to monitor whether this position is upheld and whether any adjustment would be required in future.

For the avoidance of doubt, the five-year period is continuous and is not therefore suspended should a group fall below the threshold for being in scope as an MNE Group (i.e. the consolidated revenue test).

1.6 Entity Classification

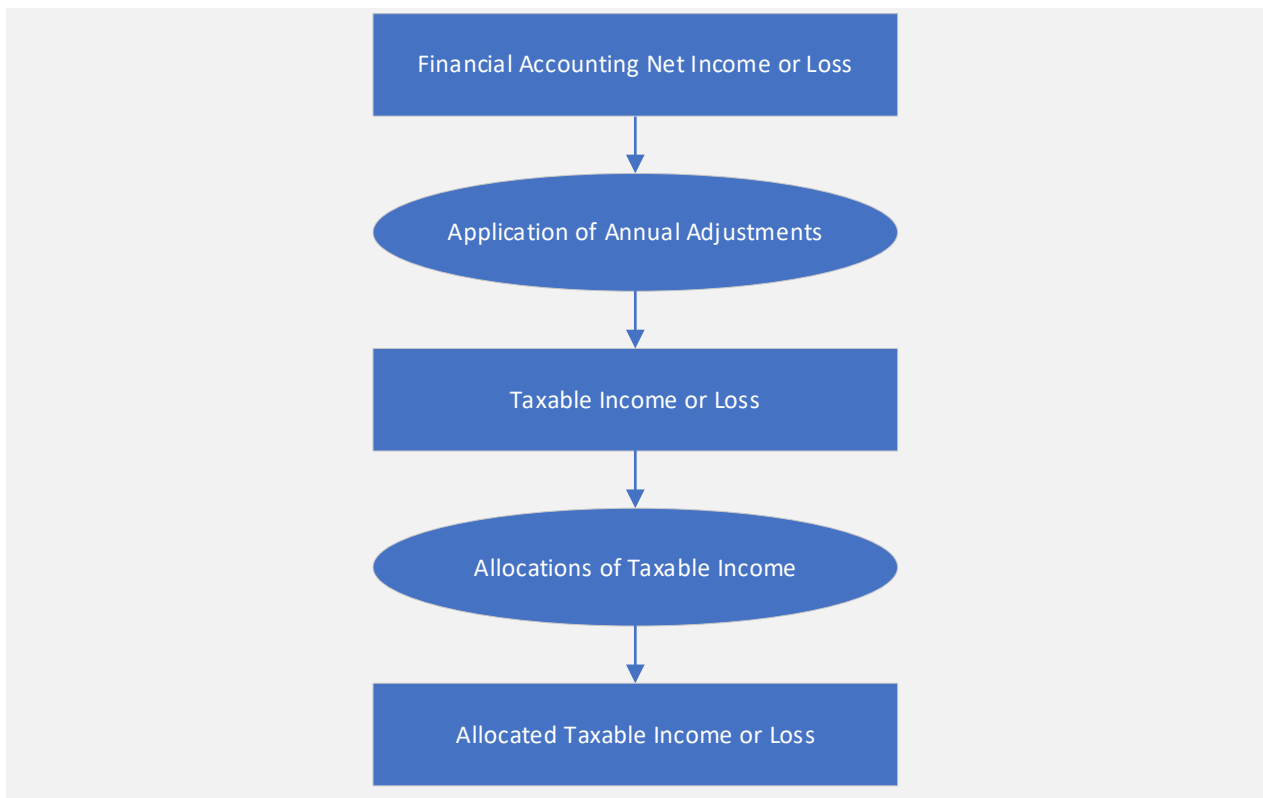
In order to apply the rules, it is necessary to determine whether an entity is a Flow-through entity (and, if so, what kind) or fiscally non-transparent. For Bermuda Entities, a list will be provided indicating the default classification of the different Bermuda legal entity forms. For non-Bermuda Entities, in general, the default classification is determined with reference to the treatment of the entity under the entity's local law. If the local jurisdiction subjects the entity to tax, it will default to non-transparent. If the local jurisdiction taxes the entity's owners regardless of whether the entity's profits are distributed, the entity will default to Flow-through. If a non-Bermuda Entity's local jurisdiction does not address classification (e.g. the local jurisdiction does not impose a corporate income tax), a separate list will show general default classifications for entities such as bodies corporate and partnerships. In addition, for non-Bermuda Entities a separate list will show general default classifications for entities in particular jurisdictions to assist in the classification determination.

The rules will also provide the ability to elect whether or not an entity, whether Bermudian or non-Bermudian, is treated as fiscally transparent or fiscally non-transparent. The Government will establish a portal for accepting entity classification elections during 2023 following the passage of the CIT law.

Question 1: Are there any comments in relation to Scope, the proposed adoption of the general rules relating to group composition and scope from the GloBE Rules, and the proposed Entity Classification Rules?

2. Calculation of Taxable Income

In general, the Taxable Income or Loss of a Bermuda Constituent Entity is computed by following the sequence shown in the following diagram:



2.1 Financial Accounting Net Income or Loss – Accounting Standards

The starting point for determining Bermuda taxable income is the Financial Accounting Net Income or Loss (“FANIL”) of each Bermuda Constituent Entity which is then adjusted for certain items.

The First Public Consultation indicated that the starting point for determining the net income or loss of each Tax Resident Entity or Bermuda PE should be the accounting standard used in preparing the consolidated financial statements of the Ultimate Parent Entity (“Consolidated Financial Statements”). It was further recognised that additional consideration would be given to whether it was feasible to allow taxpayers to adopt other accounting bases such as those adopted locally in a particular jurisdiction as a starting point in the determination of taxable income.

Various responders to the First Public Consultation indicated that the CIT rules should allow for the determination of Taxable Income or Loss on the basis of an accounting standard other than the standard used in the preparation of the Consolidated Financial Statements (such as Bermuda or US NAIC statutory accounting principles).

The CIT rules will provide that the starting point for determining the taxable income of a Bermuda Constituent Entity will be the net income or loss determined under the

accounting standard adopted by the Ultimate Parent Entity in preparing the Consolidated Financial Statements. The CIT rules will also permit an election for a Bermuda Constituent Entity to instead use an Approved Financial Accounting Standard as the starting point for determining taxable income, provided that, if the use of the Approved Financial Accounting Standard results in permanent differences in excess of €1 million as compared to the result using the accounting principle applied by the Ultimate Parent Entity, the treatment of relevant items under the Approved Financial Accounting Standard must be adjusted. Approved Financial Accounting Standards are expected to include all Acceptable Financial Accounting Standards (as defined in the GloBE Rules), Bermuda statutory accounting principles and US NAIC statutory accounting principles. This list may be updated from time to time.

Consistent with the GloBE Rules, adjustments to income or expense attributable to purchase accounting for an acquired business (irrespective of when the business was acquired) that are reflected in the consolidated accounts of the MNE Group in which the Bermuda Constituent Entity is a member, rather than the separate accounts of the Bermuda Constituent Entity itself, are not taken into account in the computation of the FANIL of the Bermuda Constituent Entity.

As in the Commentary to the GloBE Rules, where a business combination arose prior to December 1, 2021, the Bermuda Constituent Entity may use the carrying value reflected in its separate accounts after the application of “push down” accounting, if permitted, or the carrying value of assets and liabilities determined as per the financial accounting standard used by the Ultimate Parent Entity, but only if the MNE Group in which the Bermuda Constituent Entity is a member does not have sufficient records to determine its FANIL with reasonable accuracy based on the unadjusted carrying values of the acquired assets and liabilities.

Items of income and expense, other than those attributable to purchase accounting, that are reflected in the consolidated accounts of the MNE Group in which the Bermuda Constituent Entity is a member, rather than the separate accounts, may be taken into account only to the extent they can be reliably and consistently traced to the Bermuda Constituent Entity.

Question 2: Are there any comments in relation to the appropriate Financial Accounting Standards to be used?

2.2 Annual Adjustments to determine Taxable Income or Loss

A Bermuda Constituent Entity's FANIL is adjusted for the following items ("Annual Adjustments") to arrive at Taxable Income or Loss:

2.2.1 Accrued Pension Expense

The CIT rules will align with the GloBE Rules, meaning that Pension liabilities are allowed as expenses in the computation of Taxable Income or Loss to the extent of contributions to a pension fund during the Fiscal Year.

The adjustment for Accrued Pension Expense is equal to the difference between (a) the amount of pension contributions during the year and (b) the amount accrued as an expense in the computation of FANIL during the Fiscal Year. The adjustment to FANIL for this difference will be a positive amount if the amount accrued as an expense in the financial accounts exceeds the contributions for the year. It will be a negative amount in Fiscal Years in which the contributions exceed the expense accrued in the financial accounts.

2.2.2 Asymmetrical Foreign Currency Gains or Losses

Asymmetrical foreign currency gains or losses ("FXGL") are generally those that arise due to differences between the functional currency for accounting purposes and the one used for local tax purposes. The CIT rules will adopt provisions similar to those in the GloBE rules to address the main types of FXGL that arise.

2.2.3 Branch Exemption Election

In general, Bermuda Tax Resident Entities will be subject to CIT on their worldwide income. However, an election may be made by a Filing Bermuda Constituent Entity to allocate FANIL of the Bermuda Constituent Entity to a Permanent Establishment located outside Bermuda through which the business of the Bermuda Constituent Entity is carried out (a "Branch Exemption Election"). Any amounts allocated to a non-Bermuda PE pursuant to a Branch Exemption Election are excluded from Taxable Income or Loss.

A Branch Exemption Election applies only to the specific Permanent Establishment designated by the Filing Bermuda Constituent Entity and is permitted with respect to any or all of the Permanent Establishments through which the business of the Bermuda Constituent Entity is carried out.

2.2.4 Economic Transition Adjustment

Bermuda Constituent Entities that will become subject to the CIT beginning in 2025 will be at different stages in their business and life cycles and may have made significant investment in Bermuda at a time when no deductions were provided for such investments, while becoming taxable on all future profits associated with such investments. Further, those Entities will apply a wide array of financial accounting principles which can result in distortive timing of the recording of income and expenses.

As a result, the Government believes it is appropriate for the CIT rules to provide a transition adjustment upon entry into the CIT system (the “Economic Transition Adjustment”) in order to ensure a fair and equitable transition into the CIT system for Bermuda Constituent Entities.

An elective opening adjustment will be provided to align a Bermuda Constituent Entity’s starting point for the tax regime more closely with its economic position prior to the application of the CIT. This is expected to achieve a fairer measure of taxable income generated once the CIT is in effect.

If the election is made, a Bermuda Constituent Entity would recognise an Economic Transition Adjustment with respect to all its assets and liabilities (with the exception of goodwill) held as of September 30, 2023 (the “Basis Adjustment Valuation Date”). Under this election, an adjustment arises equal to the difference between the fair market value of each asset and liability as of the Basis Adjustment Valuation Date and the carrying value of the asset and liability (as adjusted where appropriate for purchase accounting and similar items) in the Consolidated Financial Statements (potentially as adjusted if the Bermuda Constituent Entity adopts a financial accounting standard for CIT purposes that differs from that used in preparing the Consolidated Financial Statements) as of the Basis Adjustment Valuation Date.

In relation to identifiable intangibles (i.e., intangibles other than goodwill), a deduction equal to ten percent of the adjustment shall be allowed for the purposes of calculating Taxable Income or Loss for the Fiscal Year beginning on or after the Effective Date and each of the nine Fiscal Years following that

Fiscal Year. If an identifiable intangible is disposed of before the end of the ten-year amortization period, gain or loss recognized on the disposition is adjusted for the remaining unamortized adjustment. In the case of all other assets (other than goodwill) and liabilities, FANIL would be recalculated by reference to the new tax basis (i.e., rather than the carrying value recognized in the financial statements) and would run off after the Basis Adjustment Valuation Date consistent with how the asset or liability itself runs off or is settled under the relevant financial accounting principles.

The amount of the Economic Transition Adjustment that can be deducted in a given Fiscal Year will be limited to 80% of the positive taxable income of the Bermuda Constituent Entity Group before applying Tax Loss Carryforwards. Any excess deductible Economic Transition Adjustment is carried forward into future periods as a Tax Loss Carryforward without expiration and will be subject to the same offset limitations annually at the Bermuda Constituent Entity Group level.

The Economic Transition Adjustment is elective in recognition of the fact that there may be considerable administrative cost and effort in determining the basis of assets and liabilities within the scope of the rules. Government acknowledges that taxpayers that acquire assets in business transactions between the Basis Adjustment Valuation Date of September 30, 2023 and the Effective Date will not be eligible for any Economic Transition Adjustment related to those assets. However, Government believes a cut-off date is warranted to prevent the potential for assets to be transferred to Bermuda Constituent Entities for the purposes of benefiting from the Economic Transition Adjustment.

2.2.5 Excluded Dividends

The CIT rules will follow the GloBE Rules with regards to the identification and treatment of Excluded Dividends.

2.2.6 Excluded Equity Gain or Loss

The CIT rules will follow the GloBE Rules with regards to the identification and treatment of Excluded Equity Gain or Loss.

2.2.7 Included Revaluation Method Gain or Loss

The CIT rules will follow the GloBE Rules with regards to the treatment of included Revaluation Method Gain or Loss.

2.2.8 Insurance Companies

Insurance companies which are Bermuda Constituent Entities shall exclude from the computation of Taxable Income or Loss any amounts charged to policyholders for Taxes paid by the insurance company in respect of returns to policyholders. Those companies shall also include in the computation of Taxable Income or Loss any returns to policyholders not reflected in FANIL to the extent the corresponding increase or decrease in liability to the policyholders is reflected in FANIL.

2.2.9 International Shipping Income

The CIT will include provisions which parallel those in the GloBE Rules to exclude international shipping income and qualified ancillary shipping income from Taxable Income or Loss.

2.2.10 Loss Reserve Discounting

In order to properly account for the time value of money, the Government is considering whether insurers and reinsurers will be required to discount reserves. Further consideration of the nature of particular reserves, whether they are currently discounted or not in the financial statements, and related factors, will be required.

2.2.11 Matching Election

It is recognised that at the commencement of the CIT regime, companies may have accounting mismatches embedded in the financial statements used in the calculation of FANIL, and that such mismatches may also arise on an ongoing basis, causing volatility which would not be appropriate in the computation of taxable income (for example, under funds withheld or modified co-insurance arrangements where the asset side is accounted for at fair market value as an embedded derivative and the liability side is accounted for at book value). Such mismatches are most commonly seen by life reinsurers

who prepare their financial statements using US GAAP, but may exist outside of this scenario.

An election will be available to match the carrying values of assets and liabilities of a Bermuda Constituent Entity. This election would permit the company to record its assets and liabilities on a consistent basis for the purposes of the CIT. If the Economic Transition Adjustment to fair value has also been made, an adjustment will be required to ensure that there is no double taxation or double deduction as a result of both elections being made.

It is further intended that the election is available for a particular group of assets and associated liabilities in an entity which could create a mismatch.

2.2.12 Net Taxes Expense

Consistent with the GloBE Rules, CIT and Creditable Foreign Taxes are generally not deductible against taxable income. Allowing a deduction and a credit for the same taxes provides a double benefit for the same taxes. Therefore, an adjustment must be made to add back any CIT and Creditable Foreign Taxes included in FANIL.

2.2.13 Policy Disallowed Expenses

Consistent with the GloBE Rules, there is an adjustment for Policy Disallowed Expenses, including illegal payments such as bribes and kickbacks and expenses related to fines and penalties.

2.2.14 Prior Period Adjustments and Changes of Accounting Principles

A general rule is required for changes in accounting principle or policy (as used in the relevant financial statements used to determine FANIL), as such changes may be accounted for in opening retained earnings, which would not affect taxable income.

The general rule would be to calculate an adjustment equal to the cumulative effect of the change on previously reported taxable income and any Tax Loss Carryforwards as of the beginning of the year of change. The year of change is the fiscal year for which the change is first adopted in the relevant financial statements. If the adjustment is a decrease in taxable income (or increase in

Tax Loss Carryforward), the entire adjustment is taken into account in the year of the change. If the adjustment is an increase in taxable income (or a reduction in Tax Loss Carryforward), the adjustment is spread over four fiscal years starting with the year of change. The same guidance can be applied to prior period corrections, though this may only apply if the correction applies to fiscal years where the statute is still open. There will be flexibility for special rules where a different cumulative effect adjustment or spread periods are warranted by the nature of the change.

A specific elective rule will be introduced for the effects of adopting International Financial Reporting Standard 17 (“IFRS 17”), which addressed the accounting for Insurance Contracts, and US GAAP Long Duration Targeted Improvements (“LDTI”). IFRS 17 took effect on January 1, 2023, and LDTI took effect on January 1, 2023 for public companies and takes effect on January 1, 2025 for private companies with early adoption permitted. IFRS 17 and LDTI significantly change the accounting for long-duration insurance business, including the timing of when profits or losses are recognized over the lifetime of insurance and reinsurance contracts. Both require the use of a current estimate of insurance liabilities compared to traditional approaches that used locked-in assumptions at the policy issue date. However, they use different concepts and can result in very different outcomes in terms of profit recognition patterns. These new accounting principles both potentially involve a restatement of opening equity for existing insurance and reinsurance contracts, which can cause several years of previously earned profits to be reversed and earned again in the future (especially under IFRS 17 with its new unearned profits reserve called the “contractual service margin”).

It is proposed that an election spread period of ten Fiscal Years be introduced for the effect of IFRS 17 and LDTI, to be applied to the amount which has not reversed as at the Effective Date of the CIT. The election is available on an entity-by-entity basis and applies to changes in accounting in the future where local financial accounting standards adopt new guidance to conform with IFRS 17 or LDTI.

For the avoidance of doubt, the election is available in relation to amounts accounted for in retained earnings prior to the commencement of the Bermuda

tax regime. The straight-line amortisation commences with the Effective Date of the CIT regime.

If this election is made, there will be provision to ensure that double counting is eliminated between this election and the other elections contained in the CIT rules.

2.2.15 Realisation Basis

Bermuda Constituent Entities will be permitted to elect to treat assets and/or liabilities on a realisation basis for tax purposes. The election may be made in relation to an entity, or particular assets within an entity. The opening tax basis for the period for which the election is made will take into account the previous adjustments of assets and liabilities i.e. whether it has previously been marked to market, or has been subject to rebasing as a result of an election made pursuant to the CIT Rules.

It will be made clear that the election will be available to reinsurers in relation to funds withheld and modified co-insurance contracts.

2.2.16 Stock-based Compensation

A Bermuda Constituent Entity Group may elect to substitute the amount of Stock-Based Compensation in the financial accounts with the amount computed under special rules which provide for a deduction for Stock-Based Compensation which has an exercise date during the Fiscal Year, to the excess of the fair market value on exercise over the value of any consideration received for the stock. Reasonable tracing of the expense to the Bermuda Constituent Entity that received the services for which the compensation was provided will be required.

2.2.17 Transfer Pricing and Intra-Group Transfers

Consistent with the GloBE Rules, any transactions between a Bermuda Constituent Entity and another Constituent Entity located in a different jurisdiction which is not recorded at the same amount in the financial statements of each entity must be adjusted to the same amount and consistent with the Arm's Length Principle. Any amount which is not consistent with the Arm's Length Principle must be adjusted to be so consistent.

Further consideration will be given to the appropriate approach to the treatment of transactions between Bermuda Constituent Entities.

2.2.18 The CIT rules may also include Annual Adjustments for other items addressed in the GloBE Rules or otherwise, as appropriate, such as the treatment of Restricted Tier One Capital, reorganisations, etc.

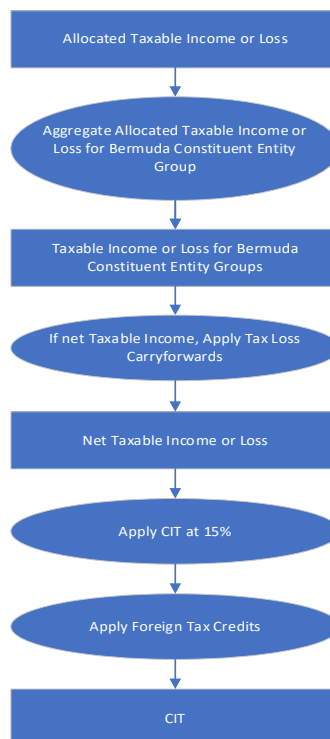
Question 3: Are there any comments with respect to the Annual Adjustments made to arrive at Taxable Income or Loss in Section 2.2 above?

2.3 Allocation of Taxable Income or Loss

The CIT rules will follow Articles 3.4, 3.5, 7.1 and 7.4 of the GloBE Rules with respect to the allocation of Taxable Income or Loss to Permanent Establishments, non-Constituent Entity-Owners of Flow-through Entities and Constituent Entity Owners of Tax Transparent Entities, as well as between Bermuda Constituent Entities and their owners, to the extent the Bermuda Constituent Entity is a Flow-through Entity which is also the Ultimate Parent Entity of the MNE Group or an Investment Entity or Insurance Investment Entity.

3. Calculation of Corporate Income Tax Liability

In general, the calculation of the CIT liability follows the sequence shown in the following diagram:



3.1 Losses

The amounts of Taxable Income or Loss for each Bermuda Constituent Entity are aggregated to arrive at a preliminary measure of Taxable Income or Loss for the Bermuda Constituent Entity Group of which the Bermuda Constituent Entity is a member.

To the extent that the Bermuda Constituent Entity Group earned Taxable Income for the Fiscal Year, it would generally be permitted to deduct its Tax Loss Carryforward (if any) from prior periods in arriving at Net Taxable Income. The Tax Loss Carryforward deduction is intended to prevent taxation in excess of economic income and recognizes that the Bermuda Constituent Entity Group should not be subject to CIT on the mere recovery of prior period losses. The Tax Loss Carryforward is comprised of the following elements:

- 3.1.1 An Opening Tax Loss Carryforward, determined in the same manner as if the Bermuda Constituent Entity Group had been subject to CIT in the five Fiscal Years preceding the Effective Date, and
- 3.1.2 Net Taxable Losses generated by the Bermuda Constituent Entity Group in Fiscal Years beginning on or after the Effective Date.

There is no limit on the number of years for which the Tax Loss Carryforward may be carried forward. However, the amount of Tax Loss Carryforward which may be used against Taxable Income in a particular Fiscal Year is limited to 80% of the Taxable Income determined prior to the Tax Loss Carryforward deduction. This limitation is prudent to retain sufficient income in charge to CIT to provide a reliable source of government revenue at least in the early years transitioning into the new CIT system. This limitation will need to be coordinated with other provisions which provide for a reduction in Taxable Income spread over a number of periods, such as the Economic Transition Adjustment, which are also subject to a similar limitation. There is no provision for loss carry-back. Elections will be provided to allow for a lesser amount of brought forward loss to be applied against Taxable Income in a given Fiscal Year.

Although the limitation on the utilisation of losses is determined at the Bermuda Constituent Entity Group level, it is necessary for groups to record and track losses at the Bermuda Constituent Entity level so that appropriate adjustments can be made when entities leave the group whether through liquidation, redomiciliation or sale.

It is recognised that Solvency II or equivalent regimes may allow for a capital benefit known as the “Loss Absorbing Capacity of Deferred Taxes”. This benefit would reduce the Solvency Capital Requirement that a group is required to hold and reflects the benefit that a group can expect to receive if it were to incur a “shock loss”, meaning an event with a probability of 0.5%. To recognise this benefit, a group must be able to show that it can use the shock loss for tax purposes against other income. As a result, an exception to the 80% limitation on the Tax Loss Carryforward deductions may be provided

3.2 Corporate Income Tax Rate

Many respondents to the First Public Consultation expressed a preference for a rate which did not result in more tax being paid in Bermuda than would otherwise have arisen under the application of Pillar Two rules in other jurisdictions. Further, respondents (particularly those from multinational groups headquartered in Bermuda) expressed a strong preference for a rate which would not likely result in the application of UTPR in affiliate jurisdictions as this would lead to potentially significant additional administrative cost.

A statutory rate of 15% would in principle prevent material amounts of Top-Up Tax arising, and would preserve the ability of certain investment entities and insurance investment entities to elect to be tax transparent.

It is, however, recognised that statutory rates may not align with effective tax rates and that it is the effective tax rate upon which Top-Up Tax is calculated. There were also concerns expressed as part of the First Public Consultation that the effective tax rate might be higher than 15% and support for the 15% rate was in some cases based on the proviso that the rate would not be higher than 15%.

Taking into account all feedback received during the First Public Consultation, the Government intends to adopt a CIT rate of 15%.

3.3 Foreign Tax Credits

The tentative CIT liability determined by applying the 15% CIT rate to Net Taxable Income or Loss may be reduced by a Foreign Tax Credit for a Fiscal Year. The amount of the Foreign Tax Credit for a Fiscal Year is the lesser of the tentative CIT liability of the Bermuda Constituent Entity Group or the sum of the Adjusted Creditable Foreign Taxes (defined below) for all members of the Bermuda Constituent Entity Group. All Creditable

Foreign Tax amounts described below should be determined before considering any foreign tax credit a foreign jurisdiction might allow for CIT incurred by a Bermuda Constituent Entity.

3.3.1 Creditable Foreign Taxes include:

- Non-Bermuda (federal, state, and local) income taxes imposed on the income or profits of a Bermuda Constituent Entity
- Non-Bermuda taxes imposed in lieu of a generally applicable corporate income tax (including taxes imposed on premiums of insurance contracts such as the tax imposed under US Internal Revenue Code section 4371)
- Non-Bermuda taxes levied by reference to retained earnings and corporate equity, including a tax on multiple components based on income and equity
- Non-Bermuda withholding taxes imposed on income (other than dividends from another Constituent Entity) earned by a Bermuda Constituent Entity
- Non-Bermuda withholding taxes imposed on dividends paid by Bermuda Constituent Entities

3.3.2 Creditable Foreign Taxes do not include:

- Top-Up Tax incurred with respect to Pillar Two in respect of a Bermuda Constituent Entity (pursuant to the application of an IIR or UTPR);
- A Disqualified Refundable Imputation Tax (as defined under the GloBE Rules); and
- Taxes paid by an insurance company in respect of returns to policyholders

3.3.3 The Adjusted Creditable Foreign Taxes are determined by taking the current tax expense accrued in the FANIL of the Bermuda Constituent Entity with respect to Creditable Foreign Taxes in the Fiscal Year, adjusted for deferred taxes determined in a manner consistent with Article 4.4 of the GloBE Rules, including the limitation on the rate applicable to deferred taxes to 15%.

Add:

- Any Creditable Foreign Taxes accrued in the profit before taxation in the financial accounts;
- Any credit or refund with respect to a Qualified Refundable Tax Credit recorded as a reduction in current tax expense in the FANIL with respect to Creditable Foreign Tax for the Fiscal Year;
- Any non-Bermuda withholding taxes imposed on dividends paid by the Bermuda Constituent Entity;
- Any amount of Creditable Foreign Taxes paid during the Fiscal Year related to an uncertain tax position where the amount of Creditable Foreign Taxes was previously subtracted in determining Adjusted Creditable Foreign Taxes;

Subtract:

- Any current tax expense for Creditable Foreign Taxes not expected to be paid within 3 years of the last date of the Fiscal Year;
- Any credit or refund with respect to a Non-Qualified Refundable Tax Credit that is not recorded as a reduction to current tax expense in the FANIL with respect to Creditable Foreign Tax for the Fiscal Year;
- Any current tax expense relating to income otherwise permanently excluded from the computation of Taxable Income;
- Any amount of Creditable Foreign Taxes refunded or credited (other than QRTCs) that were not treated as adjustments to current tax expense;
- Any current tax expense relating to uncertain tax positions;

Finally, add or subtract Creditable Foreign Taxes recorded in equity or Other Comprehensive Income relating to amounts included in the computation of Taxable Income or Loss.

3.3.4 Adjusted Creditable Foreign Taxes are allocated under the following principles:

- The amount of any Adjusted Creditable Foreign Taxes of a Bermuda Constituent Entity with respect to Taxable Income or Loss of a Permanent Establishment for which a Branch Exemption has been made is allocated to the Permanent Establishment;

- The amount of any Adjusted Creditable Foreign Taxes of a non-Bermuda Main Entity with respect to Taxable Income or Loss allocated to a Bermuda PE is allocated to that Bermuda PE;
- The amount of any Adjusted Creditable Foreign Taxes of a Tax Transparent Entity with respect to Taxable Income or Loss allocated to a Constituent Entity Owner is allocated to that Constituent Entity Owner;
- In the case of a Constituent Entity that is a Hybrid Entity (as defined in the GloBE Rule) the amount of any Adjusted Creditable Foreign Taxes of a Constituent Entity Owner on income of the Hybrid Entity is allocated to the Hybrid Entity; and
- The amount of any Adjusted Creditable Foreign Taxes accrued in the financial accounts of a Constituent Entity's direct Constituent Entity Owners on distributions from the Constituent Entity during the Fiscal Year are allocated to the distributing Constituent Entity.

In the case of a Bermuda Constituent Entity whose Constituent Entity Owners are subject to a Controlled Foreign Company ("CFC") regime, it is currently expected that the amount of any Adjusted Creditable Foreign Taxes included in the financial accounts of its direct or indirect Constituent Entity Owners under a CFC regime on their share of the Bermuda Constituent Entity's income would be allocated to the Bermuda Constituent Entity.

However, given the complex nature of many CFC regimes and potential challenges that arise in identifying the portion of the shareholder's tax that relates to the Bermuda Constituent Entity's income (particularly in situations where the shareholder owns multiple CFCs, and is required to blend the income from such CFCs with other income of the shareholder), the Government is considering the development of potential allocation mechanisms and ordering rules, as well as possible simplification measures such as an exclusion for the portion of the Bermuda Constituent Entity's Taxable Income or Loss that is subject to CFC inclusion (potentially limited to certain identified CFC regimes).

Question 4: Are there any comments in relation to the computation of tax liability, including the treatment of losses, rate, and the Foreign Tax Credit? Are there any specific comments related to the Foreign Tax Credit treatment of CFC regimes ?

3.4 *De Minimis* Exclusion

The CIT liability may, at the election of the Filing Bermuda Constituent Entity, be deemed to be zero if *de minimis* provisions apply. These will mirror the provisions in Article 5.5 of the GloBE Rules.

4. **Qualified Refundable Tax Credits**

Many respondents to the First Public Consultation expressed support for Qualified Refundable Tax Credits that would reduce the cost of doing business in Bermuda. Nonetheless, the Government requires additional time to undertake economic and cash flow analyses and therefore proposes to introduce details of a Qualified Refundable Tax Credit program in 2024, noting that it remains the intention to have such credits in place before the Effective Date of the legislation.

In principle, a Qualified Refundable Tax Credit could be given for certain substance-based factors. These may fall into a number of categories, such as:

- Bermuda-based jobs, including eligible payroll costs and support for existing and expanded employment opportunities for Bermudians and residents;
- Training, career development, education, internships and apprenticeships;
- Investment in Bermuda-based infrastructure;
- Expenditure to promote investments to help address climate change, environmentally responsible energy, innovation, housing, health care and philanthropy in Bermuda; and
- Other items consistent with Bermuda's desire to be an attractive mid-shore jurisdiction.

Question 5: Are there any comments in relation to what types of underlying items should be included in a Qualified Refundable Tax Credit? Should Bermuda consider other

types of tax credits, including those that may not be considered qualified as prescribed by the GloBE Rules ?

5. Tax Administration

The CIT law will include provisions relating to Returns and Assessment, General Provisions as to Interpretation, Appeals and Relief for Mistake, Collections and Repayments and Revenue Powers. Details will likely be addressed in separate delegated legislation in 2024.

The Government recognises that the administration and management of the CIT is a significant undertaking and will require committed resources beyond what is currently available. As a result, the Government is already developing an implementation process which will address the resource needs for proper management of the proposals both in the immediate short term and beyond. This includes recognition of the fact that some elections under the CIT may need to be made on or before December 31, 2023. The Government will announce details of the format and manner of such elections and the process by which they can be filed.

Question 6: Are there any comments in relation to administrative matters?

Question 7: Are there any comments on any other aspects of this Second Public Consultation not addressed by the preceding questions?

List of Questions

- 1: Are there any comments in relation to Scope, the proposed adoption of the general rules relating to group composition and scope from the GloBE Rules, and the proposed Entity Classification Rules?
- 2: Are there any comments in relation to the appropriate Financial Accounting Standards to be used?
- 3: Are there any comments with respect to the Annual Adjustments made to arrive at Taxable Income or Loss in Section 2.2 above?
- 4: Are there any comments in relation to the computation of tax liability, including the treatment of losses, rate, and the Foreign Tax Credit? Are there any specific comments related to the Foreign Tax Credit treatment of CFC regimes?
- 5: Are there any comments in relation to what types of underlying items should be included in a Qualified Refundable Tax Credit? Should Bermuda consider other types of tax credits, including those that may not be considered qualified as prescribed by the GloBE Rules?
- 6: Are there any comments in relation to administrative matters?
- 7: Are there any comments on any other aspects of this Second Public Consultation not addressed by the preceding questions?

