TAXATION LAW RESEARCH PROGRAMME (TLRP)

THE PILLAR TWO MODEL RULES: ENSURING MINIMUM TAXATION FOR MULTINATIONAL ENTERPRISES

25 September 2024 (Wednesday), 5:00 – 6:00 PM Hong Kong Time via ZOOM

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Overview

- ✓ The **Pillar Two Model Rules** (*i.e.* “Global Anti-Base Erosion” or **“GloBE” Rules**), have been released on 20 December 2021 and are part of the Two-Pillar Solution to address the tax challenges of the digitalization of the economy. This project was agreed by 137 Member jurisdictions of the OECD/G20 Inclusive Framework on BEPS and endorsed by the G20 Finance Ministers and Leaders in October 2021.

- ✓ These Rules are designed to ensure **large multinational enterprises (MNEs)** pay a **minimum level of tax** on the income arising in each jurisdiction where they operate. They are drafted as **model rules** that provide a **template** that **jurisdictions** can **convert into domestic law**, which should facilitate them in implementing Pillar Two within the agreed timeframe and in a **coordinated manner**.

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Structure of Pillar II Model Rules

The Pillar Two Model Rules consist of 10 chapters:

- ✓ **Chapter 1 -** scope;
- ✓ **Chapters 2-5 -** key operative rules;
- ✓ **Chapter 6** - mergers and acquisitions;
- ✓ **Chapter 7 -** special rules that apply to certain tax neutrality and existing distribution tax regimes;
- ✓ **Chapter 8** - tax administration;
- ✓ **Chapter 9** - rules on transition;
- ✓ **Chapter 10** - definitions.

The **Pillar Two Model Rules have been designed to make sure they admit different tax systems**, including different tax consolidation rules, income allocation, entity classification rules etc., as well rules for specific business structures such as joint ventures and minority interests. As such, many of the specific provisions of the Pillar Two Model Rules will not apply to all jurisdictions or each individual in scope MNE.

Key Steps to determine liability under the Pillar Two Model Rules

Step 1 – Constituent Entities within scope

- Identify Groups within Scope and the location of each Constituent Entity within the Group

Step 2 – GloBE Income

- Determine Income of each Constituent Entity

Step 3 – Covered taxes

- Determine taxes attributable to Income of a Constituent Entity

Step 4 – Effective Tax Rate and Top-up Tax

- Calculate the Effective Tax Rate of all Constituent Entities located in the same jurisdiction and determine resulting Top-up Tax

Step 5 – IIR and UTPR

- Impose Top-up Tax under IIR or UTPR in accordance with agreed rule order

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The GloBE Rules

Aim of the Model Rules

The Model Rules lay down rules for ensuring **minimum level of effective corporate taxation** (ETR ≥ 15%) of large MNEs Groups through **three different set of rules**

Income Inclusion Rule (IIR)

- Imposing a **top-up tax on a parent entity in respect of its allocable share in the low taxed income** of a constituent entity of an MNE group or a large-scale domestic group.

Undertaxed Profit Rule (UTPR)

- Backstop to the IIR and applies in situations **where (i) there is no qualifying IIR; or (ii) the UPE and the other constituent entities in the same jurisdiction are low-taxed**.

Domestic Top-up Tax (DMTT)

- Member State can **elect to apply the top-up tax domestically** to constituent entities located in their territory.

Scope of the GloBE Rules

Objective Scope - Art. 1(1)

1

Objective Scope

The GloBE Rules apply to Constituent Entities that are members of an **MNE Group** that has annual **revenue of EUR 750 million** or more in the **Consolidated Financial Statements** of the **Ultimate Parent Entity (UPE)** in **at least two of the four Fiscal Years immediately preceding the tested Fiscal Year**. Further rules are set out in Article 6.1 which modify the application of the consolidated revenue threshold in certain cases.

2

Revenue threshold & Fiscal Year lenght

If one or more of the **Fiscal Years** of the MNE Group taken into account is of a **period other than 12 months**, for each of those Fiscal Years the EUR 750 million threshold is **adjusted proportionally** to correspond with the length of the relevant Fiscal Year.

3

Excluded entities

Entities that are Excluded Entities are not subject to the GloBE Rule

Subjective Scope - Art. 1(2)

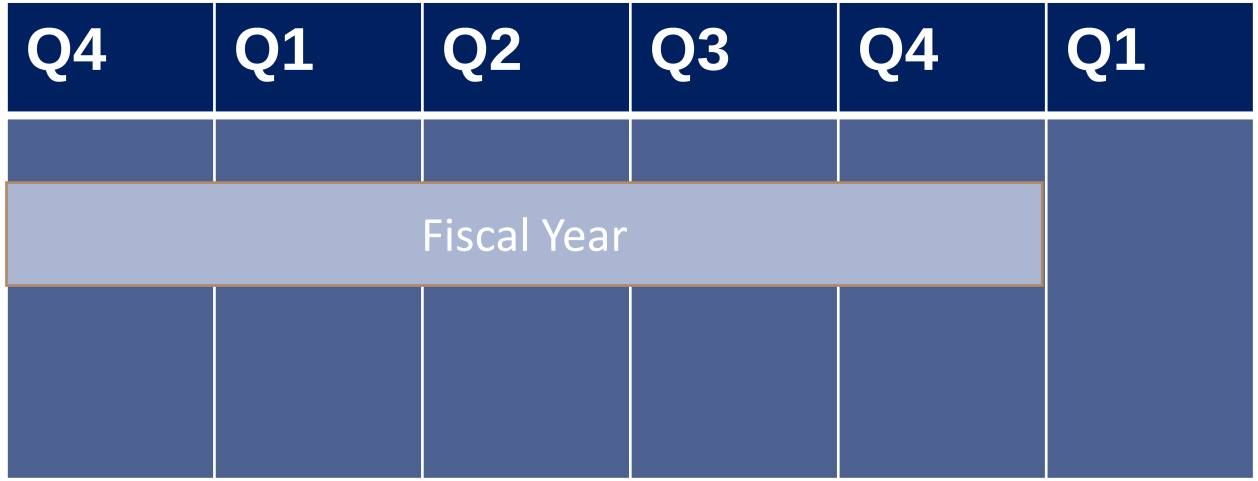
1

Group Definition

A **Group** includes entities that are related through **ownership or control** (see IFRS 10 or OIC 17) as defined by the accounting framework for the preparation of **Consolidated Financial Statements** by the Ultimate Parent Entity, including any entity that may have been excluded from the consolidated financial statements of the ultimate parent entity solely based on its small size, materiality grounds or on the grounds that it is held for sale.

Calculation of the Revenue Threshold

Revenue threshold and short Fiscal Year:



Background:

- ✓ Adjust revenue threshold proportionally in case fiscal year is longer or shorter than 12 months.

Example:

- ✓ Fiscal year comprised of 15 months.
- ✓ Adjustment revenue threshold: EUR 930 million/15 x 12 = EUR 744 million ➔ **N/A**

Excluded Entities – Art. 1(5)

Excluded Entities

(a)	(b)	(c)
✓ Governmental entity; ✓ International organisation; ✓ Non-profit organisation; ✓ Pension fund; ✓ Investment entity that is UPE; ✓ Real estate investment vehicle that is UPE	✓ Entity owned at a minimum of 95% and meets: a) Ownership test b) Activities test	✓ Entity owned at minimum of 85% and primarily composed of excluded dividends or excluded equity gains or losses in accordance with Articles 15(2)(b)

Consequences:

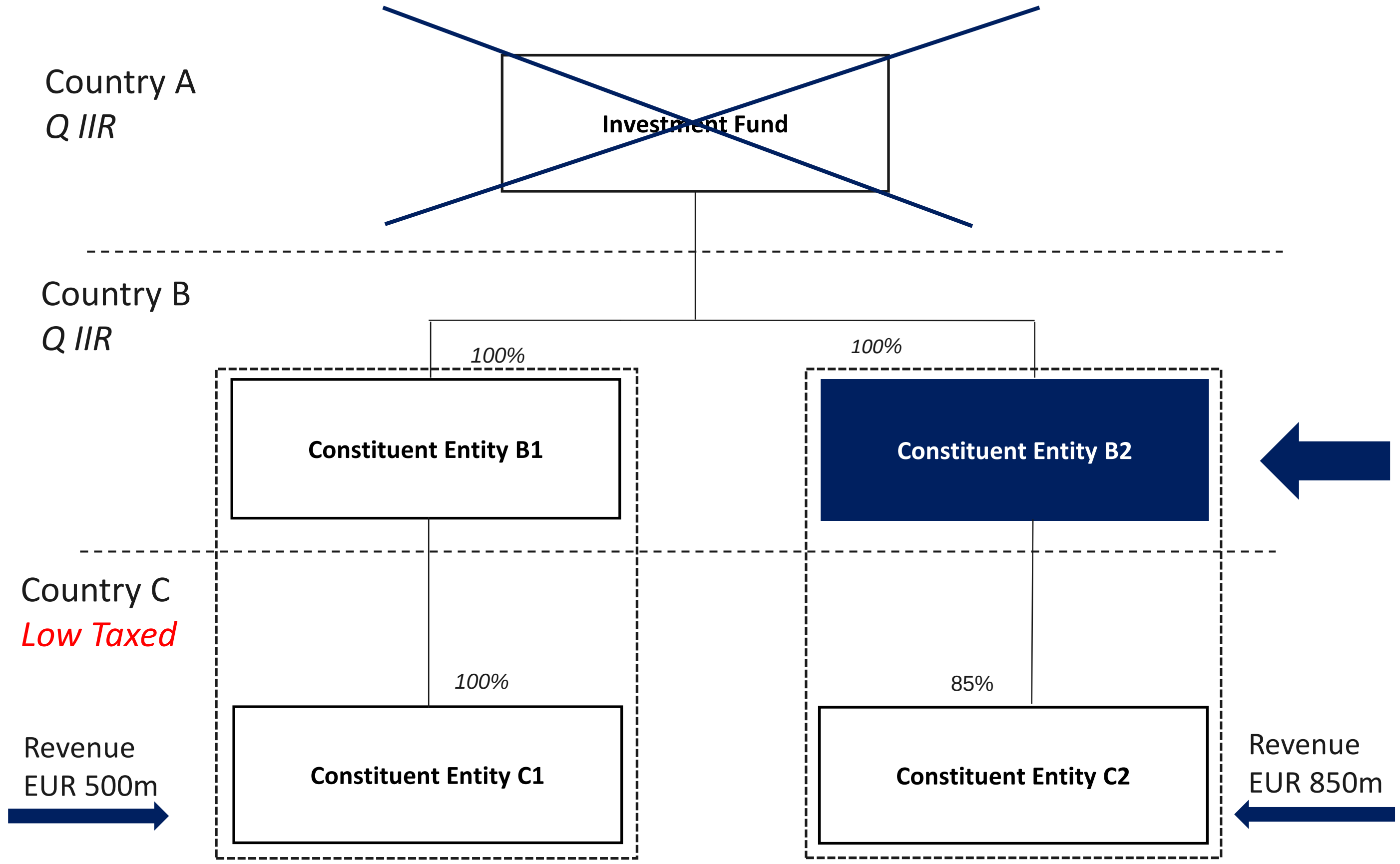
a) **IIR** and **UTPR** do <u>not</u> apply to excluded entities;

b) Removed from the relevant computations, except for the revenue threshold;

c) No administrative obligations

Exception: Unless filing CE has made election <u>not</u> to treat such entities as excluded

Excluded Entities v – Art. 1(5)



Application Directive:

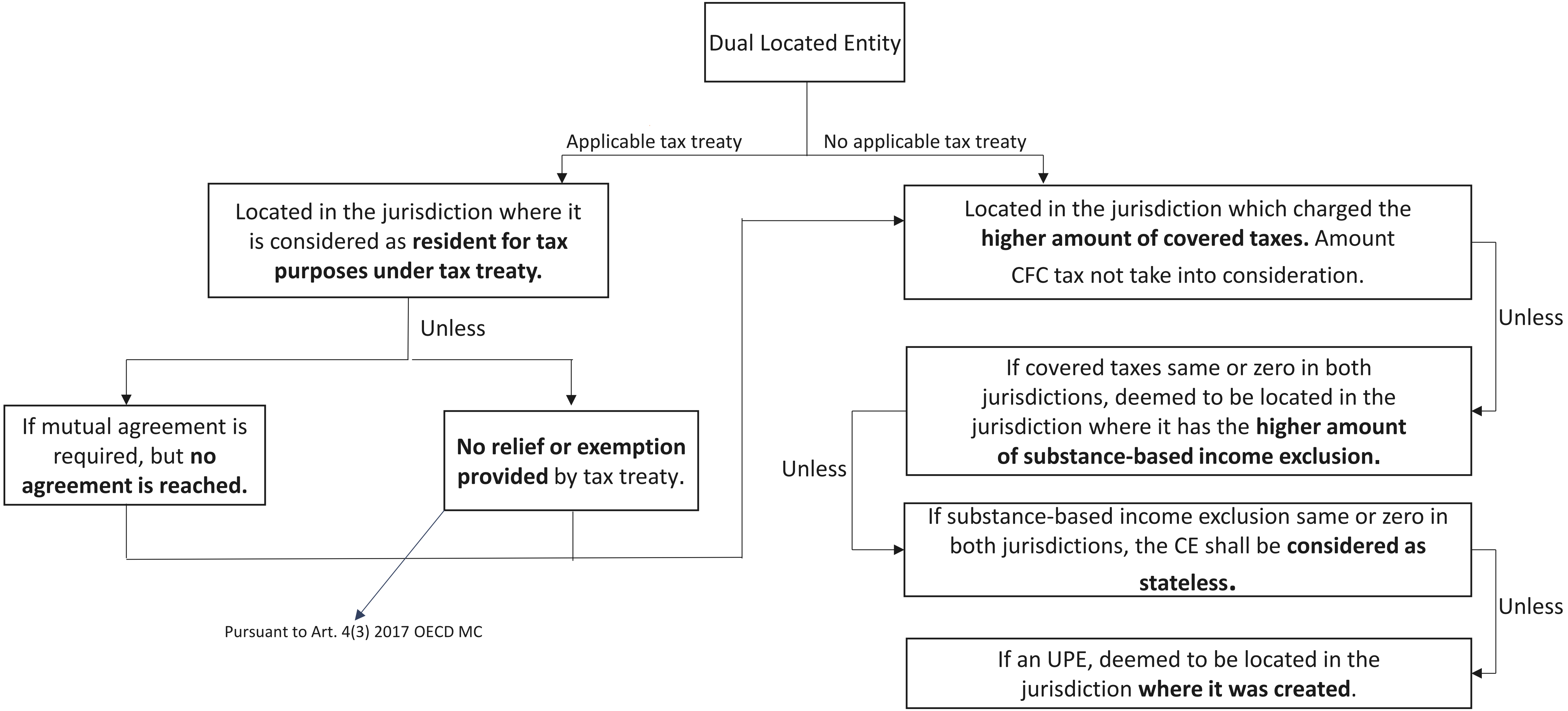
- ✓ **Investment Fund:** not a CE and not required to apply IIR
- ✓ **CE B1:** MNE Group does not meet consolidated revenue threshold of EUR 750m and CE B1 not required to apply IIR.
- ✓ **CE B2:** MNE Group meets the consolidated revenue threshold of EUR 750m and CE B2 is required to apply IIR.
- ✓ **NB:** If Investment Fund were required to consolidate B1 Group and B2 Group its financial accounts, the consolidated revenue threshold of EUR 750m would be met and CE B1 would be subject to IIR.

Location of the Constituent Entities – Art. 4(1), (2) and (3)

Location of a CE

Entity	Flow-through Entity	PE		
✓ Located in the jurisdiction where it is tax resident based on "place of management" and "place of creation" ✓ In other cases (e.g. no CIT) , it is in the jurisdiction where it is created.	✓ If it is the UPE or required to apply the IIR ➔ located in jurisdiction where it is created; ✓ In other cases ➔ treated as a stateless entity		**Definition PE**	**Location PE**
		a)	PE in accordance with an applicable Tax Treaty and taxed Article 7	Where it is treated and taxed In accordance with the Tax Treaty
		b)	PE in accordance with national corporate income tax system	Where it is subject to taxation based on its business presence
		c)	PE in accordance with OECD MTC	Where it is situated
		d)	Operations are conducted outside the jurisdiction and such jurisdiction exempts the income	Stateless PE

Location of the Constituent Entities – Art. 4(1), (2) and (3)



Flow-Through entity – Transparent Entity – Hybrid Entity – Reverse Hybrid Entity

O: owner's location jurisdiction

O/o: the owner's jurisdiction of location considers the entity to be fiscally transparent

O/e: the owner's jurisdiction of location treats the entity as fiscally opaque

E: entity location jurisdiction

E/o: the entity's jurisdiction of location considers the entity to be fiscally transparent

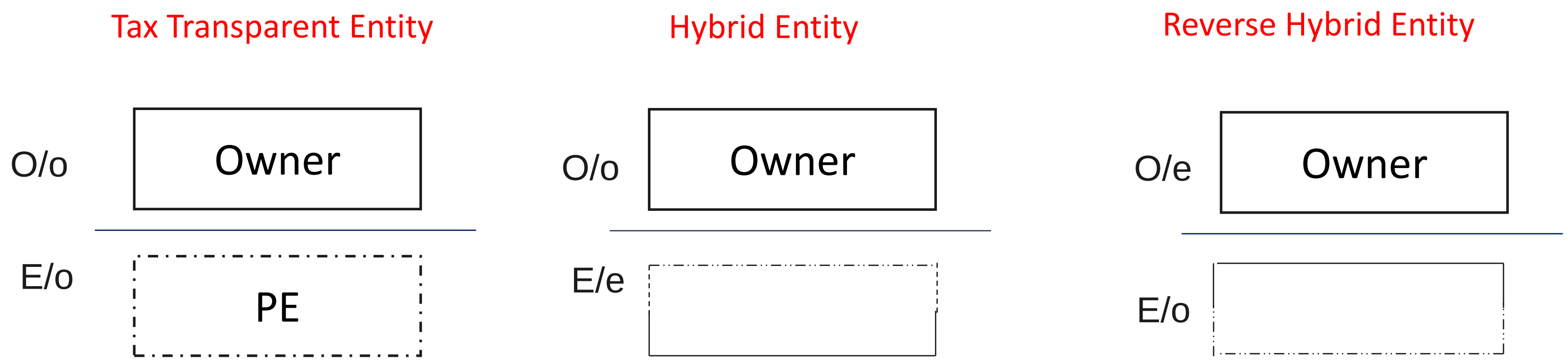
E/e: the entity's jurisdiction of location considers the entity to be fiscally opaque

Flow Through Entity: transparent for its jurisdiction of incorporation. Irrelevant to the jurisdiction of the entity ➔ E/o

Tax Transparent Entity: transparent for its jurisdiction of incorporation and transparent for the jurisdiction of the entity ➔ E/o + O/o

Hybrid Entity: opaque for its jurisdiction of incorporation and transparent for the jurisdiction of the entity ➔ E/e + O/o

Reverse Hybrid Entity: transparent for its jurisdiction of incorporation and opaque for the jurisdiction of the entity ➔ E/o + O/e



Main Definitions

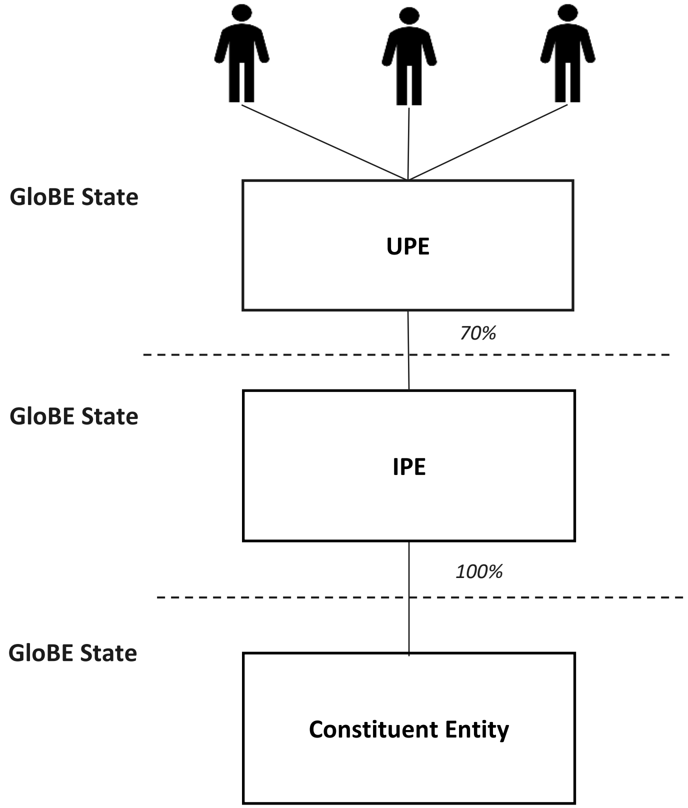
Ultimate Parent Entity (UPE)

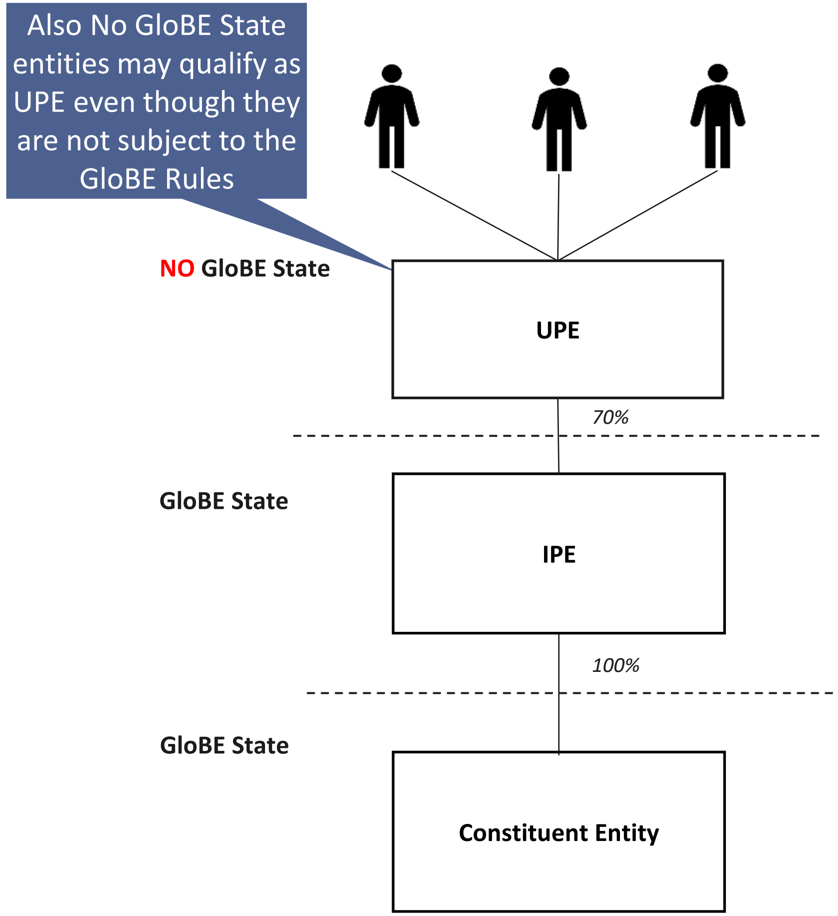
a) An entity that owns, directly or indirectly, a Controlling Interest in any other entity and that is not owned, directly or indirectly, by another entity with a Controlling Interest in it; or

b) A main entity

It identifies an individual or any entity not required to prepare consolidated financial statement

"**Controlling interest**" means an Ownership Interest in an entity whereby the interest holder is required, or would have been required, to consolidate the assets, liabilities, income, expenses and cash flows of the entity on a line-by-line basis, in accordance with an acceptable financial accounting standard

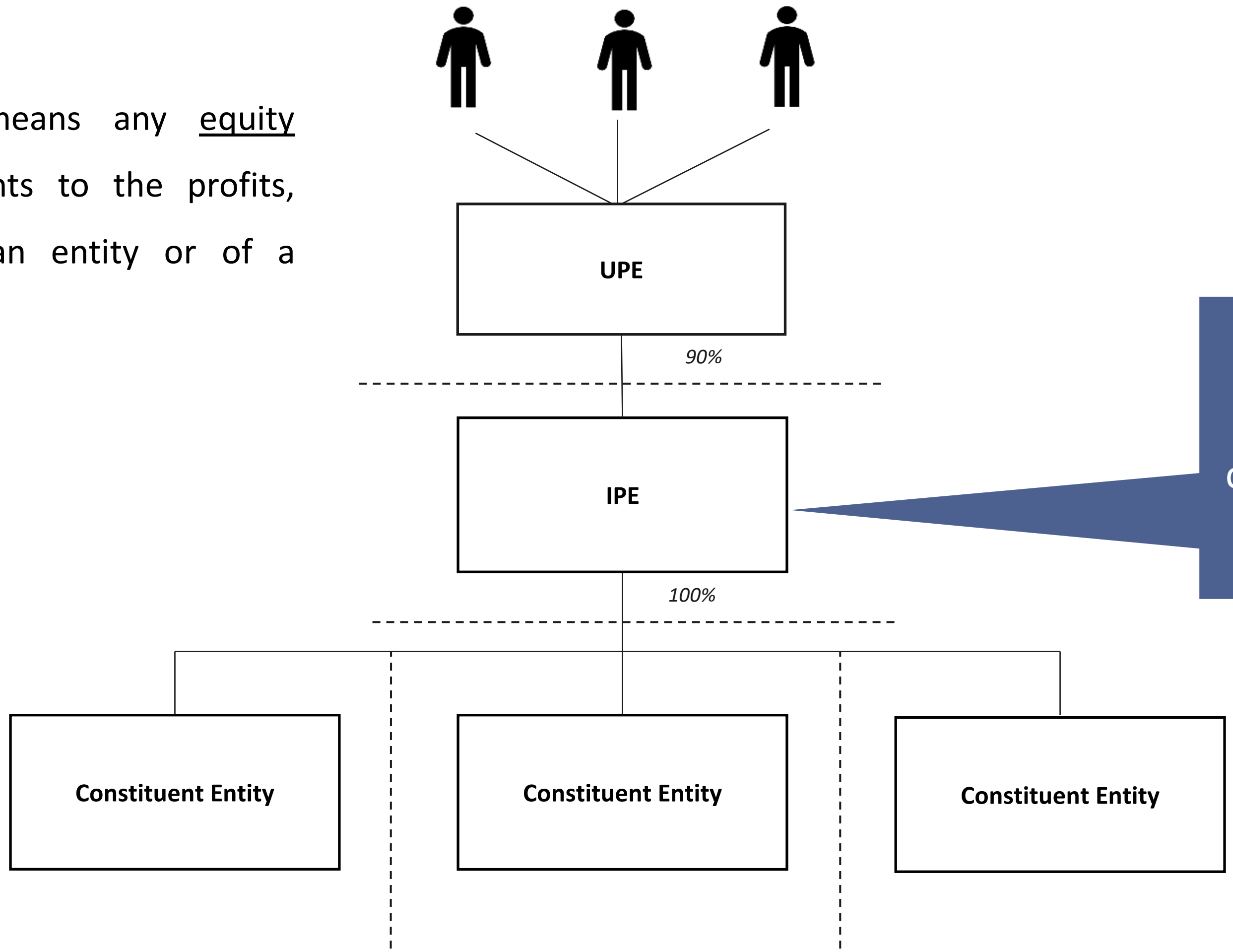




Intermediate Parent Entity (IPE)

A constituent entity that owns, directly or indirectly, an ownership interest in another constituent entity in the same MNE group and that does not qualify as an ultimate parent entity, **a** partially-owned parent entity, **a** permanent establishment or **an** investment entity

"**Ownership Interest**" means any equity interest that carries rights to the profits, capital or reserves of an entity or of a permanent establishment.

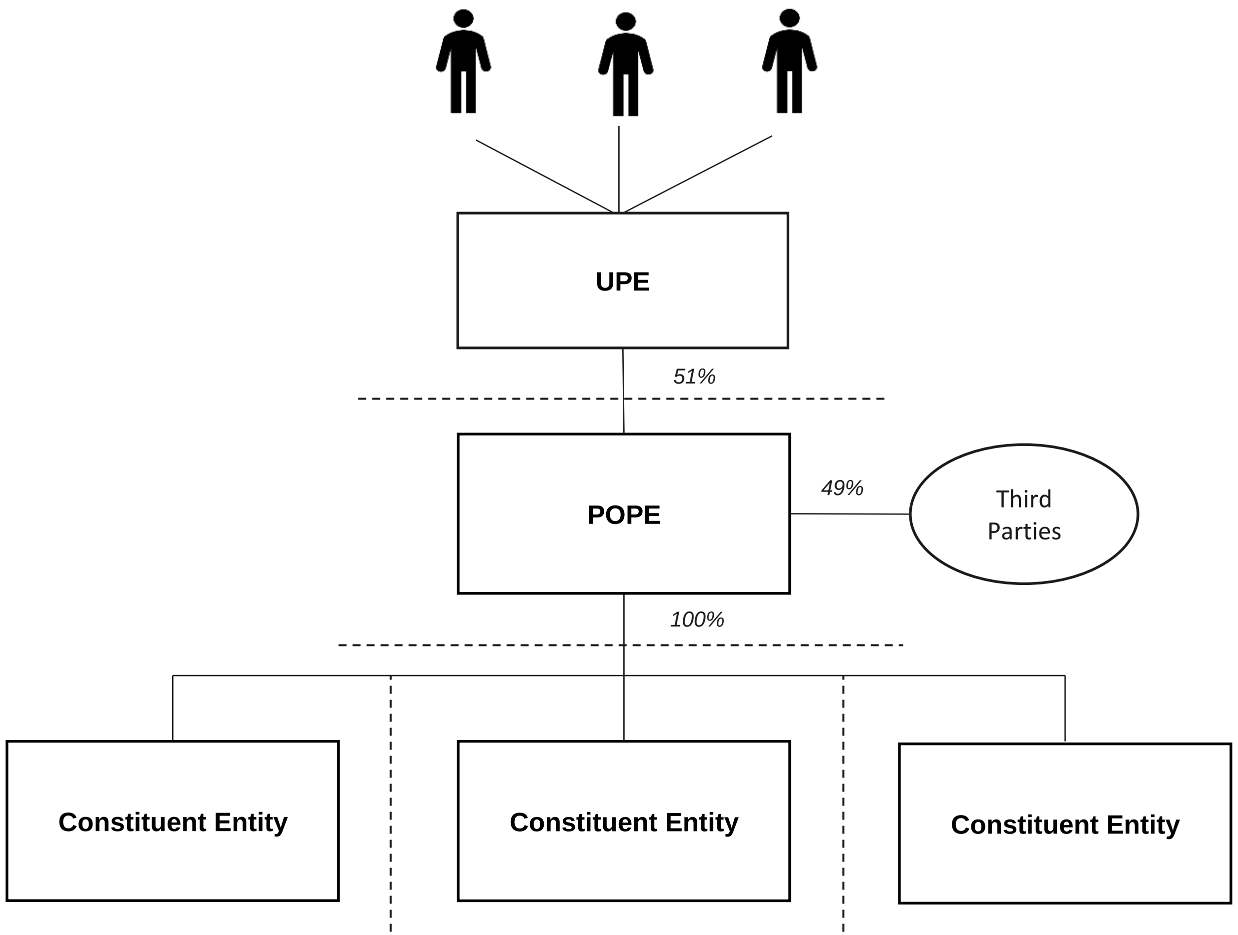


Even if such company controls several Constituent Entities, if it is in its turn controlled by another entity = it cannot qualify as UPE

Partially-Owned Parent Entity (POPE)

A constituent entity that (i) owns, directly or indirectly, an ownership interest in another constituent entity of the same MNE group and (ii) has more than 20 % of its ownership interest in its profits is held, directly or indirectly, by persons that are not constituent entities of the MNE group **and** that does not qualify as an *ultimate parent entity*, a *permanent establishment* or an *investment entity*

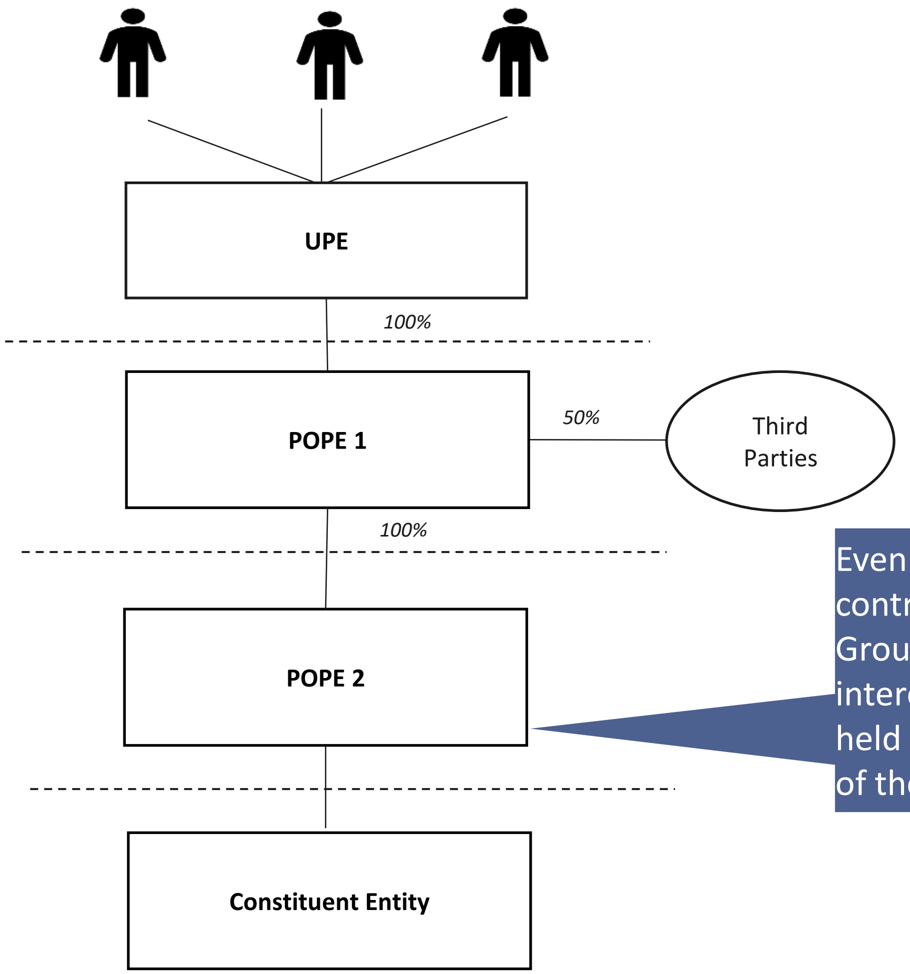
One POPE



Partially-Owned Parent Entity (POPE)

A constituent entity that owns, directly [POPE2] or indirectly [POPE1], an ownership interest in another constituent entity of the same MNE group, more than 20 % of its ownership interest in its profits is held, directly [POPE1] or indirectly [POPE2], by persons that are not constituent entities of the MNE group and that does not qualify as an ultimate parent entity, a permanent establishment or an investment entity

Two POPEs



Even if such company is entirely controlled by another entity of the Group, more than 20% of the interest in its profit is indirectly held by an entity which is not part of the Group

The GloBE Rules

The Effective Tax Rate (ETR)

- ✓ To know if top-up tax is due, it is necessary to compute the **Effective Tax Rate (ETR)** in each jurisdiction where the MNE operates. This requires *first* a calculation of the <u>income</u> (“*GloBE Income or Loss*”), and *second* a calculation of the <u>taxes on that income</u> (“*Adjusted Covered Taxes”*).
- ✓ The <u>**GloBE Income or Loss**</u> is calculated based on **financial accounts**, which provides a **base** that is **harmonized across all jurisdictions**. Certain **adjustments** are needed to better align the financial accounts with tax purposes and to reflect common permanent differences (such as to remove most dividends and equity gains so that the minimum tax does not apply to such income, or to remove expenses disallowed for tax purposes such as bribes and to correct prior year errors). <u>There is also an exclusion for international shipping income.</u>
- ✓ The <u>**Adjusted Covered Taxes**</u> are calculated, including **income taxes**, defined in a way to provide consistent and flexible recognition across a wide range of tax systems. It does **not include non-income-based taxes** such as indirect taxes, payroll and property taxes. Rules are also provided to allocate income taxes which are charged as a withholding tax or following the application of a **Controlled Foreign Company (CFC)** regime (which are allocated to the entity that earned the underlying income).
- ✓ Some rules are set out for <u>addressing temporary differences</u>, which arise when income or loss is recognized in a different year for financial accounting and tax.

The Effective Tax Rate (ETR)

The effective tax rate ("**ETR**") is one of the **key** elements of the Model Rules as **it serves two purposes**;

1

It **triggers the application of the IIR, UTPR or DMMT** (if the ETR MNE group's CEs in a jurisdiction falls below 15%).

2

It **measures the amount of top-up tax** due in each and every jurisdiction.

Effective tax rate: $\dfrac{\textit{\textbf{Adjusted Covered Taxes} of all the constituent entities located in a given jurisdiction}}{\textit{\textbf{GloBE Income or Loss} of all the constituent entities located in the same jurisdiction}}$

Calculation of the Top-Up Tax (1/3)

- ✓ Once the effective tax rate is calculated (i.e., the tax divided by the income and aggregated on a per jurisdiction basis) it is necessary to determine how much **top-up tax** is owed.
- ✓ The rate of tax owed is the **difference between the 15% minimum rate and the ETR in the jurisdiction**. That top-up tax percentage is then applied to the GloBE income in the jurisdiction, after deducting a *substance-based-income-exclusion* (or "**SBIE**"). The substance-based-income-exclusion reduces the exposure to the minimum tax and is calculated as a percentage mark-up on tangible assets and payroll costs.

Calculation of the Top-Up Tax (2/3)

Below are the formulas that are used to calculate the Top-Up Tax, see the example in the next slide.

Top-up Tax Rate:

15% - ETR

GloBE Income or Loss:

FANIL + Adjustmemts

Top-Up tax Amount:

Top-up Tax Rate * Excess Profit

FANIL:

Profit after tax as reported in the cd. *consolidation package*

Excess Profit:

GloBE Income – SBIE

SBIE:
Formulaic deduction computed based on the value of employments costs and tangible assets

Calculation of the Top-Up Tax (3/3)

EXAMPLE

ETR: 12.5%

Top-up Tax Rate: 15% - 12.5% = 2.5%

Globe Income and Loss of the CE (A-B-C-D-E-F) located in the jurisdiction

Globe Income of the jurisdiction: Euro (2.000 + 3.000 + 4.000 + 2.000 – 1.000) = **10.000**

SBIE: Euro 4.000

Excess Profit: Euro (10.000 – 4.000) = Euro 6.000

Top-up Tax Amount: 6.000 * 2.5% = **Euro 150**

If **QDMTT** exists, then 150 is paid by A-F collectively to the Jurisdiction Government

If **QDMTT** does not exist, then 150 must be levied through IIR

If **QDMTT** and **IRR** does not apply, then the amount of 150 must be levied through UTPR

Determination of the Group Entity Liable for the Top-up Tax

✓ A liability to top-up tax for a member of an in-scope MNE group arises under two types of provisions:

Income Inclusion Rule (or "**IIR**")

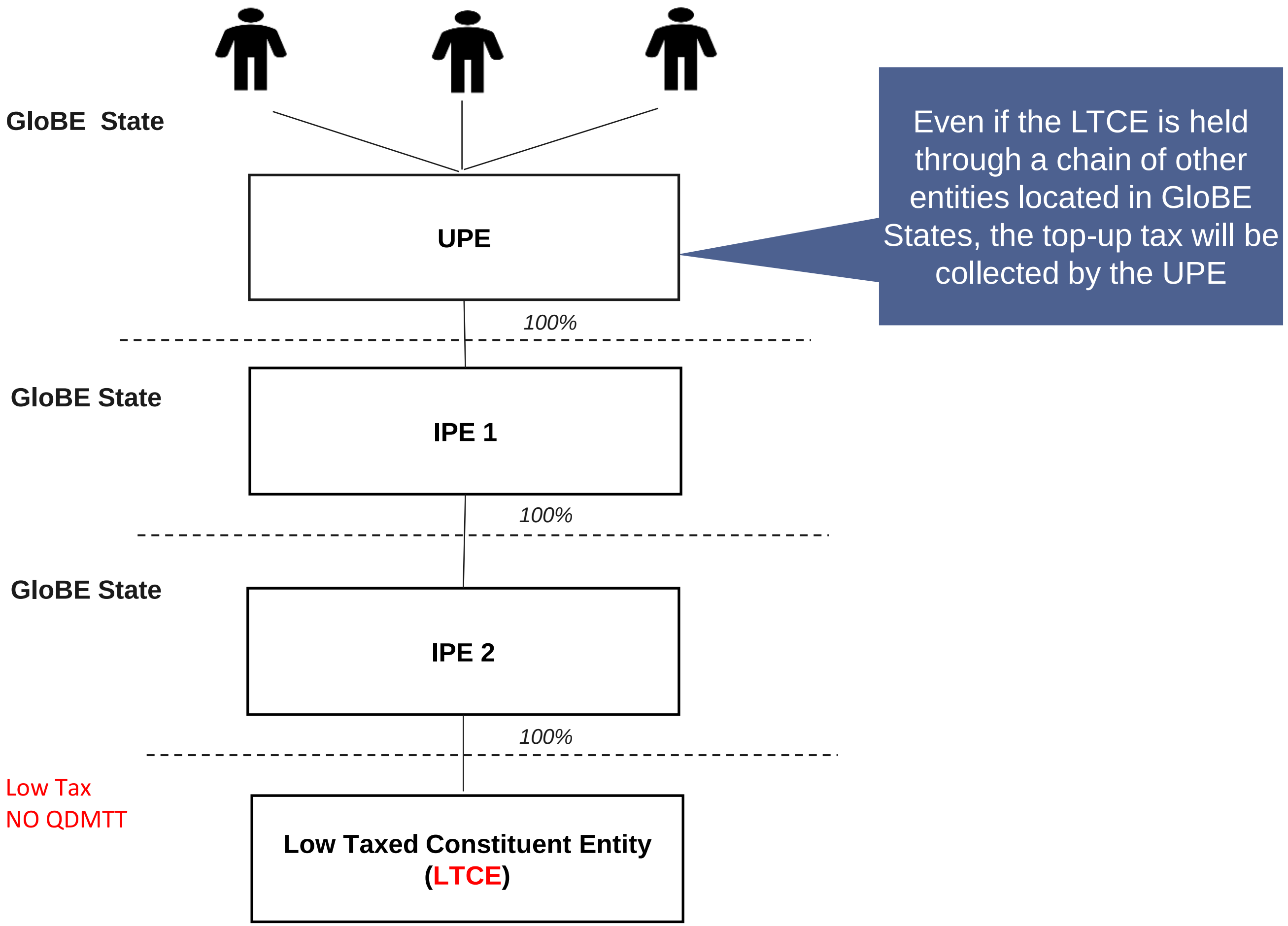
Under the IIR, the minimum tax is paid at the level of the parent entity, in proportion to its Ownership Interests in those entities that have low taxed income. Generally, the IIR is applied at the top, at the level of the ultimate parent entity, and works its way down the ownership chain. Rules are also provided to allow the IIR to be applied by a parent entity in which there is a significant minority interest, to minimize leakage of low taxed income.

Undertaxed Profits Rule (or "**UTPR**")

This rule works by requiring an adjustment (such as a denial of a deduction) that increases the tax at the level of the subsidiary. The adjustment is an amount sufficient to result in the group entities paying their share of the top-up tax remaining after the IIR. The share of the top-up tax is calculated based on a formula, in proportion to the relative share of assets and employees. This helps to ensure the rule is administrable, but also attaches the adjustment to entities that are most likely to have the capacity to pay the required amount of top-up tax.

The IIR Liability | IPE

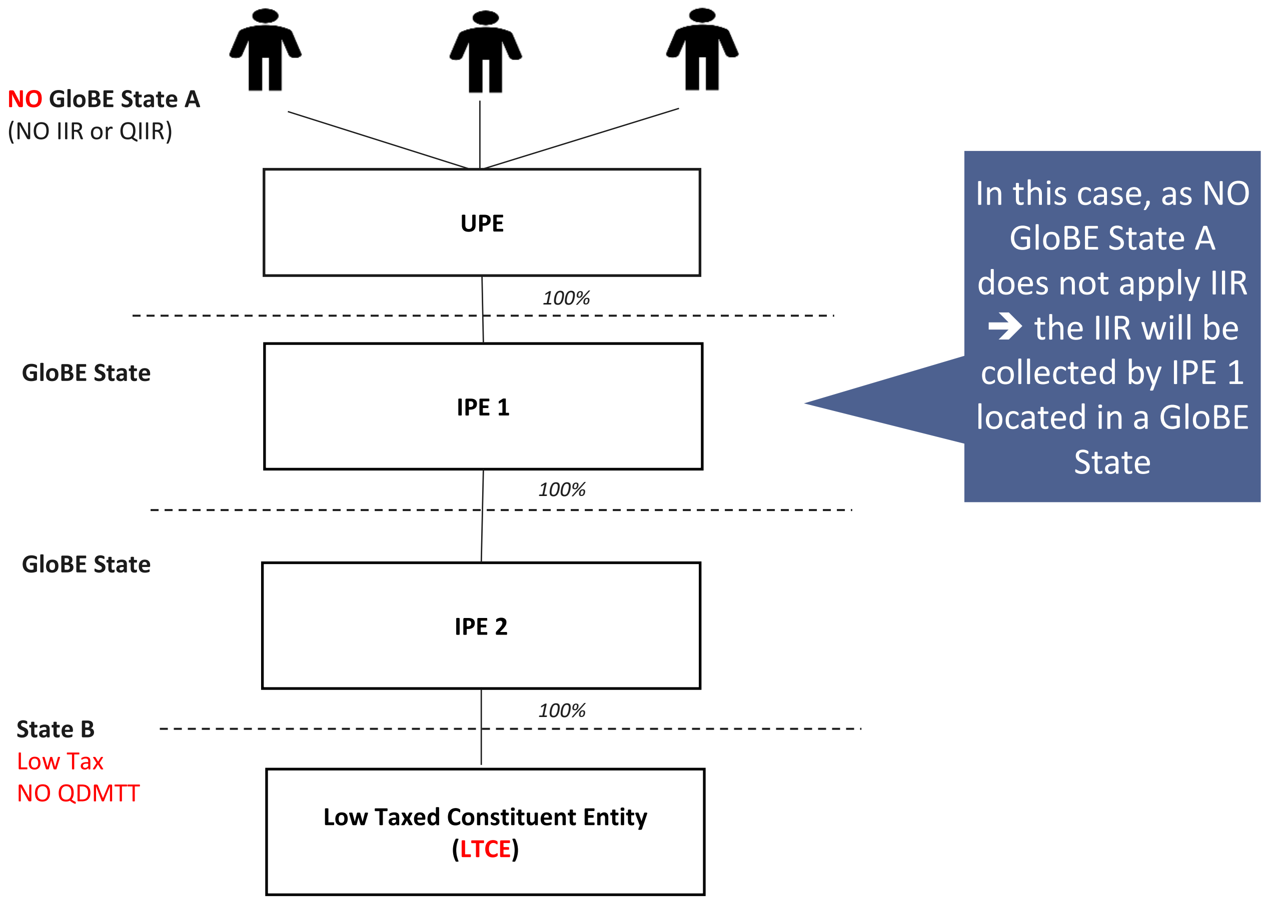
UPE in a GloBE State



✓ The **IIR** works by imposing a **<u>top-up tax</u>** on a parent entity in respect of the low-taxed income of group entities. The <u>IIR applies on a top-down basis</u>, which means that it is applied by the entity that is at, or near, the top of the ownership chain in the MNE Group, which is normally the UPE. <u>However</u>, <u>in case where the UPE does not apply the IIR</u>, one or more IPE will have to apply the IIR to their low-taxed constituent entities

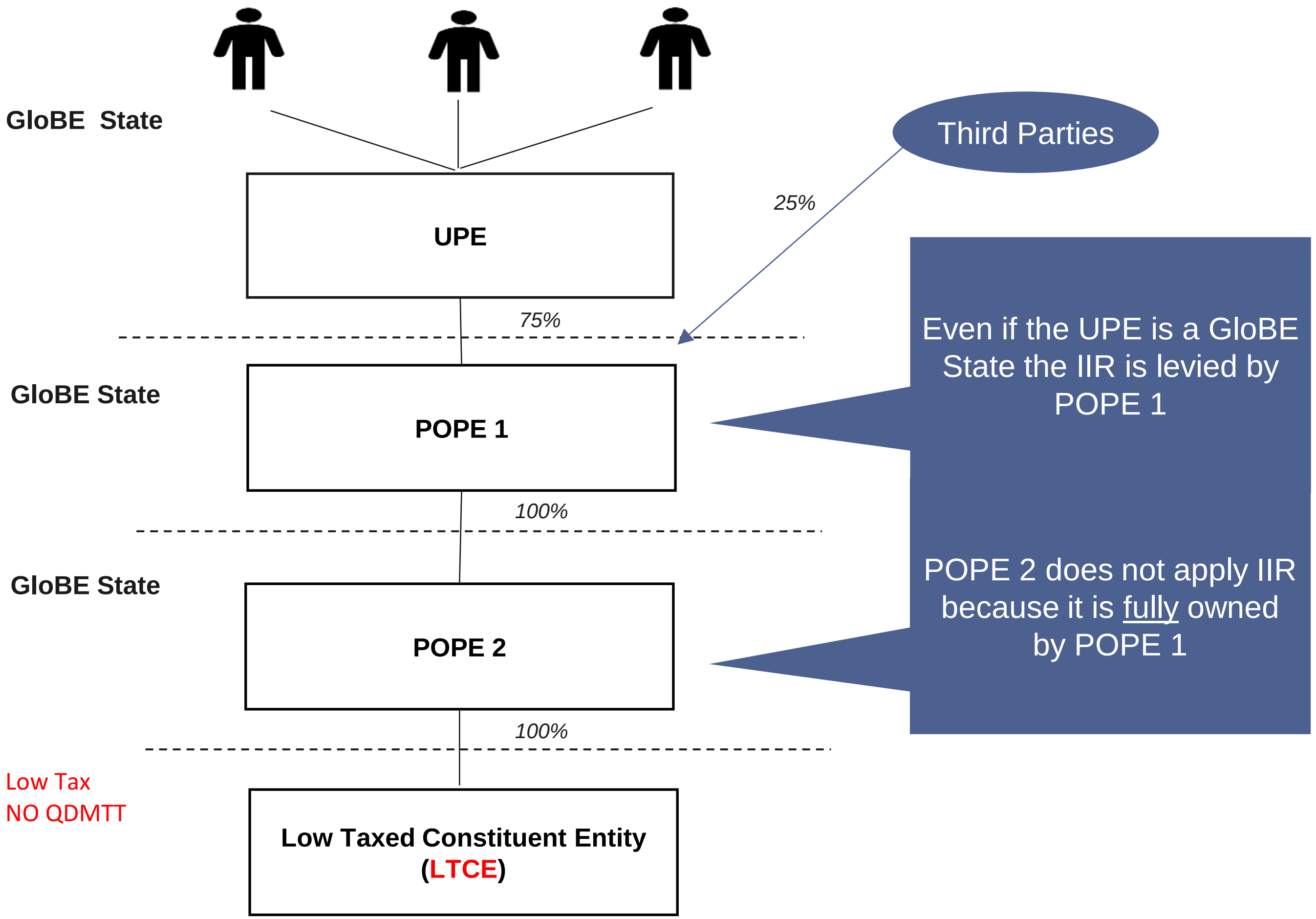
The IIR Liability | IPE

UPE not in a GloBE State



The IIR Liability | POPE

UPE in a GloBE State



- ✓ An exception to the top-down approach is provided when the ownership chain includes a POPE. In such cases, the POPE is required to apply the IIR even if the UPE applies the GloBE rules, but only to the extent of the top-up tax attributable based on the ownership share. Consequently, the UPE must reduce its top-up tax by the amount owed by the POPE. If the POPE is wholly owned by another POPE, the IIR is applied exclusively by the first one.

Allocation of the IIR top-up tax

1

IIR top-up tax due by Parent Entity = Top-up Tax of a low-taxed CE multiplied by parent entity's Allocable Share in such top-up tax

2

Allocable share = proportion of the parent entity's interest (*i.e.* income entitlement) in the income of the low-taxed CE

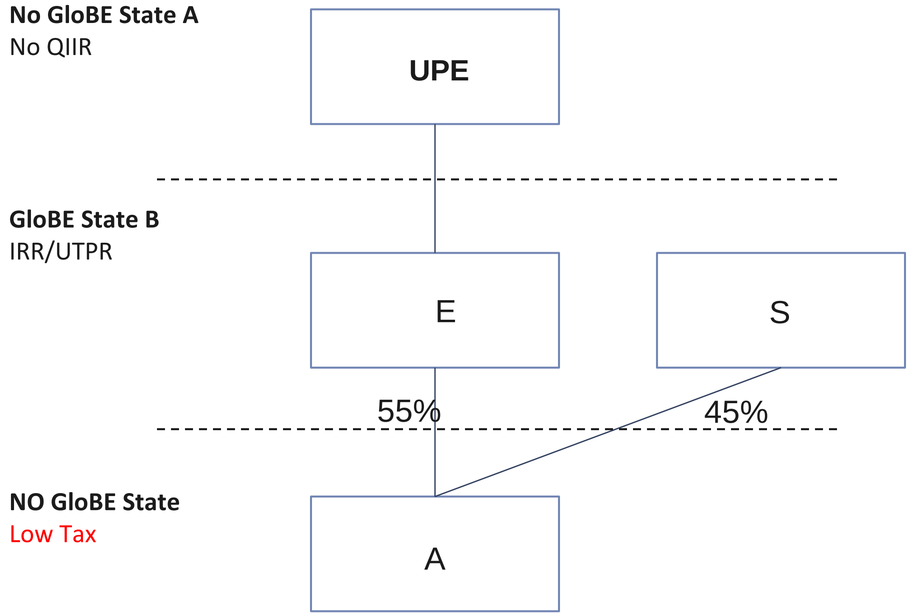
3

Include in the amount of the IIR Top-Tax due by Parent Entity the Top-up Tax computed for the parent entity itself

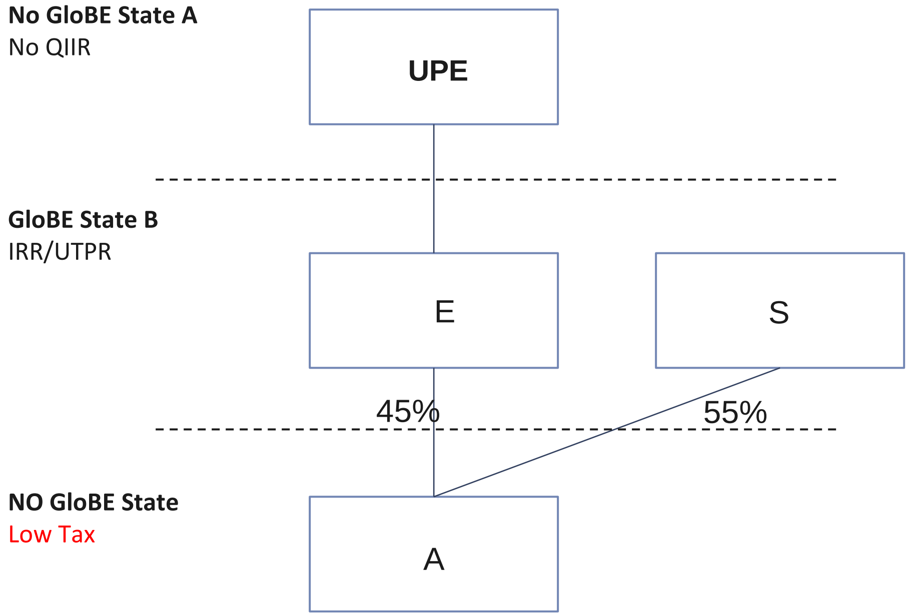
Allocation of the IIR top-up tax

The Top-up tax of the jurisdiction is allocated to the CEs in proportion to the GloBE Income or Loss of a specific CE as opposed to the GloBE Income or Loss of the jurisdiction

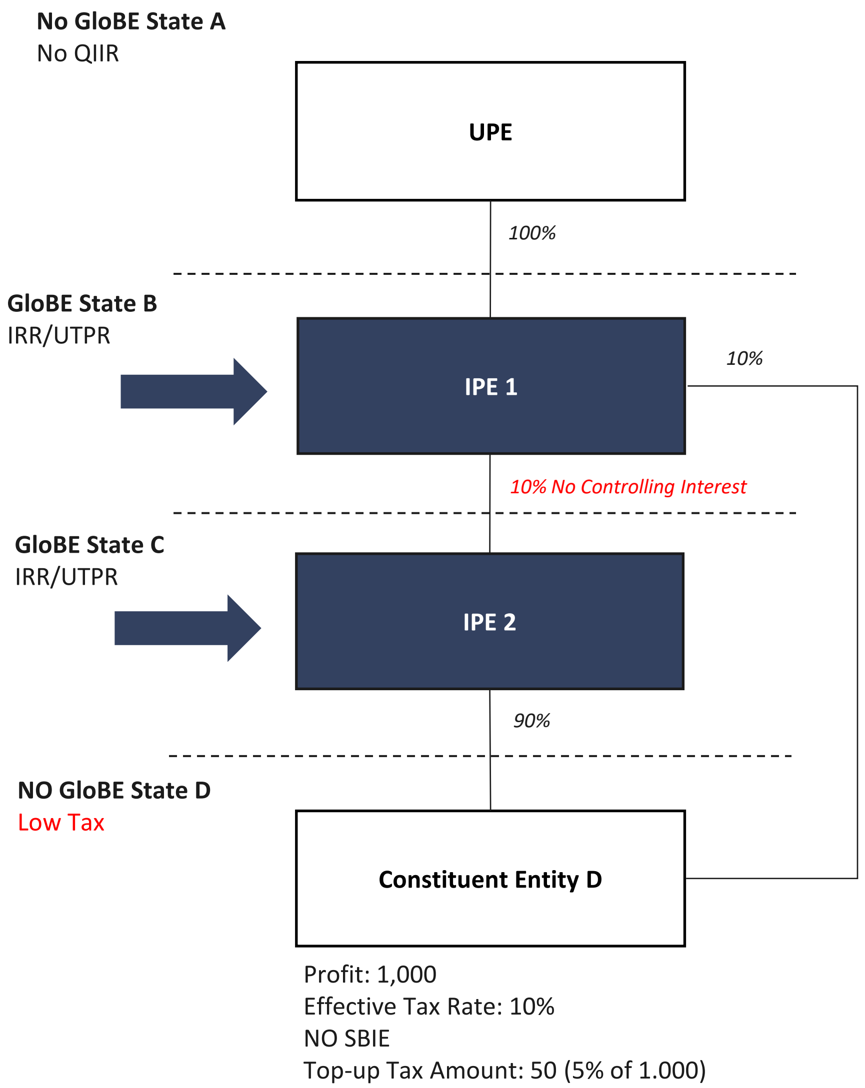
"A" Top-Up Tax Amount: 150
"A" GloBE Income: 2.000
GloBE Income of the jurisdiction:10.000
150 * (2.000/10.000) = 30
IRR of E: 55% of 30



"B" Top-Up Tax Amount: 150
"B" GloBE Income: 3.000
GloBE Income of the jurisdiction: 10.000
150 * (3.000/10.000) = 45
IRR of E: 45% of 45



Income Inclusion Rule Offset Mechanism



Art. 2.3. Income inclusion rule offset mechanism

A Parent Entity [IPE 1] that owns an Ownership Interest in a Low-Taxed Constituent Entity indirectly through an Intermediate Parent Entity [IPE 2] or a Partially-Owned Parent Entity that is not eligible for an exclusion from the IIR […] shall reduce its allocable share of a Top-up Tax of the Low-Taxed Constituent Entity […].

The reduction […] will be an amount equal to the portion of the Parent Entity's [IPE 1] Allocable Share of the Top-up Tax that is brought into charge by the Intermediate Parent Entity [IPE 2] or the Partially-Owned Parent Entity under a Qualified IIR.

With respect to this fact pattern, the GloBE Rules applies as follows:

a) IPE 2 level

IPE 2 applies IIR (Art. 2.1.2 MR) and collects a "top-up tax" with respect to the low-taxed profits of Constituent Entity D equal to €**45** (90% of 50 – *i.e.* 5% of 1000 *i.e.* Top-up tax Amount).

Art. 2.1.3(b) does not apply as IPE 1 does not have a Controlling Interest in IPE 2.

b) IPE 1 level

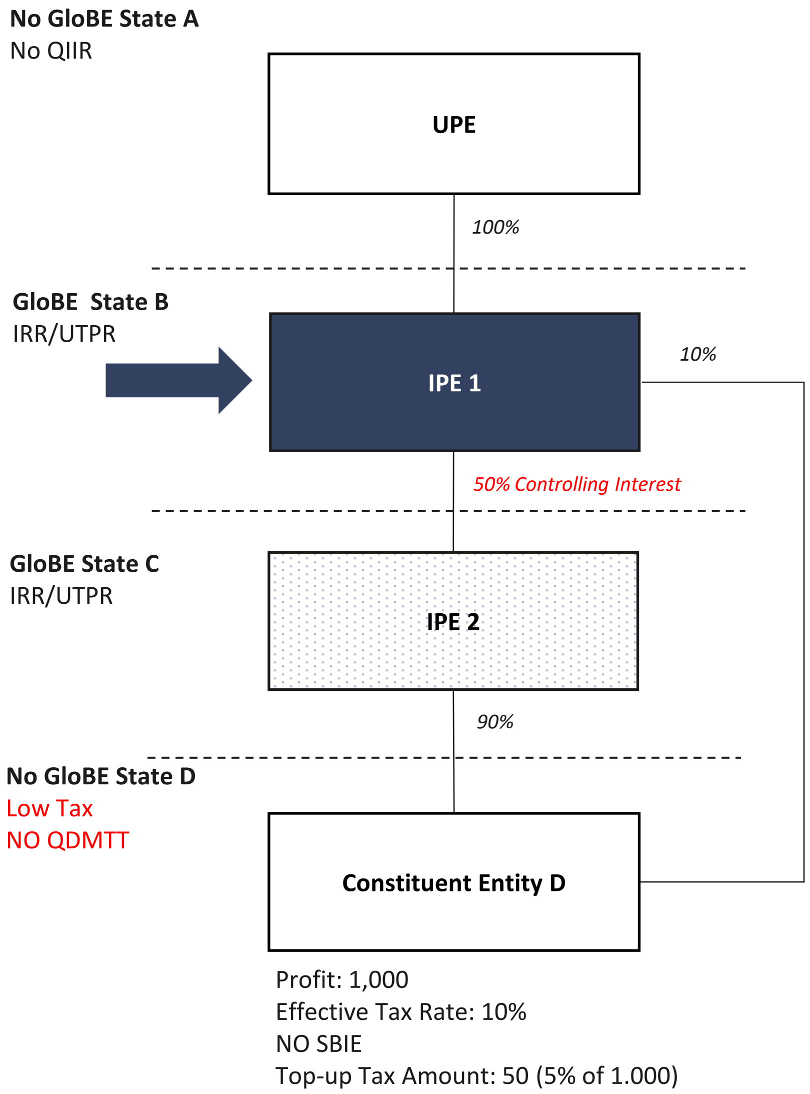
IPE 1 applies IIR (Art. 2.1.2 MR) with respect to:

- 10% of the relevant profits of Constituent Entity D. Accordingly, it shall collect a "top-up tax" equal to **5** (10% of 50 *i.e.* 5% of 1000 *i.e.* Top-up tax Amount).
- 9% of the relevant profits of Constituent Entity D with respect the indirect ownership interest through IPE 2. Accordingly, it shall collect a "top-up tax" equal to **4.5** (10% of 90% of 50 – i.e. 5% of 1000 *i.e.* Top-up tax Amount).

Under Art. 2.1.2, IPE 1 should collect a "top-up tax" equal to 9.5 ➔ however, pursuant Art. 2.3.1 and 2.3.2 this amount shall be reduced by an amount of **4.5** ➔ IPE 1 only collects **5**.

NOTE: as IPE 1 does not have a controlling interest in IPE 2, Art. 2.1.3(b) does not apply ➔ both IPE 1 and IPE 2 apply the IIR pursuant to Art. 2.1.2.

Income Inclusion Rule Offset Mechanism



Art. 2.3. Income inclusion rule offset mechanism

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The reduction […] will be an amount equal to the portion of the Parent Entity's [IPE 1] Allocable Share of the Top-up Tax that is brought into charge by the Intermediate Parent Entity [IPE 2] or the Partially-Owned Parent Entity under a Qualified IIR.

With respect to this fact pattern, the GloBE Rules applies as follows:

Top-up Tax Amount: 5% of 1,000 = 50

a) IPE 2

IPE 2 should apply Art. 2.1.2 and collect a "top-up tax" with respect to the low-taxed profits of Constituent Entity D equal to €45 (90% of 50 *i.e.* 5% of 1,000 *i.e.* Top-up tax Amount).

However, Art. 2.1.3(b) applies as IPE 1 has a controlling interest in IPE 2 ➔ IPE 2 does not apply IIR.

b) IPE 1

IPE 1 applies Art. 2.1.2 with respect to:

- **10%** of the relevant profits of Constituent Entity D. Accordingly, it shall collect a Top-up Tax Amount equal to **5** (10% of 50 *i.e.* 5% of 1,000 *i.e.* Top-up tax Amount).
- **50% of 90%** of the Top-up Tax Amount. Accordingly, it shall collect a "top-up tax" equal to **22.5.**

Application of the UTPR

1

UPE is located in a **Low Tax** Third Country that does **not apply a Qualified IIR** in respect of itself and its low taxed CEs located in the same jurisdiction

2

CE in a GloBE State is <u>not</u> an **Investment Entity**

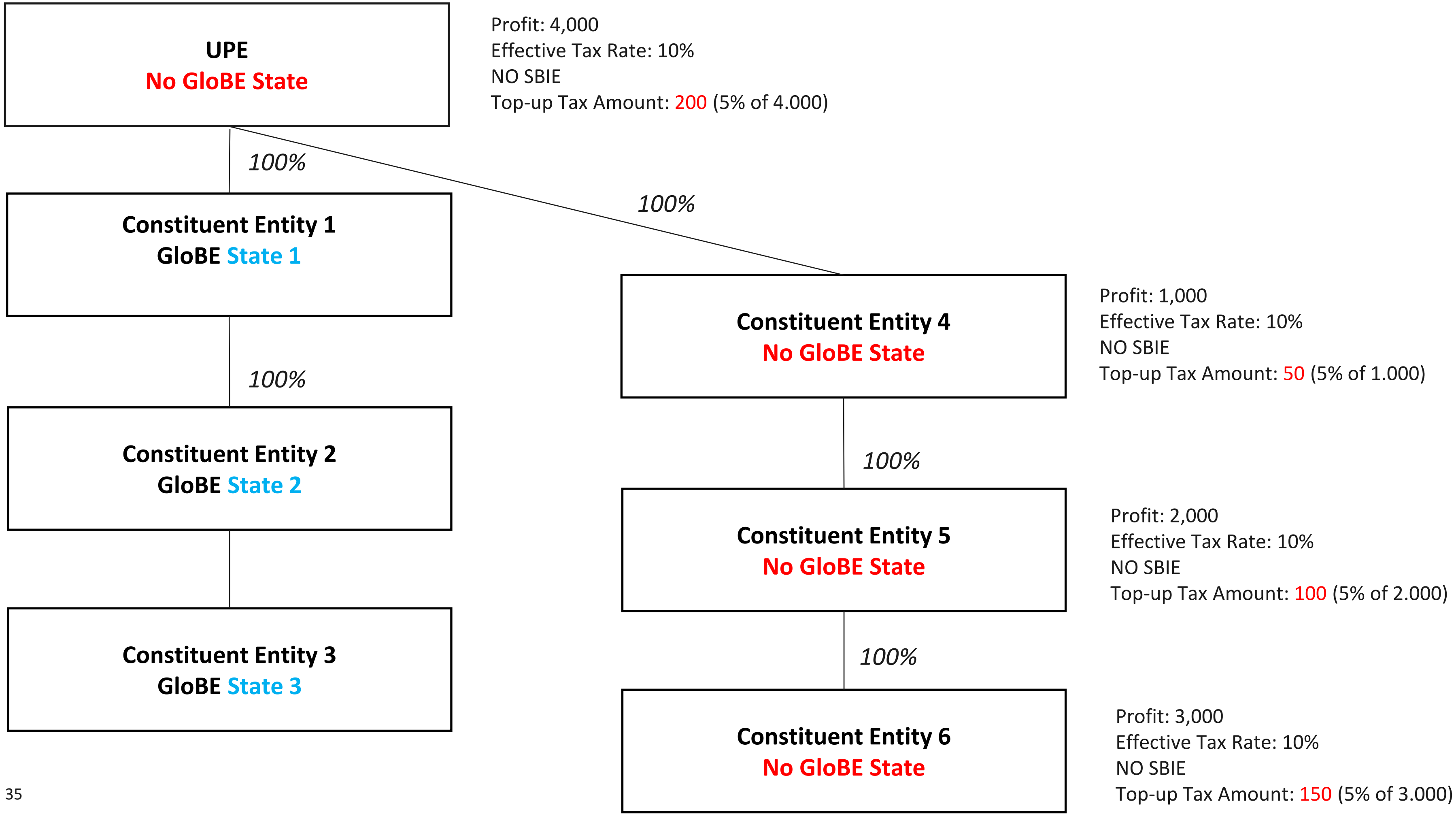
CE in a GloBE State is subject to **UTPR top-up tax** for amount allocated to a GloBE State

UTPR

Top-up tax Amounts not subject to GloBE Rules: 200 + 50 + 100 + 150 = **500**
500 must be allocated to GloBE States (1 - 2 - 3) based on certain apportionment keys
500 are taxes to be paid!

Total Apportionment Keys: 100
State 1- apportionment keys: 33% * 500 = 165 allocated to State 1 – to be further allocated to State 1 CEs
State 2 - apportionment keys: 27% * 500 = 135 allocated to State 2 – to be further allocated to State 2 CEs
State 3 - apportionment keys: 40% * 500 = 200 allocated to State 3 – to be further allocated to State 3 CEs

GloBE State
Low Tax



Application of the UTPR

UTPR Top-up Tax Amount

1

UTPR Top-up Tax

- It is the sum of Top-up Tax of all low-taxed CEs of MNE Group
- Adjustments:
  - UTPR Top-up Tax Amount is equal to zero if all of the ultimate parent entity's ownership interests in such low-taxed constituent entity are held directly or indirectly by one or more parent entities, which are required to apply a qualified IIR in respect of that low-taxed constituent entity (Art. 13(3))
  - Reduced by amount of top-up tax allocated to parent entities which are located in third country with QIIR (Art. 13(4))

✖

2

UTPR percentage

$$50\% \frac{\textit{Number of Employees in the jurisdiction}}{\textit{Number of Employees in all UTPR jurisdictions}}$$

$$50\% \frac{\textit{Tangible assets in the jurisdiction}}{\textit{Tangible assets in all UTPR jurisdictions}}$$

UTPR Percentage

UTPR %: deemed to be zero if a GloBE State has not collected the UTPR top-up tax amount of a prior fiscal year

The QDMTT

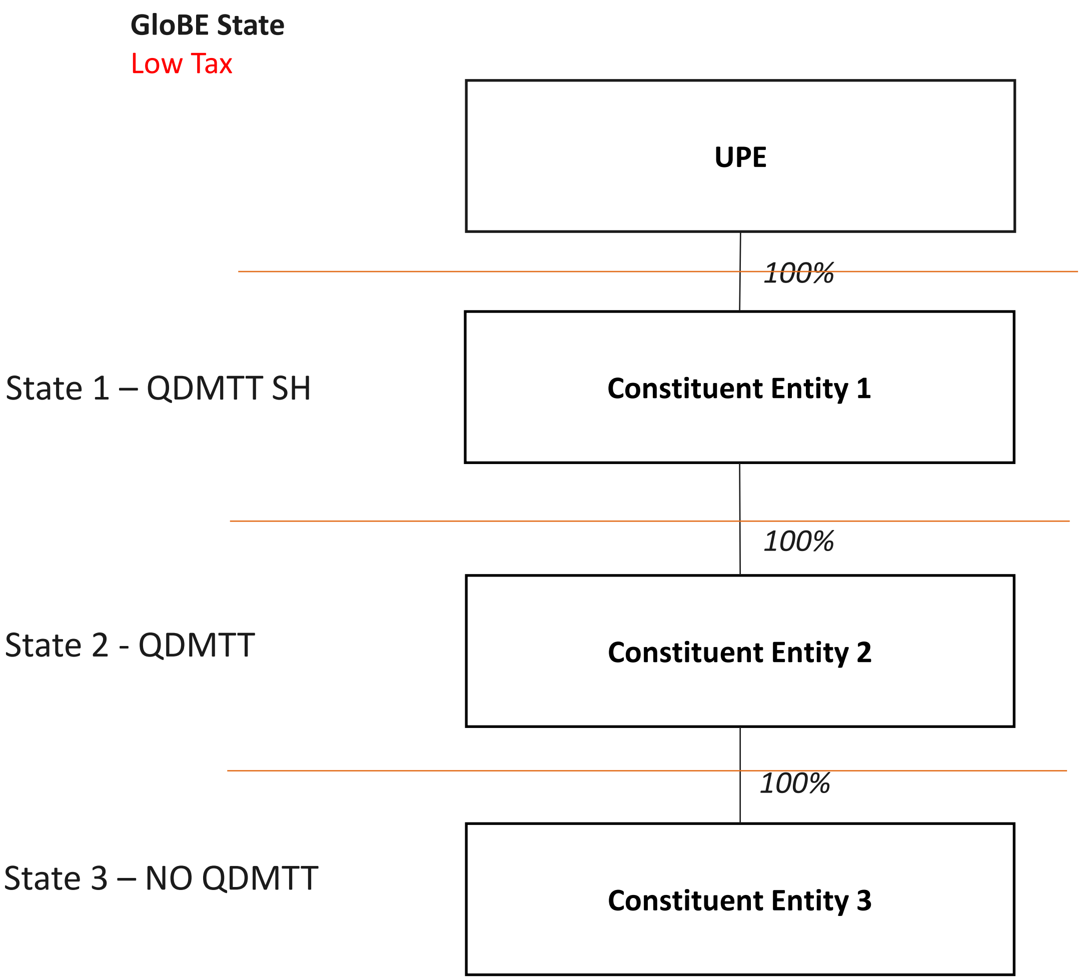
A **Qualified Domestic Minimum Top-up Tax** (QDMTT) is defined as a domestic minimum tax that applies to **local constituent entities** of multinational enterprises within the scope of the GloBE rules and achieves results consistent with those rules. The implementation of a QDMTT does not preclude the imposition of international top-up taxes under the IIR or the UTPR, but it is creditable against these top-up taxes.
The implementation of the QDMTT is not required as part of the internationally agreed-upon "common approach" to Pillar 2. Nevertheless, it is widely believed that there are compelling incentives for its adoption.

The QDMTT effectively (or almost entirely) prevents the transfer of tax revenues that would otherwise take place when an MNE generates excess profits in a low-tax jurisdiction where the ETR on local MNE profits falls below 15%.So the top-up tax is **primarily collected "at the source"** rather than in the jurisdiction where the parent entity is based or in a UTPR jurisdiction.

The QDMTT **alleviates the need for jurisdictions to reform or reduce domestic tax incentives**. With the implementation of GloBE by other countries, these incentives might be partially or fully offset by the international top-up tax. This could lead to revenue losses without enhancing the jurisdiction's appeal as a location for investment or profit shifting. The QDMTT helps prevent revenue leakage while maintaining the benefits of incentives as much as possible. Entities outside the scope of the rule can continue to fully benefit from all available incentives.

A QDMTT offers multinational enterprises (MNEs) a **safe harbor from the international top-up tax**, **relieving** them **from the additional burden of calculating ETR** for GloBE purposes, provided the QDMTT's design and administration comply with certain requirements (such as the Accounting Standard, the Consistency Standard, and the Administration Standard).

The Domestic Top-up Tax



Domestic Top-up Tax (DMTT)

If a jurisdiction has a domestic minimum tax that is consistent with the Pillar Two Model Rules (“**Qualified Domestic Minimum Top-up Tax**”, or “**QDMTT**”), such domestic tax eliminates any top-up tax liability under the GloBE rules when it is treated as a QDMTT Safe Harbour.

When it is not treated as a QDMTT safe harbour, the domestic tax is credited against any Pillar Two minimum tax liability.

UPE:

- does not levy IIR with respect to CE 1
- levies IIR with respect to CE 2 but credit the QDMTT of State 2 against IIR to-up tax
- levies IIR with respect to CE 3

Transitional Safe Harbours

Transitional Safe Harbours

- ✓ The **Transitional CbCR Safe Harbour** is designed as a short-term measure that would effectively exclude an MNE's operations in certain lower-risk jurisdictions from the scope of GloBE in the initial years, thereby providing relief to MNEs in respect of their GloBE compliance obligations as they implement the rules.

- ✓ The Transitional CbCR Safe Harbour uses Revenue and Profit (Loss) before Income Tax from an MNE's CbC Report and income tax expense from an MNE's financial accounts (after eliminating taxes which are not Covered Taxes and Uncertain Tax Positions) to determine whether the MNE's operations in a jurisdiction meet these tests.

Transitional Safe Harbours

✓ During the Transition Period, the Top-up Tax in a jurisdiction for a Fiscal Year shall be deemed to be zero where:

(a) the MNE Group reports Total Revenue of less than EUR 10 million and Profit (Loss) before Income Tax of less than EUR 1 million in such jurisdiction on its Qualified CbC Report for the Fiscal Year **[De Minimis Test]**; or

(b) the MNE Group has a Simplified ETR that is equal to or greater than the Transition Rate in such jurisdiction for the Fiscal Year **[ETR Test]**; or

(c) the MNE Group's Profit (Loss) before Income Tax in such jurisdiction is equal to or less than the Substance-based Income Exclusion amount, for constituent entities resident in that jurisdiction under the CbCR, as calculated under the GloBE Rules **[Routine Profits Test]**.

- **Qualified CbC Report** means a Country-by-Country Report prepared and filed using Qualified Financial Statements

- **Total Revenue** means an MNE Group's Total Revenues in a jurisdiction as reported on its Qualified CbC Report

- **Profit (Loss) before Income Tax** means an MNE Group's Profit (Loss) before Income Tax in a jurisdiction as reported on its Qualified CbC Report

- **Simplified Covered Taxes** is a jurisdiction's income tax expense as reported on the MNE Group's Qualified Financial Statements, after eliminating any taxes that are not Covered Taxes and uncertain tax positions reported in the MNE Group's Qualified Financial Statements.

- **Simplified ETR** is calculated by dividing the jurisdiction's Simplified Covered Taxes by its Profit (Loss) before Income Tax as reported on the MNE Group's Qualified CbC Report.

Transitional Safe Harbours

- ➢ **Transition Period** covers all of the Fiscal Years beginning on or before 31/12/2026 but not including a Fiscal Year that ends after 30/6/2028.

- ➢ **Transition Rate** means:
  - (a) 15% for Fiscal Years beginning in 2023 and 2024;
  - (b) 16% for Fiscal Years beginning in 2025; and
  - (c) 17% for Fiscal Years beginning in 2026.

- ✓ The Transitional CbCR Safe Harbour applies only where the MNE Group prepares its CbC Report using Qualified Financial Statements

- ✓ **Qualified Financial Statements** means:

a) the accounts used to prepare the Consolidated Financial Statements of the UPE (to mirror the requirement under Article 3.1.2);

b) separate financial statements of each Constituent Entity provided they are prepared in accordance with either an Acceptable Financial Accounting Standard or an Authorised Financial Accounting Standard if the information contained in such statements is maintained based on that accounting standard and it is reliable; or

c) in the case of a Constituent Entity that is not included in an MNE Group's Consolidated Financial Statements on a line-by-line basis solely due to size or materiality grounds, the financial accounts of that Constituent Entity that are used for preparation of the MNE Group's CbC Report.

Transitional Safe Harbours

- ✓ An MNE Group has not applied the Transitional CbCR Safe Harbour with respect to a jurisdiction in a Fiscal Year in which the MNE Group is subject to the GloBE Rules, the MNE Group cannot qualify for that safe harbour for that jurisdiction in a subsequent year ➔ “**Once Out Always Out**”

- ✓ To access the safe harbour, the MNE Group would need to comply with the filing requirements in the GloBE Information Return that are specific to the Transitional CbCR Safe Harbour. For example, a Tested Jurisdiction that would like to apply the routine profits safe harbour would need to include, in its GloBE Information Return, the same information for its SBIE calculation that it would otherwise be required to include if it performed a full SBIE calculation under Article 5.3 of the GloBE Rules.