Pillar Two establishes a global minimum taxation regime through a series of interlocking rules.

Leveling the playing field
On October 8, 2021, the Inclusive Framework (IF) released an updated statement setting forth the key components for an agreement on a two-pillar solution to address the tax challenges arising from the digitalization of the economy.

Pillar Two has three new rules granting jurisdictions additional taxing rights, including:

- Two interlocking domestic rules (the Global Anti-Base Erosion (GloBE) rules):
  - (i) an Income Inclusion Rule (IIR), which imposes top-up tax on a parent entity in respect of the income of subsidiaries and permanent establishments that is taxed at less than a 15% minimum effective tax rate, and
  - (ii) a supporting Undertaxed Payment Rule (UTPR), which denies deductions or requires an equivalent adjustment to the extent the low-tax income of a constituent entity is not subject to tax under an IIR
- A Subject to Tax Rule (STTR), which overrides treaty benefits for certain related-party payments that are not subject to a 9% minimum rate of tax in the recipient jurisdiction. The STTR will be creditable as a covered tax under the IIR and UTPR, i.e., the STTR applies first.

Exclusions and simplifications
- The rules will apply to multinational enterprise (MNE) groups with a total consolidated group revenue above €750 million. However, countries may apply a lower revenue threshold for the IIR in respect of groups headquartered in their country.
- There will be a carve-out from the IIR and UTPR for an amount equal to 5% of the carrying value of tangible assets and payroll costs, subject to a ten-year transition period. In the first year, those amounts will be 8% of the carrying value of tangible assets and 10% of payroll, with both percentages declining to 5% over the ten-year period.
- International shipping income and de minimis profits are also excluded. So too are MNEs in the initial phase of their international activity, defined as MNEs with less than €50 million of tangible assets abroad and operations in no more than five other jurisdictions, for a period of five years after the MNE comes into the scope of the GloBE rules.

What businesses need to know
- The IF aims to bring the Pillar Two rules into law in 2022, to be effective in 2023, although the effective date of the UTPR will be delayed for one year.
- Model GloBE rules, along with a model STTR treaty provision, will be developed by the end of November 2021. A multilateral instrument will be developed by mid-2022 to facilitate implementation of the STTR in relevant bilateral treaties, and by the end of 2022, an implementation framework will be developed that facilitates the coordinated implementation of the GloBE rules.
- A number of uncertainties remain, but Pillar Two is likely to be a radical shift in the tax landscape.
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