



Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy

On October 8th, the Organisation for Economic Cooperation and Development (OECD) announced that 136 jurisdictions (out of the 140 members of the OECD/G20 Inclusive Framework on BEPS) have joined the Statement on the Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy.

Two-Pillar Solution

The OECD notes that not all members of the Inclusive Framework have joined yet. However, the countries and jurisdictions that have joined the Two-Pillar Solution represent more than 90% of the global GDP and now also include the EU Member States Estonia, Hungary and Ireland who had previously not joined the agreement. The Two-Pillar Solution will now be delivered to the G20 Finance Ministers meeting in Washington D.C. on 13 October and then to the G20 Leaders' Summit in Rome at the end of the month.

The Two-Pillar Solution is comprised of Pillar One and Pillar Two. Pillar One aims to ensure that profits and taxing rights are distributed more fairly among tax jurisdictions by offering market jurisdictions new taxing rights over MNEs, whether or not there is a physical presence.

Pillar Two puts a floor on tax competition on corporate income tax through the introduction of a global minimum tax at a rate of 15%.

Pillar One at a high level

- » In-scope: MNEs with a global turnover of more than USD 20 billion, and a profitability of more than 10% (profit before tax/revenue), both determined by reference to financial accounting income with a small number of adjustments and a carry forward of losses. The turnover threshold may be reduced to USD 10 billion, eight years after the Pillar One agreement enters into force. Finally, extractives and regulated financial services are excluded.
- » Quantum: 25% of residual profit defined as profit in excess of 10% of revenue ("Amount A") will be allocated to market jurisdictions with nexus.
- » Nexus: Amount A is allocated to market jurisdictions where the in-scope MNE derives at least 1 million euros in revenue from that jurisdiction. For smaller jurisdictions with GDP lower than EUR 40 billion, the nexus will be set at EUR 250 000.
- » Sourcing: Revenue will be sourced to the end market jurisdictions where goods or services are used or consumed. Specific rules on sourcing are under development.
- » Safe harbour: where residual profits of an MNE are already subject to tax in a market jurisdiction, a marketing and distribution profits safe harbour will cap the residual profits allocated to that jurisdiction.



- » Prevention of double taxation and dispute resolution: measures to prevent double taxation between residence jurisdictions and market jurisdictions as well as a dispute prevention and binding resolution mechanisms will be included. However, for certain developing economies an elective binding resolution mechanism will be proposed.
 - » Administration: The entity (or entities) that will bear the tax liability will be those that earn residual profit. The additional tax compliance should be processed through a single entity.
 - » Abolishment of unilateral digital services taxes: the Multilateral Convention on the basis of which Pillar One will be implemented will require all parties to remove all digital services taxes and other relevant similar measures and commitment not to introduce such measures in the future (starting from 8 October 2021). For some members transitional arrangements are being discussed.
- Pillar Two at a high level**
- » Overall design: three interlocking domestic rules (together the Global anti-Base Erosion Rules (GloBE) rules):
 - i. an Income Inclusion Rule (IIR), which imposes top-up tax on a parent entity, flanked by;
 - ii. A Switch Over Rule (SOR) to facilitate the effective application of the IIR to low-taxed permanent establishments that would otherwise be exempt under a treaty; and
 - iii. an Undertaxed Payment Rule (UTPR), which denies deductions or requires an equivalent adjustment to the extent the low tax income of is not subject to tax under an IIR; and
 - » a treaty-based rule, the so-called Subject to Tax Rule (STTR), which allows source jurisdictions to impose limited withholding tax on certain related party payments subject to tax below a minimum rate.
 - » Status: Inclusive Framework members are not required to adopt the GloBE rules, but, if they choose to do so, they commit to implementing them consistent with Pillar Two.
 - » Scope: MNEs with a global turnover of EUR 750 million or more, but countries are free to lower the threshold if they so desire.
 - » Minimum rate: the minimum tax rate for GloBE rules will be 15%, determined on a per-jurisdiction basis. The minimum rate for the STTR will be 9%, meaning that the taxing right under the STTR comprises of the difference between the minimum rate and the actual rate at the level of the recipient.
 - » Carve-outs/exclusions:
 - i. Excluded entities: Government entities, international organizations, non-profit organizations, pension funds or investment funds that are Ultimate Parent Entities and their related investment holdings.



- ii. Substance based carve outs: 8% of the carrying value of tangible assets and 10% of payroll of a local entity is excluded from the GLoBE tax base, which is reduced over a period of 10 years to an exclusion percentage of 5.
- iii. De minimis exclusion: the GLoBE rules will not apply to jurisdictions where an MNE has revenues of less than EUR 10 million and profits of less than EUR 1 million.
- iv. Other exclusions: excluded from GLoBE rules is international shipping income.
- v. Other simplifications: the implementation framework will include safe harbours and/or other mechanisms to avoid disproportionate compliance and administrative costs.

Next steps

The OECD has also come with a Detailed Implementation Plan (which includes target deadlines) to ensure swift implementation, on which the 136 jurisdictions have agreed. The jurisdictions are aiming to sign a Multilateral Convention and Explanatory Statement for Pillar One early 2022. For Pillar Two it is aimed to further define scope and rules by the end of 2021. The effective implementation of both Pillar One and Pillar Two is targeted for 2023.

The European Commission has indicated in its roadmap of 18 May, titled "[Business taxation for the 21st century](#)", that it intends to propose EU Directives for the implementation of the Pillar One and Pillar Two proposals, to ensure harmonized implementation in the EU. Now that Estonia, Hungary and Ireland have joined the agreement, reaching unanimous consensus within the EU seems more realistic than before.

The only EU Member State who has not joined the agreement yet is Cyprus, but given Cyprus' broad support and implementation of the OECD efforts thus far, a veto from Cyprus in EU context seems unlikely.

Their non joining of the OECD efforts may be the result of political tensions with other Inclusive Framework members rather than their unwillingness to join.

Whilst the 2023 target date is highly ambitious, it is not outside the realm of possibilities, especially now that broader consensus within the EU seems to have been reached.

As such, it seems likely that both Pillar One and Pillar Two will gain traction globally, and may enter into effect in a number of jurisdictions already in 2023. If enough countries adopt the Pillar Two rules, then much of global corporate profits may face a 15% effective tax rate.

In this context, it is also noteworthy that the Biden administration has released a welcoming statement of the Two-Pillar agreement on October 8th, although it has been noted that it may be challenging to get Congress aligned on implementing these policies.



What you should do

MNEs are encouraged to closely monitor the Two-Pillar developments and – in due course – how these rules will be implemented in the individual countries in which they operate. MNEs can already start with the identification of the effective tax rate under the GLoBE rules on a per country basis by reference to the relevant subsidiaries' accounting income, to determine which countries may potentially be below the required 15%.

In addition, MNEs can already identify related party payments that are subject to tax at the level of the recipient at a rate lower than 9%. Especially once more detail is known on the revenue sourcing rules under Pillar Two, it may also be recommended to determine which countries may be entitled to receive part of Amount A. With this information, relevant MNEs can model the expected tax impact under the anticipated rules and take well considered decisions to optimize their positions and mitigate the risk of double taxation and other adverse consequences going forward.

If you have any questions or should you need assistance, please let us know.

The press release of the OECD can be read [here](#).

The highlights brochure regarding the Two-Pillar Solution published by the OECD can be read [here](#).

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