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# Top International Tax Policy To Watch In 2026

By **Kevin Pinner**

*Law360 (January 2, 2026, 12:03 PM EST)* -- The details of a proposed U.S. exemption from the global minimum tax's international provisions, possible retaliatory measures by the U.S. government and the rollout of major changes in Congress' latest budget are high priority for tax professionals going into 2026.

The policies being watched for 2026 overlap considerably with the most pressing international tax issues of 2025, although the questions tax professionals are asking have evolved. Most professionals assume the U.S. government will secure agreement among the international community to exempt American companies from top-up taxes on income worldwide, so they've begun asking how the deal will work in practice.

The U.S. government is poised to retaliate next year against any remaining foreign tax policies it considers discriminatory. Professionals are trying to anticipate how that will play out. Some think U.S. trade policy could become further entrenched as a means of inducing foreign tax policy changes.

Tax professionals also are trying to interpret and plan for the revamped international tax system under Congress' latest budget, anticipating guidance and regulations from the U.S. Department of the Treasury to assist with these tasks.

At the same time, many countries will begin collecting the first specialized returns under the global minimum tax this year, and professionals are curious how tax authorities will use the information.

Here, Law360 previews international tax practitioners' top priorities for 2026.

**Implementation of Side-by-Side**

Perhaps the most anticipated international tax policy in 2026 is a proposed U.S. exemption from the global minimum tax's international provisions, known as the side-by-side proposal. By Jan. 1, the international community was due to accept a version of this proposal aimed at recognizing the U.S. minimum tax system as separate but equivalent to the global version.

Estonia threw a wrench into that timeline in December when it formally opposed the plan's adoption at the Organization for Economic Cooperation and Development. Yet two-thirds of tax professionals surveyed by EY and The Tax Council in November expect U.S. companies to be exempt from the global minimum tax under the side-by-side proposal by the end of next year. For the most part, practitioners are turning to questions about how the agreement will be carried out.

The outstanding questions are what years it applies to, how quickly it will be implemented and what reporting obligations remain for U.S. companies, according to Jason Yen of EY.

"Everyone kind of baked in that will get an agreement," Yen said.

The palatability of the side-by-side proposal for other countries is linked to two projects that the inclusive framework is working on simultaneously: aligning the treatment of refundable and nonrefundable tax credits and a permanent safe harbor for computing effective tax rates, or ETR, according to Yen.

"The bigger questions seem to be [related to] a lot of challenges and debate about the treatment of tax credits, the changes to tax credits and about the efficacy of the new permanent safe harbor," said Yen, who previously helped negotiate Pillar Two on behalf of the U.S. government.

Pillar Two treats nonrefundable tax credits as dollar-for-dollar reductions to covered taxes but recognizes refundable tax credits as covered income; thus, nonrefundable tax credits reduce a company's ETR while refundable tax credits can increase its ETR. The inclusive framework is also working on a simplified ETR calculation for Pillar Two aimed at being a permanent replacement to the country-by-country reporting safe harbor, which applies to tax years starting before Dec. 31, 2026.

"If you make it too watered down, I think there will be some concerns that Pillar Two is no longer effective. If you make them too restrictive, then you may exacerbate some of the level-playing-field concerns," Yen said.

The European Union member states' main concern with the side-by-side proposal is the difference in tax bases, according to Wesley Boldewijn of Greenberg Traurig LLP. Since Pillar Two applies to financial accounting income, generally maximized to please investors, and the U.S. system applies to tax accounting income, generally minimized for the same reason, they would produce different results — even if they shared a statutory rate, which they do not.

"If the side-by-side approach doesn't work in the end or it's not equal, then I think it will not last for long," Boldewijn said. "It would be interesting to see — if this is working out negatively, basically, for the EU — whether the updates of the directive, which are quite significant, will also get unanimous consent from the member states."

The bloc has little appetite for new tax legislation next year, as it's been preoccupied with a deregulatory agenda, he added.

**The U.S. Stick**

The motivation for other countries to accept the side-by-side proposal is a threat by U.S. Congress to impose taxes on countries that enforce the minimum tax's backstop, called the undertaxed profits rule, or UTPR, on American companies, according to Mary Burke Baker of K&L Gates LLP.

"I call it the Section 899 Sword of Damocles; it's kind of hanging over things if they don't come to at least some sort of a principled agreement on the side-by-side negotiations by the end of the year," Baker said.

Treasury convinced Congress to shelve Section 899 — which would have penalized countries with a UTPR or a digital services tax by raising any U.S. taxes paid by their companies and individuals — from the latest budget to allow time for negotiations on the side-by-side proposal. House Ways and Means Committee Chairman Jason Smith, who first proposed the idea, is ready to dust it off if U.S. companies aren't exempted from Pillar Two, he said in early December.

A reintroduced version likely would be modified because the latest version received a wide array of criticism, Baker said. To pass it, lawmakers could rely on the reconciliation process to sidestep the 60-seat Senate majority needed to avoid the filibuster, but they may not have to, said David Skillman of K&L Gates LLP.

"Concern about Pillar Two is not strictly a partisan issue. There are plenty of Democrats who are very skeptical of Pillar Two," Skillman said.

Although there is talk of a reconciliation bill taking place early next year, "even if they don't have a reconciliation process pending, I could definitely see Smith and [Senate Finance Committee Chairman Mike Crapo, R-Idaho] introducing a stand-alone bill on 899," Baker said.

Alternatively, the government may attack its tax concerns from a trade angle, as President Donald Trump's administration has already shown a willingness to do.

"There's no reason that [U.S. Trade Representative Jamieson Greer] couldn't declare Pillar Two a trade barrier and levy a [Section 301] tariff," Skillman said, referring to a provision that allows tariffs in response to foreign trade policies deemed discriminatory. "In our conversations with Treasury, they have frequently pointed at USTR's authority in this [discriminatory tax] space as kind of the stick."

Multinational companies located in jurisdictions with statutory corporate tax rates above 20% have thus far been shielded from the UTPR under a transitional safe harbor, but this expires for tax years beginning on or after Jan. 1, 2026, and ending on or after Dec. 31, 2026. This opens up the opportunity for countries to begin applying the UTPR worldwide unless the U.S. is exempted.

**EU Melding DSTs With VAT**

Even with a side-by-side deal in place, Section 899 may reemerge because of DSTs. For the European Union countries with the levies, "there's currently no sign that these DSTs will be abolished," and, in fact, they're taking on new forms, Boldewijn of Greenberg Traurig said.

"Italy recently tried to put these digital services under the [value-added tax] system, which is now ... probably going through the European Court of Justice to determine whether or not this is valid under the EU VAT system," Boldewijn said.

The Italian government wants to treat user data provided to social media companies as consideration paid in exchange for their otherwise free services, the VAT committee of the European Commission, the EU's executive branch, reported in a November opinion. The committee thinks this interpretation may be valid if the company provides a reduced service to users who decline to provide their data, according to the nonbinding opinion. Rather than adopting DSTs, it's likely that EU countries will move toward Italy's approach, provided it holds up in court, Boldewijn said.

"I don't know whether that will already be clear in 2026, but it's definitely something that will impact the decisions of member states and the European Commission on how we continue with taxing the digital economy," he said.

**Pillar Two Tax Returns**

Come summer, most of the countries that have enacted Pillar Two will begin collecting the system's specialized tax returns and enforcing the full breadth of the interlocking provisions. This will take place June 30 for much of the EU, the U.K., Canada, Australia and South Korea, while other deadlines are sprinkled throughout the year.

Yen of EY said he's concerned some countries will try to "aggressively audit" these returns. Boldewijn mentioned Latin America as a potential hot spot for this risk.

Usually tax authorities provide "a little bit of grace" with first-time filings for a new tax, but a separate concern is how the information in the returns may be used elsewhere, Starling Marshall of Crowell & Moring LLP said.

"Now that information is out there, is it useful for enforcement in other instances?" Marshall said.

**U.S. International Tax Changes**

Most changes to international tax policies under Congress' latest budget begin to apply in 2026, said Eric Homsi of Crowell & Moring.

"It is important to understand their impact," Homsi said. "It will also be interesting to see whether the changes further President Trump's policy agenda."

Implementation of Congress' latest budget ranked as the most common priority for 2026 among tax professionals in a November survey by EY and The Tax Council, followed by international tax policy, including Pillar Two.

The renaming of key provisions, though least influential in principle, is important to note for clarity's sake. The global intangible low-taxed income, or GILTI, regime is now known as net controlled foreign corporation tested income, or NCTI. Likewise, the foreign-derived intangible income, or FDII, regime is now known as foreign-derived deduction-eligible income, or FDDEI.

Perhaps the most meaningful change to each of these systems is the new rules surrounding expense allocation, Yen said. Expenses for interest and research and experimentation no longer will be deductible under NCTI and FDDEI while expenses that are "directly allocable" to covered income will be, according to the new Section 904(b)(5) of the IRC. Companies are expecting guidance from Treasury on what exactly the law meant by "directly allocable," Yen said.

"Does that include things like stewardship and other sorts of general administrative costs?" Yen said.

At the same time, companies can now deduct expenses tied to interest and domestic research and experimentation from their U.S. taxable income without reducing benefits under NCTI and FDDEI.

Another "dramatic change" that will require further guidance from Treasury is the elimination of the so-called hot potato rule, overwriting 50-plus years of precedent, according to Yen.

Under Sections 951(a) and 951A(e), Subpart F and GILTI income had been assigned to U.S. shareholders of a controlled foreign corporation, or CFC, based on who held it on the final day of the year. Now that income will be assigned on a pro rata basis across all U.S. shareholders who owned the CFC's shares at any point during the year.

Companies are wondering how to apportion CFC income between two different periods under the new system, as "it's not something we really had to do before," Yen said. Since this issue is "quite complicated," he said he doesn't expect Treasury to issue guidance immediately, but "that will be very important for companies, because these kinds of transactions happen every day, and the statute itself, I think, is pretty spare in terms of how those rules will work."

In addition, CFCs are now required to use the same tax year as their majority U.S. shareholder following the budget's repeal of Section 898. This had provided shareholders the ability to defer one month of CFC income to the next tax year by using a one-month earlier tax year for the CFC.

These changes could increase Subpart F tax liabilities, but they also provide a more consistent treatment of CFC income, attorneys from Weil Gotshal & Manges LLP wrote for Law360 in August.

Treasury began issuing guidance and proposed regulations on the budget's international tax changes in early December, including a proposed anti-abuse rule for related-party transactions under FDDEI, which Marshall of Crowell & Moring said she's following closely.

The proposed rule is aimed at preventing companies from moving depreciable or amortized assets to related parties as a means of avoiding income from the asset's sale being excluded from deduction-eligible income, pursuant to the budget's new Section 250(b)(3)(A)(i)(VII)(bb). In turn, it prevents that income from being included in FDDEI.

"I would encourage clients to really take a look at those proposals and see if there are issues that they can plot now that would be worth submitting comments," Marshall said. "It's worth it to really think about whether there's something there that's objectionable."

Comments for the proposed rule are due Feb. 2. Treasury is also planning to issue a proposed transition rule that would prevent U.S. shareholders from reducing income under Subpart F and NCTI using untaxable CFC dividends before the budget's new inclusion rules take full effect, according to a December notice.

These proposed regulations are something to keep an eye on, Christine Lane of Crowell & Moring said.

"The notice and forthcoming proposed regulations are intended to provide symmetry on the meaning of dividends paid or deemed paid and provide clarity on certain other aspects of application of the transition rule, including a look-through rule for partnerships, S corporations and certain tiered structures," Lane said.

Although work has begun, understaffing at Treasury and the IRS — especially among legal advisers — engenders a "pessimistic" view about their ability to issue the highest-quality interpretations on the budget's changes in 2026, according to Marshall.

"You have an IRS without a chief counsel in place and a lot of leaders gone on that side who would be helpful experts to assist Treasury in understanding how their rules are being implemented in audit," Marshall said.

Regulators are also flying somewhat blind about how their interpretations will play out in audits because the IRS lacks a head of its Large Business and International Division, Marshall said.

"That's just going to leave Treasury without a lot of the necessary feedback that makes their regulations responsive to what is being seen by the examination teams in the field," she said.

Smith declined to comment.

Crapo and the OECD did not respond to requests for comment.

--Additional reporting by Asha Glover and Natalie Olivo. Editing by Tim Ruel and Emma Brauer.