Inclusive Framework BEPS Agreement

Update on Pillar 2 following Commentary Release – March 2022

Policy Perspectives update

KPMG Global Release: Executive Summary

On 14 March 2022, the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS) involving more than 140 countries, released Commentary related to the Model GloBE Rules under Pillar 2, which were first released on 20 December 2021. In addition to the March Commentary of 228 pages, a document containing 24 Examples and 49 pages was released to supplement the Commentary.

The Model, Commentary and Examples provide the framework for a Global Minimum Tax at 15% for Multi-national Enterprises (MNEs) with a turnover of more than €750 million.

Alongside the release of the Commentary, the OECD opened a public consultation on the administrative and compliance aspects of the GloBE Rules, including the potential terms of any simplifications and the use of Safe Harbors. Written comments are due no later than 11 April 2022. A follow-on public consultation meeting is scheduled for the end of April 2022.

The adoption of the new rules is based on a 'common approach' which means that jurisdictions are not required to adopt the rules, but if they choose to do so, they will implement the rules consistently with the model.

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The rules are due to be brought into law in each participating jurisdiction through domestic law changes in 2022, to be effective in 2023 for the Income Inclusion Rule (IIR), and in 2024 for the UTPR, which is a backstop to the IIR. There is also the potential for local jurisdictions to introduce a Qualifying Domestic Minimum Top-up Tax to tax entities in their jurisdiction, which could reduce or eliminate the amount of top-up taxes paid under the IIR or UTPR to nil. This timetable is ambitious.

The Commentary and Examples provide additional guidance to the Model Rules.

This KPMG document is an updated version of the analysis we released on 21 December 2021, having regard to the Commentary and Examples.

The US Administration has proposed modifications to the Global Intangible Low Taxed Income or GILTI rules, which are currently based on global blending. The Pillar 2 rules apply blending on a jurisdiction-by-jurisdiction basis. The prospects for changes to the GILTI rules to align with Pillar 2 remain uncertain.

We are also yet to see the details of the Subject to Tax Rule, which is part of the agreement under Pillar 2, and a key priority for developing nations. We will continue to share reflections on developments through our ongoing KPMG Global Tax Policy Perspectives series. You may also want to view our list of top-20 considerations for tax leaders.

Scope of the Global Minimum Tax

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Pillar 2 deals with new Global Anti-Base Erosion (or GloBE) or Global Minimum Tax rules. The agreed global minimum tax rate is 15%.

Revenue threshold

Generally, the GloBE rules apply for an MNE Group where consolidated group revenue exceeds €750 million. This is determined by looking at the consolidated financial statements. An entity located in one jurisdiction that has a permanent establishment in another jurisdiction is also deemed to be a group when applying the test. The Commentary makes it clear that the revenue in the financial statements should not be reduced for minority interests, nor is the revenue the aggregate of each Group Entity (i.e., the threshold applies to the consolidated revenue of the MNE Group and intra-group transactions are excluded from the revenue threshold). Also, the revenue of Excluded Entities will be included in consolidated group revenue for the purpose of the threshold.

Test years for consolidated revenue threshold

There is a four-year test period determining whether the threshold is met. Generally, if revenue of €750 million is exceeded in two of the previous four fiscal years, then the threshold is met. This excludes the fiscal year being tested. Where two groups merge, the test is deemed to be met for any year prior to the merger if the sum of the revenue of each group meets the €750m threshold. For demergers, the rules are more complex, with each of the demerged groups tested separately. Broadly, in the first fiscal year following the demerger, one applies the €750m threshold to the demerged group. In the second to fourth years following the demerger, the test is met if, in two out of four years (including the year after the demerger) the threshold of €750m is met.

Ultimate Parent Entity

There are a number of critical definitions which are essential to the determination of an MNE Group and its Constituent Entities which are potentially subject to the various Top-up Tax rules. One concept is the Ultimate Parent Entity (UPE). To be a UPE, a parent entity must generally have a controlling interest in another entity or entities such that it is (or would be) required to consolidate their assets, liabilities, income, and expenses on a line-by-line basis. A UPE may also consist of an entity operating a permanent establishment in another jurisdiction if such entity is not part of a larger MNE Group. An entity is not a UPE if there is an entity higher up the chain that is required to consolidate it on a line-by-line basis. The Commentary notes that this test is met if an entity is deemed to be consolidated without fully stating the nature and level of that deeming.

Excluded entities

Certain organizations, entities or arrangements are excluded from the GloBE Rules. Government Entities, which do not carry on a trade, International Organizations and Non-profit Organizations and Pension funds are fully excluded. In addition, Investment Funds and Real Estate Investment Vehicles are excluded, but only when they are the Ultimate Parent Entity of an MNE Group. The Commentary states that such rules are designed to protect the status of Investment Funds as tax neutral investments. Certain holding vehicles owned by these excluded entities are also themselves excluded based on an ownership test and an assets test, as discussed in Section 8. Importantly, there is an election available not to treat an entity as an excluded entity.

Exclusions – international shipping

There is an exclusion for international shipping income and certain related income. This applies to both the transportation of passengers and cargo but does not include income from transportation in inland waterways of the same jurisdiction. To qualify for the exclusion, the Constituent Entity must demonstrate that the strategic or commercial management of all ships concerned is effectively carried on from within the jurisdiction where the Constituent Entity is located. The Commentary notes that “strategic or commercial management” is determined on the basis of the relevant facts and circumstances and provides several “relevant factors”.

The Model Rules agreed in 2021 are to be implemented as part of a common approach which requires that countries do not introduce rules that are contrary to the basic design. The Commentary states that an IIR rule which is below the €750m threshold would be like any other controlled foreign corporation (CFC) rule and not contrary to the design, but that a UTPR with a lower threshold would be unacceptable.

Income inclusion rule

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Top-down approach & Intermediate Parents

The GloBE Rules are designed to ensure that large MNEs pay a minimum level of tax on the income arising in each jurisdiction in which they operate. To this end, and as explained further in Section 5, the rules calculate the ETR of the MNE in each jurisdiction. Where the ETR in a jurisdiction falls below 15% these rules determine an amount of top-up tax for each Constituent Entity in the jurisdiction.

The IIR is the primary rule to impose this top-up tax. Under the IIR a parent entity within the MNE group will pay tax, in its jurisdiction of tax residence, in respect of its allocable share of the top-up tax of a low-taxed Constituent Entity. In this regard the IIR bears similarities to CFC rules.

Under the top-down approach, priority is given to the parent entity at the highest point in the ownership chain. Therefore, in a multi-tiered structure, where the UPE of the MNE group is subject to a qualified IIR (i.e., one conformant to the GloBE Rules design), it will pay the IIR tax in respect of the top-up tax of a low-taxed Constituent Entity, rather than an intermediate parent entity. Where the UPE is not subject to a qualified IIR, IIR taxing rights will 'drop' down to the jurisdiction of the intermediate parent entity beneath it, to the extent it applies a qualified IIR and so on down the chain of ownership.

Split ownership rules

An exception to the top-down rules can apply where a low-taxed Constituent Entity has a significant (i.e., more than 20%) minority interest holder outside the MNE group. The split-ownership rules apply to address the potential for leakage that would result from simply subjecting the UPE's allocable share of the low-taxed Constituent Entity's income to IIR tax (as opposed to subjecting all such low-taxed income to tax at the UPE level).

For example, take the case where the UPE has a 75% ownership interest in an intermediate parent entity, and the latter has a 100% ownership interest in a low-taxed Constituent Entity. In this case, the IIR taxing rights would 'drop' to the jurisdiction of the intermediate parent entity, assuming the latter applies a qualified IIR. This is termed a 'partially-owned parent entity'. The effect of the rule is that 100% of the top-up tax is subject to IIR tax at the level of the partially owned parent entity, rather than 75% of top-up tax being taxed at the level of the UPE. The rules provide that the allocable share of higher-tier parents (e.g., 75% share of the UPE in this case) will be reduced to the extent IIR tax is imposed by lower tier parents (i.e., down to zero in this case).

The Commentary provides extensive clarification on how the parent allocable share is determined, which includes a hypothetical accounting consolidation exercise, as well as illustrative examples. The example scenarios elaborate on how IIR tax impositions at the level of UPEs, intermediate parent entities, and partially-owned parent entities interact, including deactivation and offset rules.

Optional application to local entities

The Commentary clarifies that jurisdictions can extend the operation of the IIR to domestic low-taxed Constituent Entities. A local parent would then be obligated to pay IIR tax not just in respect of top-up tax for foreign entities in which it has an ownership interest, but also for top-up tax in respect of local entities in which the parent has an interest, as well as top-up tax arising at the level of the parent itself. This is the direction of travel taken by the draft EU Pillar 2 directive. It is noted though that a Qualified Domestic Minimum Top-up Tax (as defined herein) would still have precedence over such a domestically applied IIR, as would an IIR applied at the level of a higher tier parent in another country that is given priority under the top-down approach.

UTPR

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Situations where UTPR applicable and top-up tax calculation

The UTPR operates as a backstop to the IIR, to be applied where insufficient top-up tax is collected under the IIR. Importantly, the UTPR also serves the purpose of ensuring low-tax income in the UPE jurisdiction is subject to tax at the minimum rate. Central to the application of the UTPR is the determination of the Total UTPR top-up tax amount. This is an aggregate 'pool' of all the top-up tax of low-taxed Constituent Entities, across the MNE group, which is not adequately taxed by an IIR or otherwise excluded.

The amount of the top-up tax for a given low-taxed Constituent Entity for this purpose depends on whether all of the UPE's ownership interests in such low-taxed Constituent Entity are held directly or indirectly by a parent entity required to apply a qualified IIR in respect of such entity. If so, then the top-up tax in respect of such entity is reduced to zero. However, if not, then the amount of the top-up tax in respect of such entity is reduced by the amount of top-up tax brought into charge under a qualified IIR. For example, if the UPE has a 75% ownership interest in a low-taxed Constituent Entity, and the IIRs applied at the level of group parents (including partially owned parent entities) tax the full 75% of the low-taxed Constituent Entities' top-up tax, then for UTPR purposes the low-taxed Constituent Entities' top-up tax will be reduced to zero (despite 25% of the top-up tax remaining untaxed). If this is not the case (e.g., group parents subject 74% of the potential 75% to IIR, as the 1% holder is not an IIR-applying jurisdiction), then the top-up tax is not reduced to zero. Instead, the top-up tax for UTPR purposes is reduced by the amount subject to IIR (e.g., 26% remains). These core rules are accompanied by special rules.

In the case of a Joint Venture (JV), for example, the top-up tax 'ceiling' for the UTPR is the UPE's ownership interest in the JV (e.g., 50% of JV top-up tax for a 50%-owned JV). For investment entities within a group, the UTPR does not apply.

Denial of a deduction or other mechanism

The total UTPR top-up tax is allocated to jurisdictions in which the MNE has Constituent Entities, and which have adopted the UTPR into law (UTPR jurisdictions). It is left open to UTPR jurisdiction tax authorities how they go about ensuring that the Constituent Entities in their jurisdiction have an additional cash tax expense equal to the allocation for the fiscal year. It could be by way of denial of tax deductions of any type, including for notional expenses. Alternatively, an equivalent adjustment could be used, e.g., deemed taxable income or a new tax. Notably, the Commentary emphasizes that such measures would need to be coordinated with obligations under tax treaties.

The rules provide that to the extent that top-up tax allocations cannot be imposed as cash tax immediately, for example due to a lack of deductions that can be denied or due to significant local tax losses, the additional cash tax expense may end up arising in a subsequent year. The Commentary sets out the various scenarios in which these rules can play out, including future utilization of tax losses limited by UTPR deduction denials, or carry forward of the UTPR tax for imposition in a future year (particularly relevant where local tax losses are time limited). These are supported by illustrative examples. Filing requirements are established to track the payment of the additional cash tax over time.

The Commentary notes that UTPR jurisdictions have considerable latitude in how they allocate the UTPR burden over the Constituent Entities in a jurisdiction. This may involve making allocations to wholly owned entities first, before allocation to partly owned entities, to limit impositions on minority owners. Jurisdictions are free to set rules that can change the burden allocation amongst local Constituent Entities, from one year to the next, to the extent this may expedite the collection of the tax.

Jurisdictions are also free to decide what happens in situations such as an entity, originally subject to UTPR tax, leaving an MNE group – the jurisdiction could let the burden remain with the departing entity or have it reallocated to remaining group members. Given that the GloBE Information Return is filed 15 months after group fiscal year end (extended to 18 months in the first fiscal year that the MNE Group is within scope), jurisdictions may also provide for filing of amended returns by local Constituent Entities, to collect the UTPR tax for the local tax year that aligns to the relevant MNE fiscal year.

Allocation key for UTPR

The allocation mechanism for the total UTPR top-up tax takes into account the relative 'substance' of Constituent Entities in UTPR jurisdictions. A given jurisdiction's UTPR percentage (i.e., the share they are allocated of the total UTPR top-up tax) is determined by calculating (i) the jurisdiction's number of employees as a proportion of the total employees in UTPR jurisdictions, and (ii) the carrying value of the tangible assets in the jurisdiction as a proportion of the total carrying value of tangible assets in all UTPR jurisdictions. Each of these proportions is given a 50% weighting in determining the UTPR percentage.

Employee numbers and tangible assets are evaluated largely in the same manner as for country-by-country reporting (CBCR), though employees will be treated as located in the jurisdiction of a Permanent Establishment to the extent the separate Permanent Establishment accounts include the relevant payroll. The Commentary provides further detail on the determinations, such as allocating employees and assets of flow through entities, though notes that additional guidance will need be developed under the GloBE Implementation Framework (e.g., with regard to staff working in multiple jurisdictions).

An important feature of the allocation key is that if a UTPR jurisdiction does not fully collect the top-up tax allocated to them for a given fiscal year (by imposing additional cash tax), then their UTPR percentage is reduced to zero for subsequent periods until the amount from the previous years has been imposed. This would mean that a UTPR jurisdiction is incentivized to impose UTPR top-up tax allocations expeditiously, to avoid loss of allocations in future years which would otherwise be shared amongst other jurisdictions. The Commentary provides illustrative examples.

Covered taxes

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Taxes on income and adjustments

For each fiscal year, the ETR for a jurisdiction is determined as the total adjusted covered taxes for the Constituent Entities in a jurisdiction, divided by the net GloBE income or loss of the jurisdiction. The starting point for Constituent Entity adjusted covered taxes is the current tax expense accrued in the Constituent Entity financial accounts in respect of covered taxes – this is then subject to various adjustments (including in respect of deferred taxes). This makes it important to understand (i) the meaning of covered taxes and (ii) the nature of the various adjustments.

Covered taxes are defined to include taxes recorded in respect of a Constituent Entities' net income, as well as taxes in lieu of a corporate income tax (e.g., withholding tax on foreign income), taxes imposed under eligible distribution tax systems and on retained earnings and corporate equity (e.g., Zakat in Saudi Arabia). The Commentary provides further detail on the assessment of whether a tax is covered, noting for example that Pillar One Amount A tax and STTR tax will be covered taxes, while digital services taxes are not.

The adjustments made to the current tax expense number include reductions for amounts related to excluded income. Examples include, dividends received other than those in respect of a short-term portfolio shareholding, uncertain tax positions, accrued taxes not paid within 3 years, and adjustments for certain refundable tax credits. There is also a mechanism to address temporary differences, which draws on deferred tax accounting, with several adjustments. The Commentary provides illustrative examples on these adjustments.

Specific provisions also deal with post-filing adjustments to Constituent Entities covered tax liabilities; this can trigger recalculation of prior year ETRs and top-up tax amounts.

R&D Credits

On the specific area of R&D tax credits, practice differs across countries on whether refunds are granted – some allow for refunds and others do not. For those providing for refunds, some limit these to smaller enterprises which may not be in scope of GloBE. It remains to be seen to what extent countries might, in response to GloBE, update their R&D credit provisions to make them refundable so that they can be treated as an increase to GloBE income, rather than as a reduction to Covered taxes, allowing for a higher ETR calculation. It may be that some countries conclude that a shift to R&D grants is the better approach.

Allocation of taxes between Constituent Entities

In arriving at adjusted covered taxes it is sometimes necessary allocate some covered taxes from one Constituent Entity to another.

For example, withholding taxes suffered on a distribution received by a recipient Constituent Entity and recorded in its accounts, will be allocated to the distributing Constituent Entity as its covered tax. Specific provisions cover Constituent Entity to Constituent Entity allocations for Permanent Establishments and hybrid entities (both treated as Constituent Entities) as well as in relation to CFC and transparent entity taxes. The Commentary provides further detail on how these allocations are to be performed but notes that, in view of the specificities of certain country's tax regimes, common allocation methodologies will need to be further developed under the GloBE Implementation Framework.

The pushdown of taxes in respect of passive income earned by CFC and hybrid entities is capped. The policy justification for this capping mechanism is unclear, but as explained in the Commentary, the intent is to limit the ability to blend taxes paid on that passive income in the Constituent Entity-owner's high tax jurisdiction with other income arising in the low-tax jurisdiction.

Deferred tax to address timing differences

As noted above, a key step in arriving at the number for Constituent Entity adjusted covered taxes is the adjustment for deferred tax. This is intended to address the ETR volatility that would otherwise arise due to accounting (book) to tax differences. Carryforward tax losses are also effectively dealt with by means of deferred tax assets (DTAs). While the calculation of the number for inclusion in Constituent Entity adjusted covered taxes starts with the Constituent Entity's accounting deferred tax expense accrued, there are a number of adjustments required. There are also special transitional rules for deferred tax attributes existing when an MNE Group first comes within the scope of the GloBE Rules.

Deferred tax attributes must be recast at the 15% rate, where calculated using a tax rate in excess of 15%. Furthermore, deferred tax assets calculated at a lower rate may be recast up to 15%, to the extent they relate to GloBE losses in order that these losses adequately offset any top-up tax otherwise due in respect of an equal amount of income earned in the future in such jurisdiction. Any deferred tax valuation allowances made must be reversed, as well as any adjustments made in response to changes in tax rates. Deferred tax recorded in respect of tax credits or uncertain tax positions must be removed.

Where a deferred tax liability, initially reflected in Constituent Entity adjusted covered taxes, does not reverse within 5 years, then this must be reversed out and a retrospective ETR recalculation performed; alternatively, the Constituent Entity can choose not to include it in covered taxes in the first instance. However, for a prescribed list of deferred tax liabilities, this 5-year reversal rule does not apply.

There is also a special 'alternative' regime that can be used (on election and made on a jurisdiction-by-jurisdiction basis) in lieu of these deferred tax provisions. It provides for the calculation of a deemed DTA for certain losses at the minimum rate and its carry forward for inclusion in adjusted covered taxes. This may be particularly relevant for no/low tax jurisdictions.

The Commentary provides additional insights on how the deferred tax provisions are to apply. It indicates, for example, that deferred tax liabilities must be tracked on an item basis to see if they reverse within 5 years, though it remains to be seen if the GloBE Implementation Framework guidance may allow for category level tracking.

The Commentary confirms (including with an illustrative example) that article 4.1.5 can cause top-up tax to be payable for a jurisdiction where the Constituent Entity is in a loss position for the relevant year. This situation arises where the entity has, in tandem with a GloBE loss, a permanent benefit for tax purposes such as an enhanced deduction. The Commentary also explains how local tax loss carry backs are to interact with the deferred tax provisions.

Effective Tax Rate – Normal Cases

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The GloBE rules prescribe that the ETR of the MNE Group for a jurisdiction with Net GloBE Income is calculated for each Fiscal Year. The ETR of the MNE Group for a jurisdiction is equal to the sum of the Adjusted Covered Taxes of each Constituent Entity located in the jurisdiction (numerator) divided by the Net GloBE Income of the jurisdiction for the Fiscal Year (denominator). For the purposes of this rule, each Stateless Constituent Entity shall be treated as a single Constituent Entity located in a separate jurisdiction.

Calculation of Net GloBE Income

The Net GloBE Income of a jurisdiction for a Fiscal Year is the positive amount, if any, computed in accordance with the following formula:

Net GloBE Income = GloBE Income of all Constituent Entities from that jurisdiction - GloBE Losses of all Constituent Entities from that jurisdiction.

GloBE income of each Constituent Entity is defined as the financial accounting net income or loss determined for the Constituent Entity for the Fiscal Year adjusted for certain specific items.

Two of the most notable adjustments are in respect of stock-based compensation expense and the treatment of certain “qualified refundable tax credits.” As relevant to stock-based compensation, the Model Rules allow Constituent Entities to make an election (that applies to all Constituent Entities in a jurisdiction) to substitute the amount allowed as a deduction in the computation of its taxable income for the amount expensed in its financial accounts. The intent of this rule seems to be to prevent top-up tax arising in respect of book-to-tax differences associated with stock-based compensation plans.

With respect to refundable tax credits, the Model Rules provide that qualified refundable tax credits (generally refundable tax credits that require the portion of which has not already been used to reduce covered taxes be paid as cash or cash equivalents within four years) be treated as income, whereas other nonqualified refundable tax credits are instead treated as offsets to covered tax expense. The assessment of whether a credit is refundable for purposes of the GloBE Rules is made on an objective, rather than taxpayer-specific, basis. If the tax credit regime provides for only a partial refund, such that only a fixed portion is refundable, then the refundable portion of the credit may be treated as a qualified refundable tax credit, provided that it will become refundable within four years from when the conditions for granting the credit are met. Although the Model Rules do not explicitly address government grants, such grants would generally be included in GloBE Income based on general financial accounting principles.

Adjusted Covered Taxes and GloBE Income or Loss of Constituent Entities that are Investment Entities are excluded from the determination of the Effective Tax Rate and the determination of Net GloBE Income and dealt with separately under special rules.

Effective Tax Rate – special cases

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Adjustments to the calculation of the GloBE ETR to account for certain special circumstances.

Constituent Entities joining and leaving a group

Under the Model Rules, and as elaborated in the Commentary, special provisions apply to disposals and acquisitions of a controlling interest in an entity (target) that results in such entity becoming or ceasing to be a Constituent Entity of an MNE Group. The Commentary explains that because the GloBE rules are drafted as if the MNE Group and its Constituent Entities will continue in a steady state, the rules for acquisitions and dispositions are included to ensure that the results of the target are properly reflected in the consolidated financials of both the acquiring and disposing MNE Group.

In general, a target is treated as a member of a group in an acquisition year if any portion of its assets, liabilities, income, expenses, or cash flows are reflected on a line-by-line basis in the consolidated financial statements of the UPE for the year. As a result, a Constituent Entity may be considered a member of two MNE Groups in the year of an acquisition. In the acquisition year, only the target's income and taxes that are reflected in the UPE's consolidated financial statements are considered for GloBE purposes. Further, in the year of acquisition, the target may be required to apply the IIR of its jurisdiction in respect of low-taxed constituent entities in both MNE Group's if it is a parent entity in respect of such low-taxed entities and the relevant UPEs of each group are not subject to qualified IIRs.

As provided in the Model Rules, the target's income and taxes (during the acquisition year and all succeeding years) are determined using the historical carrying value of its assets and liabilities, rather than the fair market value, as permitted under the financial accounting rules of certain jurisdictions. The Commentary explains that these rules related to the carrying value are necessary to align the treatment of the seller and the buyer, to prevent gain and loss with respect to the target's assets from going untaxed under the GloBE Income and Loss computation rules, and to provide consistency as the domestic laws of the Inclusive Framework jurisdictions may not provide for purchase accounting adjustments. This rule applies regardless of whether the acquisition took place before the effective date of the GloBE Rules, with a limited exception for acquisitions occurring prior to 1 December 2021.

For purposes of applying the substance-based exclusion, the amount of payroll costs taken into account reflect only those included in the MNE Group's financial statements and the carrying value of the target's assets (which solely for this purpose does take into account purchase accounting adjustments) is adjusted based on the period during which the target was a member of each MNE Group. The annex to the Commentary provides an example of the application of these rules. In the example, a MNE Group (the "disposing group") sells a Constituent Entity ("target") that owns an asset to another MNE Group (the "acquiring group"). Consistent with the rules for allocating the carrying value of an asset, the example illustrates that target's asset carrying value is proportionately allocated between the disposing group and acquiring group based on the time period that each owned target during the fiscal year of the sale.

Moreover, for purposes of applying the deferred tax accounting rules:

a) Deferred tax items, except for certain losses for which an election has been made, that transfer from the disposing MNE Group to the acquiring MNE Group are taken into account by the acquiring MNE Group as if the acquiring MNE Group controlled the target when those deferred items arose;

b) From the perspective of the disposing MNE Group, the target's deferred tax liabilities are deemed to have fully reversed (as relevant to the 5-year reversal requirement for deferred tax liabilities);

c) From the perspective of the acquiring MNE Group, the target's deferred tax liabilities are treated as arising in the acquisition year, and if the deferred tax liability does not reverse within 5 years of the acquisition year, it is treated as a reduction to covered taxes in the recapture year, rather than the year the deferred liability arose.

Transfers of assets and liabilities and certain reorganizations

The Model Rules provide separate provisions that govern a Constituent Entity's disposition or acquisition of assets and liabilities. In the case of a disposition of assets and liabilities, the disposing entity will include the gain or loss on the disposition in its GloBE Income or Loss and the acquiring entity will determine its GloBE Income or Loss using the acquiring entity's carrying value of the assets and liabilities under the accounting standard used in the UPE's consolidated financial statements. Note that, for these purposes, the Model Rules treat an acquisition or disposal of a controlling interest in a Constituent Entity as a disposal of the assets and liabilities if the target's jurisdiction taxes the transaction as a deemed transfer of assets and liabilities.

The Commentary indicates that the intent of this rule is to align, for GloBE purposes, the amount realized by the disposing entity with the acquiring entity's adjusted carrying value for financial accounting purposes. Thus, unlike the results discussed above that apply in the case of a disposition of a controlling ownership interest in a Constituent Entity, a disposition of assets and liabilities generally does not result in inconsistencies in the treatment of the buyer and seller and the risk of gain or loss on the acquired assets from being taken into account under the GloBE rules upon a future disposition.

Consistent with this intent, the disposing entity's GloBE Income or Loss generally will exclude any amount realized as part of a "GloBE Reorganization", and the acquiring entity will inherit the disposing entity's carrying values of the acquired assets and liabilities (except to the extent of gain recognized). This result is consistent with the rules described above for acquisitions and disposals of ownership interest in a Constituent Entity in which the target does not recognize gain or loss upon the disposition.

A GloBE Reorganization is generally a transfer of assets and liabilities such as a merger, demerger, liquidation, or similar transaction where (i) the consideration for the transfer is in whole or significant part equity interests issued by the acquiring entity (or the target entity in the case of a liquidation); (ii) the disposing entity's gain or loss on the assets is not taxed in whole or in part; and (iii) the tax laws of the jurisdiction of the acquiring entity requires the acquiring entity to compute taxable income using the disposing entity's tax basis in the assets. If certain non-qualifying consideration is received pursuant to the GloBE Reorganization, however, the disposing entity's GloBE Income or Loss will include the associated gain or loss and the acquiring entity's carrying value will be adjusted consistent with local tax rules.

Additionally, in certain instances, an election is available that would allow a Constituent Entity to make certain adjustments and use the fair value of assets or liabilities on a go-forward basis provided it recognizes GloBE income or loss in respect of such assets and liabilities.

Multi-Parented MNE Groups

If two or more MNE Groups meet the definition of a Dual-listed Arrangement or a Stapled Structure, then the MNE Groups will be treated as a single MNE Group (Multi-Parented MNE Group) and Entities and Constituent Entities of each Group will be treated as members of a single Group. A "Stapled Structure" is an arrangement under which 50% or more of the Ownership Interests in the UPEs of each separate Group are "stapled" together (i.e., combined through their form of ownership, restrictions on transfer, or other terms and conditions that precludes separate transfer or trading) as if they were the Ownership Interests of a single Entity. A "Dual-listed Arrangement" is an arrangement whereby the UPEs combine their businesses through contract (rather than ownership) and the activities of the combined groups are collectively managed as if carried out by a single economic entity, despite that the Groups may trade independently. In addition to the foregoing, under a Stapled Structure and a Dual-listed arrangement, the UPEs must prepare consolidated financial statements in which the Groups are presented as a single economic unit.

For purposes of determining the composition of the Multi-Parented MNE Group, the Model Rules treat each Entity of either MNE Group as an Entity of the Multi-Parented MNE Group, including when applying the consolidated revenue threshold. The Model Rules also treat any Entity, except an Excluded Entity, as a Constituent Entity of a Multi-Parented MNE Group, if such Entity is consolidated on a line-by-line basis with the Multi-Parented MNE Group, or its Controlling Interests are held by Entities of such Multi-Parented MNE Group. This two-pronged test for determining when an Entity is a Constituent Entity of a Multi-Parented MNE Group is intended to expand the definition of Constituent Entity to include those Entities that would not meet the Constituent Entity definitional requirements if each MNE Group were tested on a standalone basis, but where such definitional requirements are met when the MNE Groups are tested on a combined basis.

The Consolidated Financial Statements of the Multi-Parented MNE Group are those referred to in the definition of Stapled Structure or Dual-listed Arrangement that present the Group as a single economic unit. As applied to Multi-Parented MNE Groups, references in the Model Rules to the accounting standard of the UPE are deemed to be the accounting standard used to prepare the Multi-Parented MNE Group's Consolidated Financial Statements.

The UPE of each Group is treated as a UPE under the Model Rules, such that the Multi-Parented MNE Group will have two or more UPEs that must each apply the IIR in the jurisdiction in which each is located with respect to each's Allocable Share of the Top-Up Tax of Low-Taxed Constituent Entities. While the split ownership rules are also applicable, the determination of whether an Entity is a POPE must take into account the UPE's Ownership Interests in an Entity on a combined basis. Accordingly, an Entity that would meet the ownership requirements to be treated as a POPE for a stand-alone MNE Group will not be treated as a POPE if the Multi-Parented MNE Group, on an aggregate basis, held 80% or greater of the Ownership Interests of such Entity.

If only one UPE of the Multi-Parented MNE Group is subject to a Qualified IIR, then the application of the top-down approach will depend on the Multi-Parented MNE Group's legal holding structure. For instance, if a UPE that is subject to a Qualified IIR has an Ownership Interest in an Intermediate Parent Entity, then such UPE and not the Intermediate Parent Entity will apply the IIR provided that the other UPE that is not subject to a Qualified IIR does not hold any of the Ownership Interest in the Intermediate Parent Entity. Alternatively, if an Intermediate Parent Entity is at least partially owned by a UPE that is not subject to a Qualified IIR, then the Intermediate Parent Entity is required to apply the IIR based on its Allocable Share of the Top-Up Tax of the LTCE and the other UPE that is subject to a Qualified IIR would reduce its Allocable Share of the Top-Tax of the LTCE.

With respect to the UTPR, all the Constituent Entities located in an implementing jurisdiction are to apply the UTPR, taking into account all relevant members of the Multi-Parented MNE Group. Accordingly, an Entity that would otherwise be a Constituent Entity of only one of the MNE Groups can be required to apply the UTPR with respect to an amount of Top-up Tax of a Constituent Entity of the other MNE Group.

Finally, both UPEs must submit the GloBE Information Return, unless a single Designated Filing Entity is appointed, which could be one of the UPEs or another Constituent Entity of the Multi-Parented MNE Group. Each GloBE Information Return must include information as if all of the MNE Groups were a single MNE Group.

Equity method accounting

The financial accounting net income or loss and covered taxes of an entity that is not a Constituent Entity are generally excluded from the application of the GloBE Rules to the MNE Group. Financial accounting standards typically require "equity method accounting", in which an owner includes its proportionate share of the Entity's after-tax income or loss in the computation of its Financial Accounting Net Income or Loss when the MNE Group holds a significant but non-Controlling Interest in an Entity, ordinarily between 20% and 50% of the equity interests in an Entity.

Accordingly, the Model Rules generally require adjustments to Financial Accounting Net Income or Loss to exclude amounts otherwise included under the equity method of accounting when computing GloBE Income or Loss. Equity method income or loss is excluded from the computation of GloBE Income or Loss without regard to whether the owner has included any such amount in its taxable income computation under its relevant tax law. For example, income or loss under the equity method is removed from the owner's GloBE Income or Loss computation even if the Entity is treated as a Tax Transparent Entity (such as a partnership) in the owner's tax jurisdiction. Likewise, covered taxes attributable to income under the equity method are removed when determining the owner's GloBE ETR.

Note that certain entities subject to the equity method of accounting that are more than 50% owned by an MNE Group may be treated as JVs under the Model Rules and thus Top-Up Tax may be required in respect of such entities under the rules applicable to JVs.

Treatment of Flow-Through Entities, Hybrids and JVs

The manner in which the GloBE Rules apply to a MNE Group's investment in flow-through entities, hybrids, and JVs depends in the first instance on whether the financial results of such entity are consolidated with those of the MNE Group, rendering such entity a Constituent Entity.

If such entity is a Constituent Entity, the general rules for computing financial accounting net income or loss and covered taxes would apply, with special rules to address fiscally transparent Constituent Entities. If a Constituent entity is fiscally transparent in its or its owner's jurisdiction, the financial accounting net income or loss (and the corresponding covered taxes) of the Constituent Entity that is fiscally transparent in its or its owner's jurisdiction is allocated to a particular jurisdiction (or a permanent establishment thereof, as applicable) based on the tax treatment of the entity in its jurisdiction and in the jurisdiction of each Constituent Entity-owner.

The allocation of the financial accounting net income or loss and covered taxes of such an entity is done separately for each ownership interest in the entity because the treatment of such entity as transparent or not may vary across jurisdictions of its Constituent Entity-owners. A flow-through entity may be a tax transparent entity or a reverse hybrid entity depending on the treatment of such entity in the jurisdiction of its owner. For example, the income and taxes of a tax transparent entity (i.e., an entity treated as fiscally transparent in its

jurisdiction as well as that of its owner) generally are assigned to the jurisdiction of such owner, while the income and taxes of a reverse hybrid entity are treated as stateless and tested separately.

The GloBE Income or Loss and covered taxes of a hybrid entity generally are allocated to the hybrid entity, including any covered taxes contained in the financial accounts of a Constituent Entity-owner of a hybrid entity in respect of income or loss of the hybrid entity.

The Commentary clarifies that an entity may be considered fiscally transparent with respect to some, but not all, of its items of income, expenditure, profit, or loss. To illustrate this point, the Commentary provides an example of a trust that is subject to tax in its jurisdiction of creation except to the extent of income attributable to its beneficiary. In such case, the trust would only be considered fiscally transparent to the extent of the income attributable to the beneficiary, but not with respect to its other items of income.

The financial accounting net income or loss and covered taxes of fiscally transparent entities that are not Constituent Entities generally are excluded from the application of the GloBE Rules to the MNE Group. However, if a fiscally transparent entity is not a Constituent Entity but qualifies as a JV, special rules would apply to the income and taxes of the JV and its consolidated subsidiaries ("JV subsidiaries" and together, a "JV group"). For this purpose, the Model Rules define a JV as an entity in which the UPE holds, directly or indirectly, at least 50% of the ownership interests of such entity, and the results of such JV are included in the financial statements of the MNE Group under the equity method of accounting, subject to certain exclusions.

Significantly, the Commentary acknowledges that this definition departs from the definition commonly used in accounting rules under which a less than 50-percent owned entity may still be considered a JV for such purposes. Additionally, the Commentary explains that while a MNE Group may also own other minority interests in entities that are considered "JVs" or "associates" under accounting rules based on the MNE Group's significant influence over the entity, such entity -- because it would not meet the 50% threshold -- would not be subject to the special rules for JVs.

The Commentary specifies that in computing the jurisdictional ETR of members of a JV Group, the JV group's (rather than the MNE Group's) accounting standards would apply. Moreover, the GloBE income or loss and covered taxes of members of a JV group are not blended with the GloBE income or loss and covered taxes of other Constituent Entities of the MNE Group for purposes of computing the relevant jurisdictional ETR. Nevertheless, the Commentary clarifies that covered taxes recorded in the financial accounts of Constituent Entities within the MNE Group that are recognized with respect to GloBE income or loss of the JV group members should be taken into account for purposes of determining the jurisdictional ETR of members of the JV Group.

A Parent Entity holding (directly or indirectly) ownership interests in a member of the JV group would apply the IIR with respect to its allocable share of the top-up tax of such member (in accordance with the general IIR rules, including the "top-down" approach and split-ownership rules). The Commentary provides an example where an MNE Group owns 50% of a JV that is a low-taxed Constituent Entity with a Top-Up Tax of 100. The MNE Group's allocable share of such top-up tax is therefore 50.

The UPE's allocable share of the top-up tax of all members of the JV group (the "JV Group top-up tax") would then be reduced by the amount of top-up tax included by a Parent Entity under an IIR, and any remaining amount of JV Group Top-Up Tax would be added to the total UTPR Top-Up Tax and allocated to members of the MNE Group in accordance with the general rules.

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Substance-based Income Exclusion

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The GloBE rules provide for a substance carve-out based on the return to payroll and tangible assets.

Calculating the Substance-based Income Exclusion

The Substance-based Income Exclusion will reduce the amount of GloBE income to which the top-up tax percentage is otherwise applied.

The payroll component is based on determining the payroll costs of employees of the relevant MNE entity. A wide concept of employees is adopted and must include independent contractors who are natural persons or employed by an employment company whose daily activities are directed by the MNE entity, but not employees of a corporate contractor providing goods or services.

The rules look to where the activities of an employee take place and not the location of the employer. The Commentary states consideration will be given to the development of administrative guidance to address the situation where employees work in another jurisdiction or multiple jurisdictions. Payroll costs (apart from payroll costs capitalized into tangible assets) are also widely defined and include employee benefits, certain pension fund payments and related taxes, and stock-based compensation.

The tangible asset component is based on the carrying value in the Financial Accounts (with certain safeguards) of plant, property, equipment, land use rights and land (excluding land held for development). There are special rules for self-constructed assets, natural resources, and leased assets which aim at equivalent treatment. Special rules will be developed for tangible assets that are used in more than one jurisdiction.

The amount of the Substance-based Income Exclusion is the sum of a percentage applied to the payroll and tangible asset components. For the payroll component, the percentage starts at 10% and declines by 0.2 percentage points per year for the first 5 years to 9%, and then by 0.8 percentage points per year to reach 5% after 10 years. For the tangible asset component, the percentage starts at 8% and declines by 0.2 percentage points per year for 5 years to reach 7% and then by 0.4 percentage points for 5 years to also reach 5% after 10 years.

The Commentary states that the Substance-based Income Exclusion is determined based on jurisdictional blending such that if a Low Taxed Constituent Entity in a jurisdiction is in losses or with very low profit, its Substance-based Income Exclusion may still be used to reduce the potential top-up tax of the other blended entities in the jurisdiction.

Applying the Substance based Income Exclusion

The Substance-based Income Exclusion is subtracted from GloBE Income in a jurisdiction to produce the Excess Profit in such jurisdiction. This Excess Profit is multiplied by the top-up tax percentage (being the difference between the 15% minimum rate and the ETR for the local jurisdiction (without adjustment for the carveout.)

This product gives the top-up tax amount which is reduced by any Domestic Top Up Tax (i.e., the amount payable under a Qualified Domestic Minimum Top-up Tax in respect of such jurisdiction) imposed locally and any additional top-up tax that results from certain specified recalculations. A Qualified Domestic Minimum Top-up Tax is a minimum tax imposed by a jurisdiction on Excess Profits in such jurisdiction in a manner consistent with the GloBE Rules. A number of investment hub jurisdictions have already made public indications that they are exploring implementing such a regime. The result then flows through to the IIR or the UTPR as discussed above.

A Substance-based Income Exclusion amount that is not utilized cannot be carried forward or back. There is also an election not to apply the Substance-based Income Exclusion.

By way of example, say that an MNE's Constituent Entity in Country A has payroll of €100, a carrying value of tangible assets of €200, financial accounts profits of €100 and tax paid of €10. Assume that when profits are adjusted for the GloBE rules, the Net GloBE Income remains as €100, and the covered taxes remain as €10.

The ETR is 10% (€10/€100). The substance-based income exclusion is calculated as €26 (applying 10% and 8% to payroll and assets for year 1, respectively).

Excess profits are consequently €74 (€100 – €26). Applying the 5% (15%-10%) top-up tax rate to the Excess Profit yields top-up tax of €3.70, which is taxed through the IIR and/or UTPR. However, this would be reduced to nil if a Domestic Top-up Tax was applied by Country A.

De minimis Exclusion

There is a de minimis exclusion, available through an election made in respect of a jurisdiction, which applies to all entities in such jurisdiction unless those entities are not eligible, such as Investment Entities. The exclusion requires that the Average GloBE Revenue of the MNE Group for the jurisdiction is less than €10m. The second condition is that the Average GloBE Income (or Loss) for the jurisdiction is less than €1 million. Both tests use a three-year average based on the current year and the previous two fiscal years. The Commentary states that the election does not require separate calculations for Minority Owned Subgroups as if they were separate groups. The election is available on an annual basis. The Commentary notes that there will be some volatility if a significant amount of income arises or drops out of the three-year average.

Investment Funds

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Scope

The GloBE rules, as elaborated in the Commentary, provide for several categories of Excluded Entities ranging from Governmental Entities to Non-profit organizations and Pension Funds. If such organization or entity qualifies as an Excluded Entity, the GloBE Rules would not apply.

The list of Excluded Entities specifically also includes Investment Funds and Real Estate Investment Vehicles that are the UPE of an MNE Group. The rationale for the exclusion for Investment Funds is, according to the Commentary, found in the need to protect the status of these funds as tax neutral investment vehicles.

If an Investment Fund is not the UPE of an MNE Group, it can still be treated as a Constituent Entity of an MNE Group, provided it is consolidated on a line-by-line basis in the Consolidated Financial Statements of the UPE. Special rules then apply to calculate the GloBE ETR.

Definition of an Investment Fund

An Investment Fund is an entity that meets all of the following criteria: (i) it is designed to pool assets from a number of investors, some of which are unconnected; (ii) it invests in accordance with a defined investment policy; (iii) it allows investors to reduce transaction, research or analytic costs, or to spread risk collectively; (iv) it is primarily designed to generate investment income and/or gains or protect against a particular event or outcome; (v) where investors have a right to return from the assets of the fund or income earned on those assets, based on contributions made by investors; (vi) where the entity or the fund manager is subject to a regulatory regime in its jurisdiction of establishment or management; and (vii) where the fund is managed by fund management professionals on behalf of investors.

Vehicles owned by Excluded Entities

The GloBE rules recognize that Investment Funds may be required, for regulatory or commercial reasons, to use special purpose vehicles to hold assets or to carry out specific functions through separate controlled entities, that therefore become part of the Investment Fund infrastructure. Under the GloBE Rules, these vehicles may also qualify as Excluded Entities. To this end, the Rules prescribe that Excluded Entities include:

a. Entities that meet the ownership test whereby at least 95% of the value of the Entity is owned (directly or indirectly) by Excluded Entities, and these Entities meet the activities test whereby they i.) operate either exclusively or almost exclusively to hold assets of investment funds (pure holding vehicles) or ii.) they only carry out activities that are ancillary to the activities of the Investment Fund

b. Entities of which at least 85% of the value of the Entity is owned (directly or indirectly) by Excluded Entities provided that substantially all the Entity's income is Excluded Dividends or Equity Gain or Loss

Other issues

Questions on the rules for consolidation of group companies remain, including whether Investment Funds will be required to consolidate controlling stakes in different MNE Groups that, on an MNE Group basis do not exceed the consolidated revenue threshold of (€ 750m), but considering all controlling stakes in the different MNE Groups would. The application of the deeming provision in respect of UPEs that do not prepare consolidated financials (i.e., looking to the financial statements that would have been prepared if the UPE were required to prepare acceptable consolidated financials) may give an indication to this effect. The Commentary, on the other hand, makes it clear that the definition of Group is leading, and in this respect the applicable consolidation rules will need to be followed in assessing whether a consolidation on a line-by-line basis is required.

The Model Rules offer the option for a Filing Constituent Entity to not treat an Entity as an Excluded Entity. The election is a Five-Year Election, and when made, the GloBE Rules will apply to the Excluded Entity in the same manner as to any other Constituent Entity. If the UPE of an MNE Group is an Excluded Entity and such group includes Low-Taxed Constituent Entities for which Top-up Tax is calculated, the Top-up Tax will be charged under application of the UTPR at the level of Constituent Entities across all qualifying UTPR jurisdictions if all such Low-Taxed Constituent Entities are owned directly by the UPE. If the MNE Group makes the election to not treat the Investment Fund as an Excluded Entity, the Investment Fund can instead apply the IIR to its subsidiaries instead of subjecting all its Constituent Entities to the UTPR.

Administration

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Filing obligations

A GloBE Information Return needs to be filed by either the Constituent Entity in a jurisdiction or a Designated Local Entity acting on its behalf.

There is an alternative whereby the Ultimate Parent Entity or a Designated Filing Entity can lodge a return if they are located in a jurisdiction that has a Qualifying Competent Authority Agreement in place for that Reporting Fiscal Year.

The GloBE Information Return needs to be lodged within 15 months of the GloBE Reporting Year (extended to 18 months in the first fiscal year that the MNE Group is within scope).

The information contained in the return will be in a standard form which is to be developed but would include:

- Identification of the Constituent Entities and their location
- The overall corporate structure of the MNE Group
- Information necessary to compute the Effective Tax Rate for each jurisdiction, the top-up tax for each Constituent Entity and members of a JV Group
- The allocation of top-up tax to the IIR and the UTPR
- Record of any elections made
- Other information agreed as part of the GloBE Implementation Framework

There is an ability for local administrations to modify the information, filing and notification requirements. Local sanctions, penalties and confidentiality provisions will apply.

Notably, the ongoing consultation requests input on how the design of the information collection, filing obligations and record keeping requirements could be designed to maximize efficiency, accuracy and verifiability of information reporting while balancing compliance costs.

Safe Harbors

The Model Rules and Commentary include essentially a placeholder for the future development of “Safe Harbors”. The intent of the to-be-developed Safe Harbors is to limit unnecessary compliance and administrative burden for MNE Groups and tax administrations by not requiring effective tax rate and top-up tax calculations in jurisdictions that are likely to be taxed at or above the 15% minimum rate.

Any such to-be-developed Safe Harbor is elective, applies on a jurisdictional basis, and, assuming the MNE is eligible, has the effect of reducing the top-up tax for the relevant jurisdiction to zero in the eligible year. No detail is provided in the Model Rule or the Commentary on how the Safe Harbor will be calculated.

There has been discussion in prior guidance, including the Pillar 2 Blueprint, about potentially leveraging country-by-country reporting information for this purpose. Notably, even if an MNE is eligible for the to-be-developed Safe Harbor in a jurisdiction and makes the election, it would still be required to supply additional information to certain tax authorities if requested to do so within 36 months of the filing of the GloBE Information Return. The MNE Group would then have six months to demonstrate that the facts and circumstances identified by the relevant tax administration did not affect “materially” the eligibility of the MNE Group for the Safe Harbor in the relevant jurisdiction. There is no guidance in the Model Rules or Commentary about what “material” means for this purpose.

It is envisioned that the Safe Harbors will be finalized as part of the development of the GloBE Implementation Framework, including the consequences where the Safe Harbor is applied but is then found not applicable in conjunction with a subsequent challenge by a tax administration.

The ongoing consultation asks businesses for suggestions on measures to reduce compliance costs through simplifications, including the use of Safe Harbors.

Administrative guidance

Like the Safe Harbors, the Model Rules and Commentary include essentially a placeholder for the future development of “Administrative Guidance”. The intent of this guidance is to allow tax administrations, working together through the Inclusive Framework, to develop coordinated solutions to emerging technical issues as they arise.

If Administrative Guidance is in fact agreed, then tax administration would generally be required to interpret and apply the Model Rules in accordance with that agreed guidance.

And finally, consistent with the Safe Harbors, the ongoing public consultation asks businesses to comment if they see a need for Administrative Guidance and, if so, to specify the issues that require attention and the type of guidance needed.

Implementation process and timeline

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While the OECD has released the Commentary on the model rules, it has still to address co-existence with the US Global Intangible Low-Taxed Income or GILTI rules. On 14 March the OECD also launched a consultation on issues which should be addressed in the Implementation Framework which will focus on administrative, compliance and co-ordination issues relating to Pillar 2.

According to the OECD website, written comments should be submitted no later than 11 April 2022. They should not deal with policy choices in the Model Rules or Commentary but focus on putting in place mechanisms that will ensure tax administrations and MNEs can implement and apply the GloBE Rules in a consistent and coordinated manner while minimizing compliance costs.

Suggested questions to address include:

— Do you see a need for further administrative guidance as part of the Implementation Framework? If so, please specify the issues that require attention and include any suggestions for the type of administrative guidance needed.

— Do you have any comments relating to filing, information collection including reporting systems and record keeping? In particular, do you have any views on how the design of the information collection, filing obligations and record keeping requirements under GloBE could be designed to maximize efficiency, accuracy and verifiability of information reporting while taking into account compliance costs?

— Do you have any suggestions on measures to reduce compliance costs for MNEs including through simplifications and the use of safe harbors?

— Do you have views on mechanisms to maximize rule co-ordination, increase tax certainty and avoid the risk of double taxation?

The Inclusive Framework is also developing the model provision for a Subject to Tax Rule, together with a multilateral instrument for its implementation. A public consultation event on the Implementation Framework will be held at the end of April and on the Subject to Tax Rule in later in the year.

Agreement	Adoption into Law	Implementation
1 July 2021 – Agreement by 130 countries in the IF to a new international tax framework **October 2021 –** Detailed implementation plan for both pillars **20 December 2021 –** Agreed GloBE rules released for Pillar 2 **14 March 2022** – Commentary on GLOBE rules and Examples released **14 March 2022** – Consultation on matters to be covered by the Implementation Framework released	**April 2022** – Public Consultation on Implementation Framework **First half 2022** – Public Consultation on the STTR **Mid 2022** – A model treaty provision to give effect to the STTR together with Commentary will be developed as will a multilateral instrument to facilitate adoption of the STTR **End of 2022** – Finalization of the Implementation Framework	**2023** – According to the Executive Summary, the effective date for implementation of Pillar 2 is envisaged by 2023 with deferral of implementation of the UTPR rules for 12 months

Ten points on what tax leaders can do

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The GloBE rules can have significant impact on the ETR of MNE Groups, and it is expected to result in many different implementation challenges, as well as an increase of the administrative burden for MNE Groups that are in scope of the rules. The recently released Commentary confirms how complex the rules will be for many MNE Groups.

1. **Undertake a high-level evaluation of how the rules could potentially impact the MNE**

   This may involve the use of KPMG Assessment Tools and review of the MNE's Group Structure. While the Safe Harbor rules have yet to be developed, a delineation can be drawn between entities that will clearly exceed the minimum ETR threshold and those that may not. It will also involve an assessment of whether a structure is likely to involve Excluded Entities or how certain tax concessions might operate. It should be remembered that the position of various entities can change significantly from year to year. It should also be noted that full jurisdictional blending is not allowed in some cases.

2. **Understand the potential systems issues in collating data**

   Some information will be available through regular accounting information and some will need additional information to be gathered (for example, the extended definition of payroll, which includes certain types of independent contractors for the purpose of determining the Substance-based Exclusion Income).

3. **Ensure that there is strong liaison between tax teams and accounting teams on information**

   Because much of the information required is based on accounting data and delineations, particularly in relation to Deferred Tax, there is a need to ensure that data is available at the right level of granularity and integrity or robustness. In addition, the treatment and/or allocation of certain items of income or costs (including taxes) under the GloBE rules may differ from the accounting treatment in the financial accounts. The GloBE rules will also have accounting implications themselves.

4. **Consider a more detailed assessment model**

   After an initial evaluation provided above in 1-3, a more detailed assessment is likely to be appropriate to determine potential additional GloBE tax liabilities and the potential exercise of elections available. KPMG has a tool which can accommodate this more detailed assessment. This can be used to refine considerations of any elections.

   Also, any transaction between Constituent Entities located in different jurisdictions that is not recorded in the financial accounts consistent with the arm's length principle must be adjusted to be consistent with that principle.

5. **Inform Board and Management Committees of the potential financial and administrative impact of the new GloBE rules**

   Ensure that your budget has included additional funds for compliance costs, and that those within the organization that need to know are aware of the potential information gathering exercises to help streamline this process.

6. **Establish Tax Control Framework for GloBE**

   The GloBE rules may result in an increase of the overall effective tax rate of an MNE group and therefore can have a significant cashflow and financial statements impact. Non-compliance can result in a higher level of scrutiny from the tax authorities, higher (tax) costs as well as brand and potential reputational damage. The MNE board's tax governance needs to include a robust tax control framework that ensures compliance with these new rules.

7. **Whether a central, regional or hybrid approach is going to be adopted for dealing with GloBE**

   This will depend on the organization, but it is likely that some decentralization will be required based on the need for local information.

8. **Monitor how individual countries are reacting to GloBE and consistency of application**

   This includes amendments to introduce Domestic Top-up Taxes or Alternative Minimum Taxes, IIR and UTPR rules. Some countries may change tax-based incentives to grants and other forms of subsidy to better accommodate the rules.

   While the rules seek to involve a consistent framework, there may be differences in how they are applied to domestic entities. The potential co-existence of GILTI rules is likely to present differences in application. The EU may well introduce additional elements that extend or 'clarify' the GloBE rules in comparison to other jurisdictions.

9. **Consider future tax disclosures and interaction with the GloBE rules**

   There are an increasing number of disclosure regimes, both private and public, and early consideration of how they intersect is important. These include CBCR, GRI 207 and EU Public CBCR in addition to the GloBE rules.

10. **Consider any secondary impacts for customers and investee communications**

    There may be many secondary effects for MNEs, including customer credit profiles, cash-based evaluations of investments and dealing with minority interests. Consideration of these impacts needs to be part of an implementation plan.

More information

The following KPMG resources are available to help you continue to keep pace with developments.

Webcast: The next chapter for BEPS Pillar 2 and possible implications for MNEs	KPMG Tax Policy Perspectives	KPMG TaxNewsFlash Subscription	KPMG Future of Tax

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