Pillar Two: Global minimum taxation

Pillar Two applies where, even after the effect of Pillar One (if any), multinationals are regarded as undertaxed by reference to an agreed minimum level of taxation.

Leveling the playing field

- **Pillar Two** has four new rules granting jurisdictions additional taxing rights where other jurisdictions have not exercised their primary taxing rights or income is subject to low rates of tax.
- An Income Inclusion Rule (IIR) that would subject foreign income and controlled entities to an agreed minimum tax in the parent jurisdiction, complemented by a Switch-over Rule addressing low-taxed permanent establishments that are exempted by treaty.
- An Undertaxed Payments Rule (UTPR) that acts as a backstop to the IIR denying deductions or introducing source-based taxation under certain conditions.
- A Subject to Tax Rule that turns off treaty benefits on intragroup payments that are not subject to a minimum nominal rate of tax in the payee jurisdiction.

Exclusions and simplifications

- The intention for most practical purposes is that these rules should only apply to multinational enterprise (MNE) groups with a total consolidated group revenue above €750 million or equivalent.
- The proposals include a “carve-out” from the scope of the IIR and UTPR equal to a fixed return for payroll and tangible asset costs, which is intended to focus the rules on “excess income,” such as intangible-related income, which is regarded as most susceptible to diversion.
- A further in-principle exclusion may be to treat the U.S. global intangible low-taxed income regime as a qualifying IIR (still to be agreed).
- To limit the compliance burden on low-risk businesses, simplification options are proposed that may be based on some or all of country-by-country reporting data, de minimis profits, or low local tax risk.

What businesses need to know

- Work on Pillar Two has greatly advanced towards consensus; the main areas that still need to be resolved are around simplification measures.
- Pillar Two could have a significant impact on the effective tax rates of MNE groups by itself or in combination with Pillar One.
- Implementation of the rules will likely involve a combination of changes to domestic tax laws and bilateral tax treaties (expected to be via a multilateral convention).
- OECD invited public comments on the proposals in the form of submissions that were due in December 2020, followed by public consultation meetings, which were held in January 2021. The OECD has published its global impact analysis; potentially affected businesses should consider what these changes could mean for their effective tax rate.

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