PUBLICATION OF THE PILLAR TWO MODEL RULES

Global Anti-Base Erosion Model Rules

Introduction

On the 20th of December 2021, the OECD published the Global Anti-Base Erosion Model Rules ("**GloBE-rules**") under Pillar Two. The GloBE-rules under Pillar Two aim to create a system of taxation whereby Multinational Enterprise Groups ("**MNE Groups**") have to pay a certain minimal level of tax on income in each jurisdiction in which they are active.

In this newsletter, we briefly elaborate the purpose and the consequences of the GloBE-rules under Pillar Two.

Purpose

In 2016, the OECD and the G20 formed the OECD/G20 Inclusive Framework on BEPS, starting a project in order to tackle domestic tax base erosion and profit shifting ("**BEPS**") by MNE Groups. BEPS aims to combat tax planning strategies used by multinational enterprises that exploit gaps and mismatches in tax rules to avoid paying tax. In July 2021 a statement was issued on a Two-Pillar solution to address the tax challenges arising from the digitalisation of the economy, more specifically to reform the international taxation rules and ensure that multinational enterprises pay a fair share of tax wherever they operate and generate profits. Pillar One relates to the introduction of a new special purpose nexus rule permitting the allocation of profits to different jurisdictions and Pillar Two introduces a global minimum tax of 15% on MNE's with a revenue in excess of EUR 750 million.

Apart from the introduction of the global minimum corporate tax rate of 15% for MNE's, the Pillar Two model rules define the scope and set out the mechanism for the GloBE-rules intended to ensure that MNE's pay 15% tax on income generated in each of the jurisdictions in which they operate. Moreover, a template is provided to governments enabling them to implement the GloBE-rules into the domestic legislation in 2022. These rules, among others, define what a MNE Group consists of, when such a Group is effected by the minimum tax rate and address administrative aspects.

Scope

Under Pillar Two, a global minimum tax rate on corporate income of 15% is set. 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'. A MNE Group in this context, means any Group that includes one or more entities or permanent establishments, located in other jurisdictions than the **UPE**. Entities such as Governmental bodies, International organisations, non-profit organisations (including charitable entities), or entities that meet the definition of a pension, investment or real estate fund are excluded from these measures.

MNE Groups falling in the scope, have to calculate their effective tax rate based on the GloBE mechanics on an annual basis for each jurisdiction where they operate. In case the effective tax rate is below 15%, a top-up tax for the difference between the effective tax rate per jurisdiction and the 15% minimum rate is generally charged to the UPE of the MNE Group.

The Pillar Two model rules acknowledge that jurisdictions preserve tax sovereignty and therefore leaves the possibility to jurisdictions to introduce their own domestic minimum top-up tax based on the GloBE mechanics. This local top-up tax is then fully creditable against any liability under GloBE.

The Pillar Two model rules also address the treatment of corporate restructurings, particular holding structures and tax neutrality and distribution regimes

Summary

The publication by the OECD of the GloBE-rules under Pillar Two, is a next step in striving to eliminate harmful tax competition and aggressive tax planning.

Where BEPS already introduced minimum substance requirements and transparency rules to combat the use of shell companies, Pillar Two should now ensure that MNE's falling in the scope of these measures pay a minimum effective tax rate of 15% on profits generated in low or no tax jurisdictions (so called "tax havens"). It is expected that with a rate of 15%, the global minimum tax will generate around USD 150 billion in additional global tax revenues per year.

Following this OECD publication, the EU published a proposal for an EU Directive regarding the implementation of Pillar Two on the 22nd of December 2021. In the Course of 2022, the OECD will produce more guidance after public consultations to be held in the first quarter of 2022. The OECD provides for a very ambitious timeline to ensure an effective implementation from 2023 onwards. However, given the amount of work yet to be done by the OECD and the EU, it is doubtful whether the rules indeed enter into force as from 2023.

We strongly advise entities that are part of a MNE Group, to determine whether they will be affected by the GloBE-rules under Pillar Two. Needless to say that we are pleased to assist you with any questions concerning the Pillar Two model rules and will keep you updated of any new developments.

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