L&L DIGITAL ECONOMY
TAXATION TEAM

# Pillar One & Pillar Two

## Determining the impact and how can you plan for the next steps?

15 July 2021 – Aline Nunes / Harmen van Dam

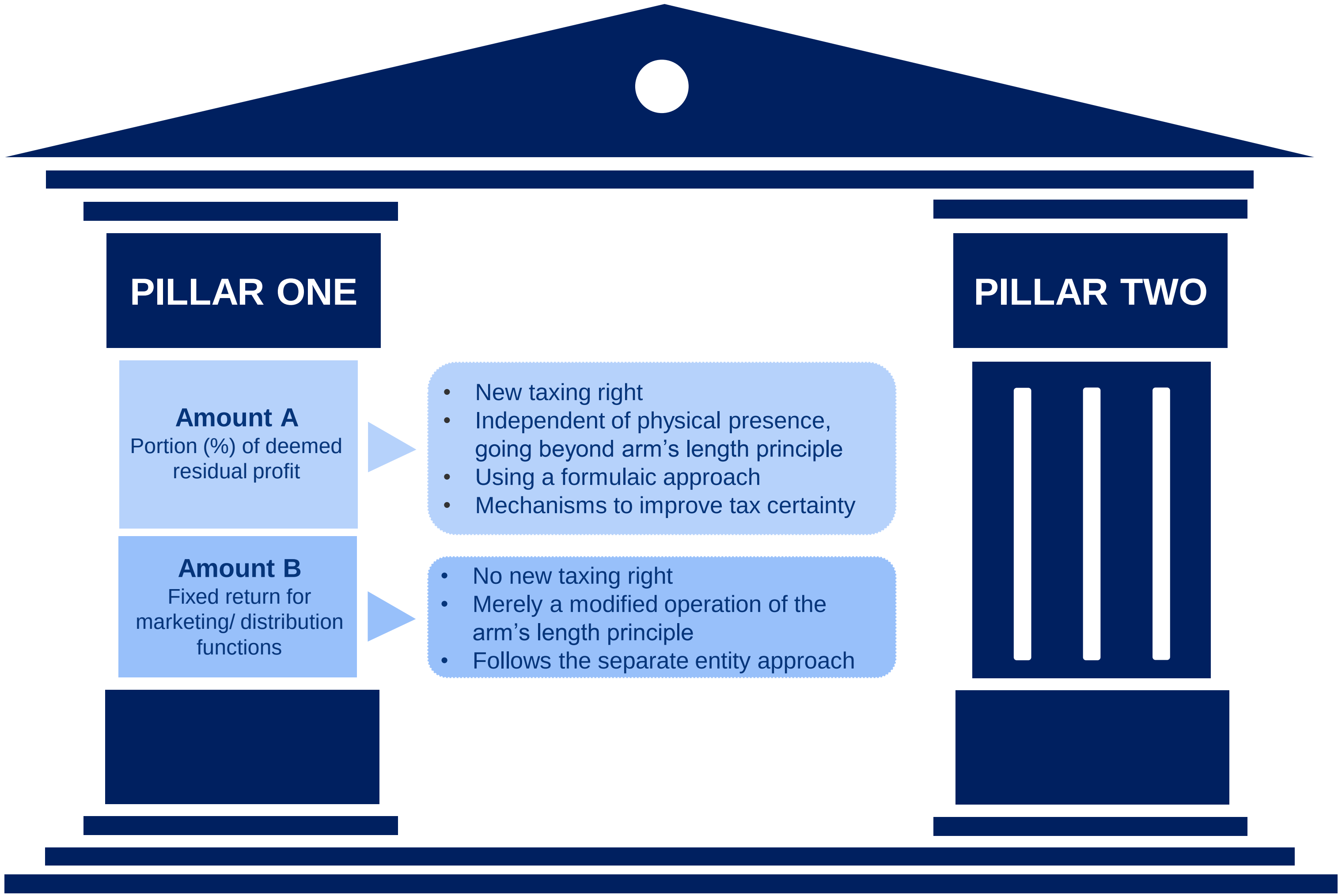
45318461

# Today's agenda

1. Welcome
2. Update on the latest developments
   a. Pillar One – new taxing rights for market/user jurisdictions
   b. Pillar Two – global minimum taxation
3. Case study
4. Next steps
5. Closing remarks

# 2 Update on the latest developments

# **Pillar One** – New taxing rights for market/user jurisdictions



# **Pillar One** – State of play

LOYENS LOEFF

## Key points from the 1 July OECD/G20 Inclusive Framework Statement*

- MNEs with a **global turnover > € 20bn** and pre-tax **profit margin > 10%**
- Extractives and Regulated Financial Services will be excluded

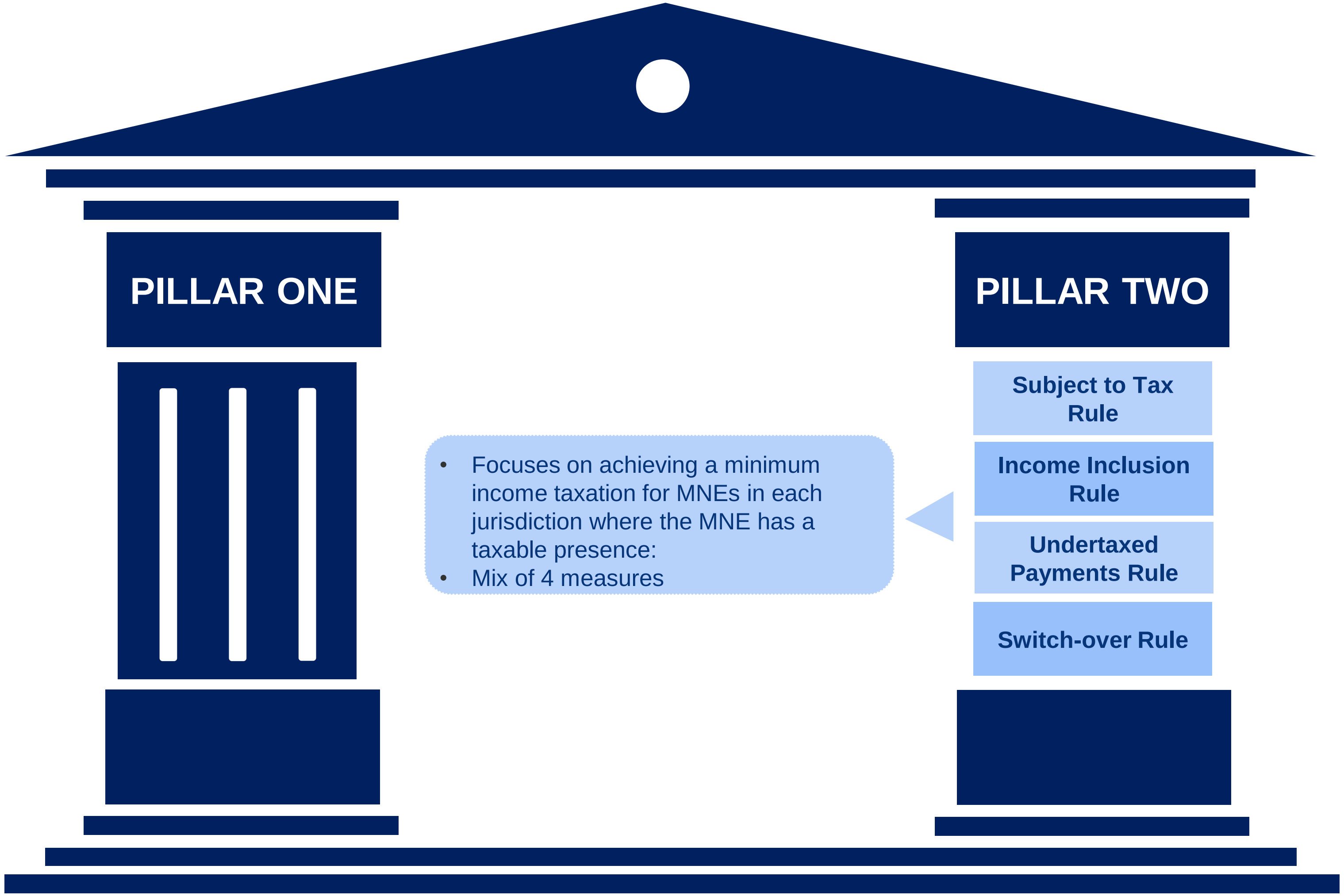
- **20-30%** of the **residual profit** (profit exceeding a 10% margin) will be allocated to market jurisdictions
- Apportionment pursuant to a revenue-based allocation key between jurisdictions with > € 1m of revenue

- **Segmentation** only in exceptional circumstances

- **Multilateral instrument** to implement Amount A available in 2022
- Target entry into force: **2023**

*Endorsed by G20 finance ministers and central bank governors on 9 July

# **Pillar Two** – Four measures for global minimum taxation



# **Pillar Two** – Four measures for global minimum taxation

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**Domestic legislation**

**Income Inclusion Rule (IIR)** 2

This rule would allow the inclusion of the income of a low taxed constituent entity in the tax base of the ultimate parent entity if that income was not taxed at a minimum effective tax rate.

**Undertaxed Payments Rule (UTPR)** 3

This is a secondary rule that applies as backstop to the IIR. The jurisdiction of the payer could deny a deduction or make an equivalent adjustment where the payment is made to a low taxed constituent entity.

**Tax treaties**

**Switch-over Rule (SOR)**

This rule would allow to switch from the exemption method to the credit method where the profits attributable to the foreign PE are low-taxed profits.

**Subject to Tax Rule (STTR)** 1

This rule would allow additional source taxation (withholding) and deny treaty benefits for "mobile payments" (interest, royalties, etc.) not sufficiently taxed in the recipient's jurisdiction.

**Parent/Residence jurisdiction**

**Source jurisdiction**

***Summary: The proposal works as worldwide minimum corporate taxation with either the source or the parent/residence jurisdiction picking up the tax if the other does not.***

# **Pillar Two** – State of play

LOYENS LOEFF

## Key points from the 1 July OECD/G20 Inclusive Framework Statement*

- Minimum **ETR** of **15%** for **IIR & UTPR**; minimum **nominal rate** of **[7.5%-9%]** for **STTR**
- **€ 750m global turnover threshold** confirmed *but* countries may optionally apply the IIR to MNEs headquartered in their jurisdiction even if they do not reach the € 750m turnover threshold
- International shipping income to be excluded

- Accommodation of distribution-based tax systems: income distributed within 3-4 years (with sufficient taxation) will not be low-taxed income for ETR computation purposes
- STTR: signatories commit to **amend** their **DTTs** with developing countries to enable them to levy this top-up WHT

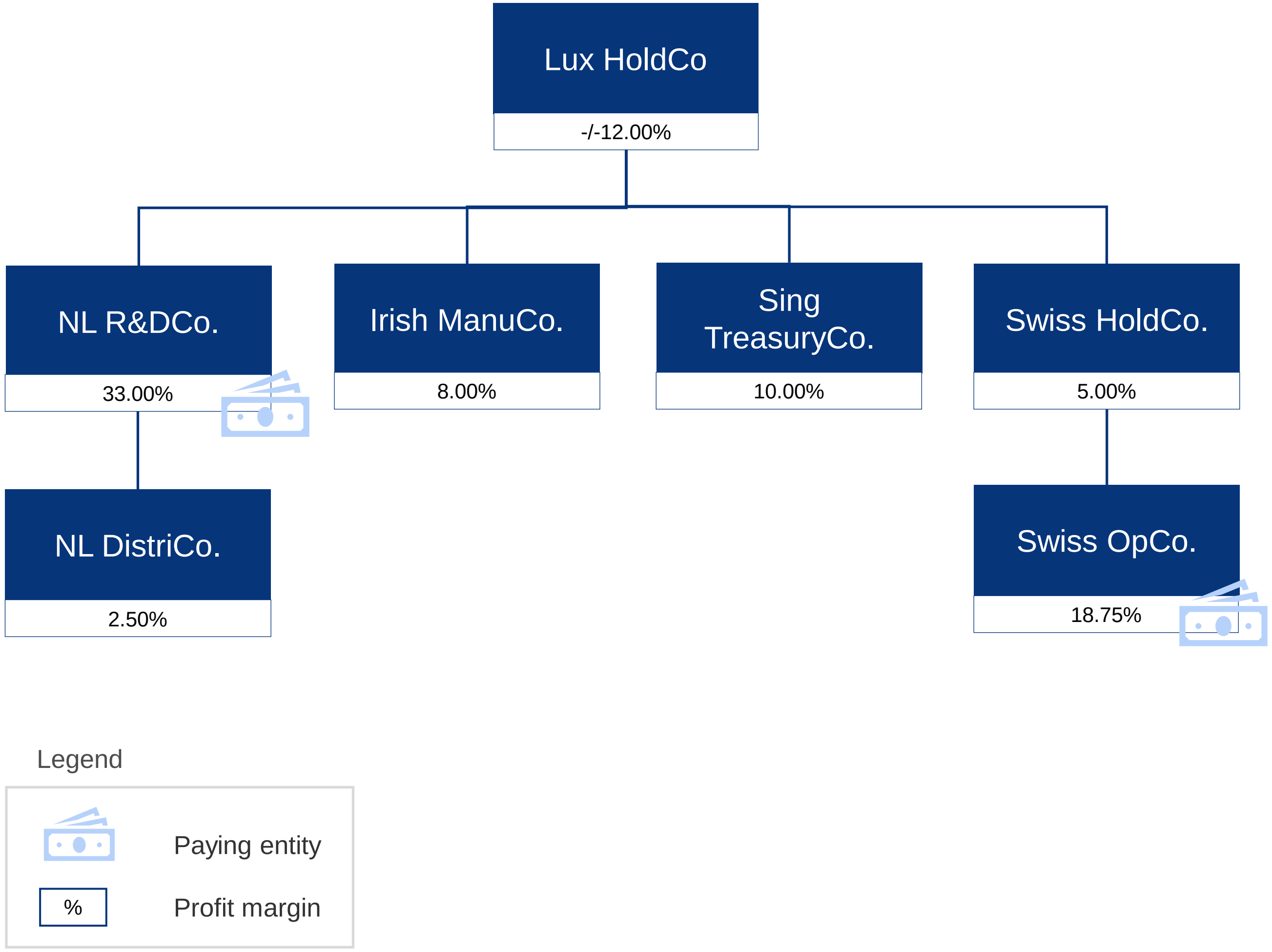
- **Substance-based carve-out** based on payroll and tangible assets (likely to be useful only for low-margin operations)

- Model legislation and multilateral instrument to implement STTR available in 2022
- Target entry into force: **2023** (UTPR might be optionally deferred)
- Commitment to respect OECD guidance/models if IIR is implemented (no obligation to implement, but obligation to respect other countries applying it)

*Endorsed by G20 finance ministers and central bank governors on 9 July

# 3 Case study

# **Pillar One** – Case study - Overview




**Consolidated**

| | |
|---|---|
| Third party revenue | € 25 billion |
| PBT | € 5.9 billion |
| Profit margin (%) | 23% |

# **Pillar One** – Case study – Amount A calculation



**Step 0a:** Determination of group standardized PBT
**Step 0b:** Determination of standardized PBT after deduction of losses

**€ 5.9 billion - € 0 = € 5.9 billion**

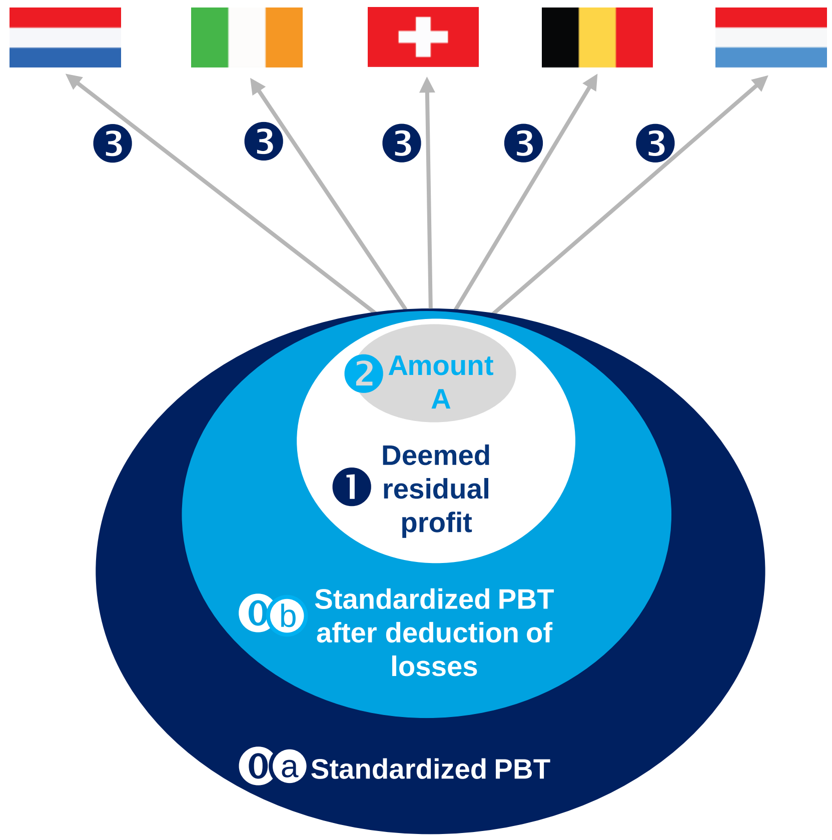
**Step 1:** "Deemed residual profit" =
PBT after deduction of losses -/- fixed % of revenue

**€ 5.9 billion – (10% x € 25 billion) = € 3.4 billion**

**Step 2:** Amount A =
Fixed % of deemed residual profit

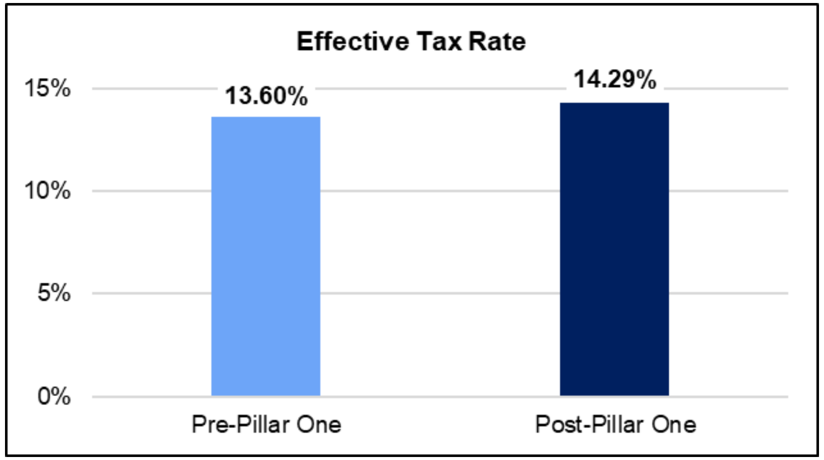
**€ 3.4 billion x 20% = € 675 million**

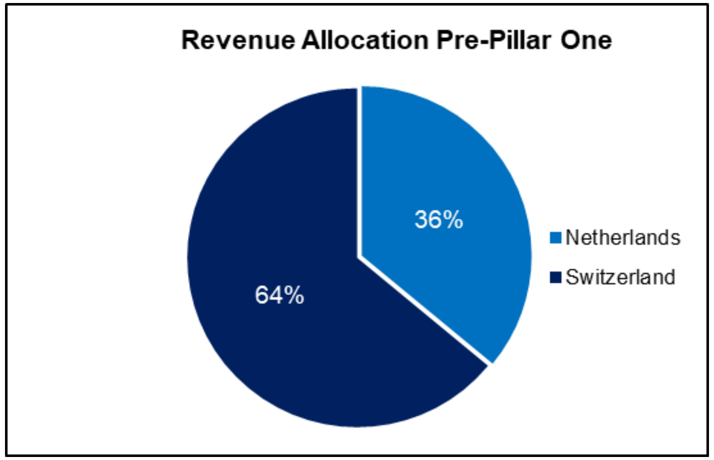
**Step 3:** Allocate relevant portion of Amount A to MJs using a revenue-based key

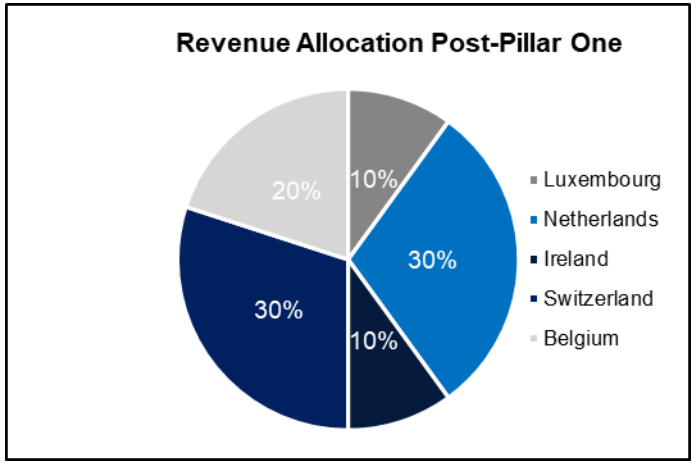


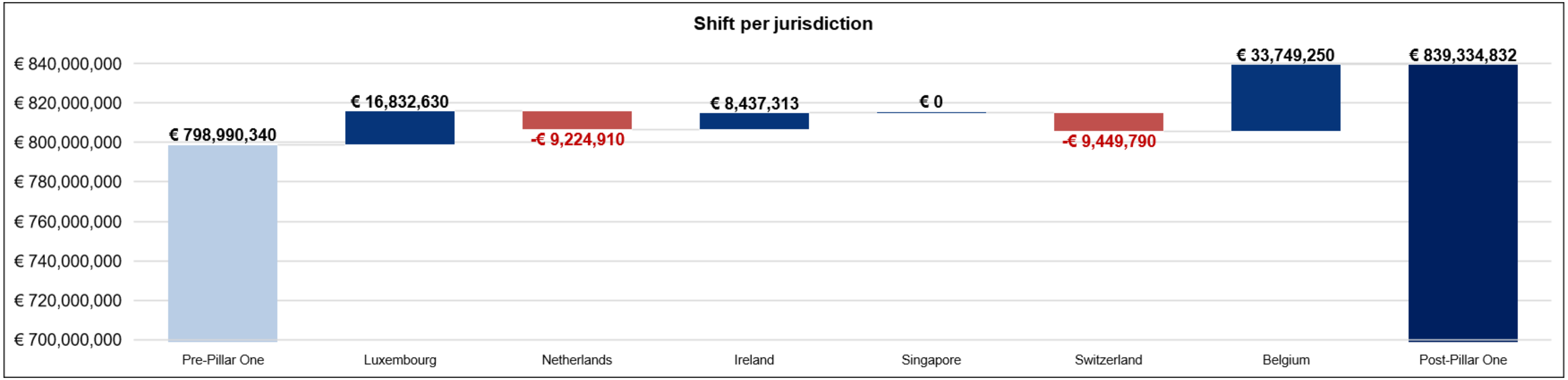
# **Pillar One** – Case study – Allocation





# **Pillar One** – Case study – Avoidance of double taxation

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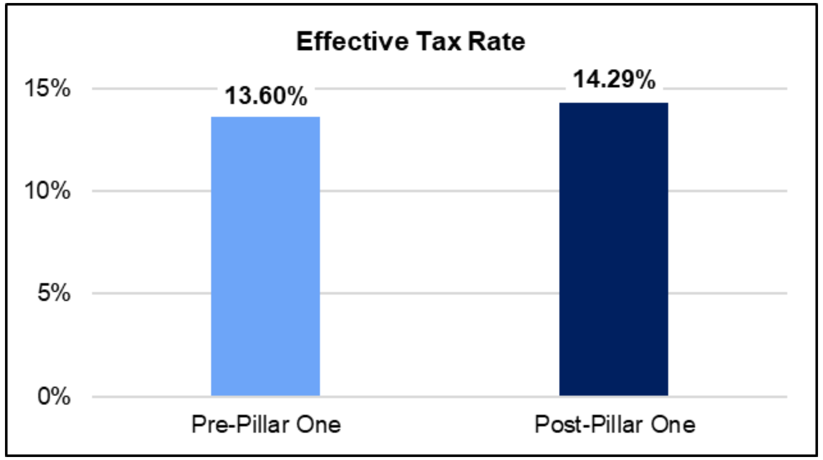
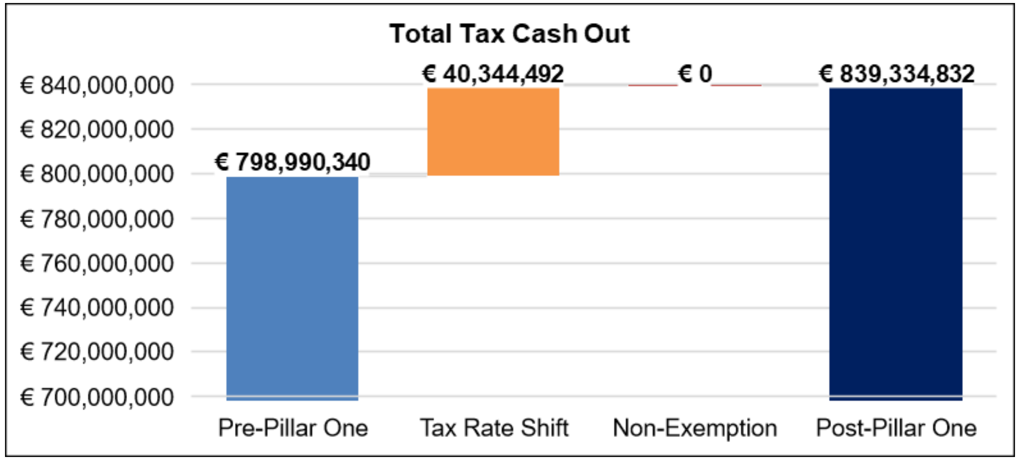
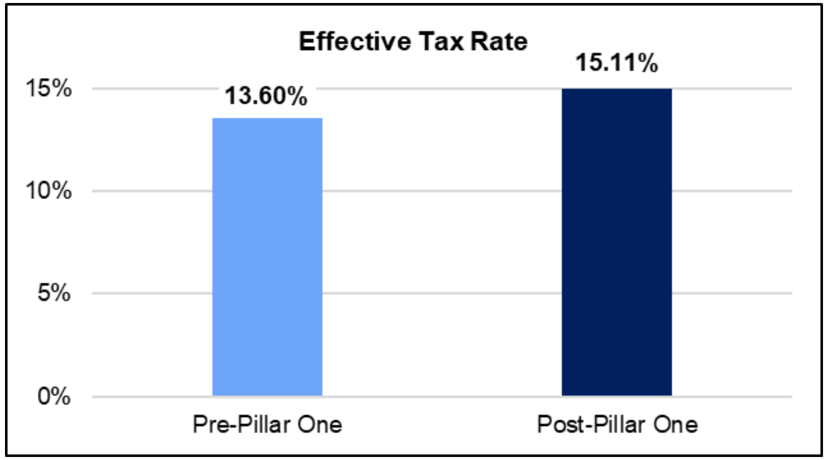
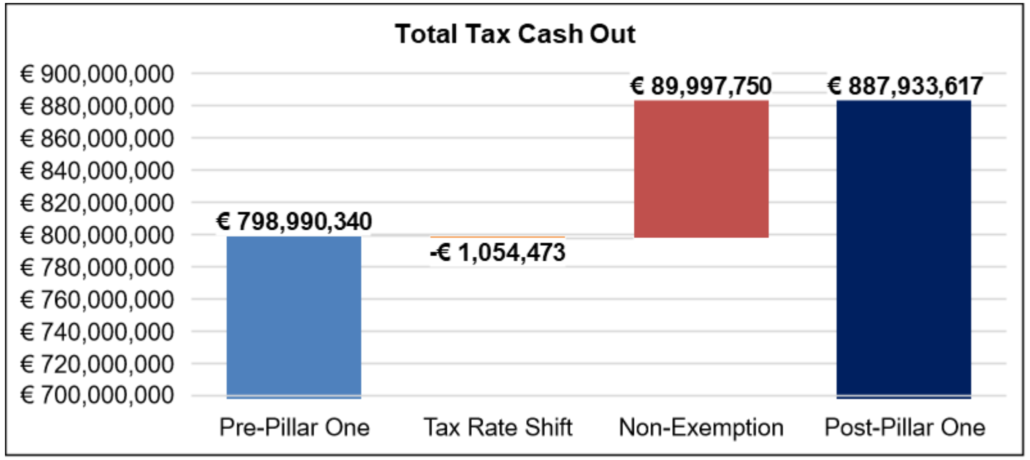
## All paying entities provide relief



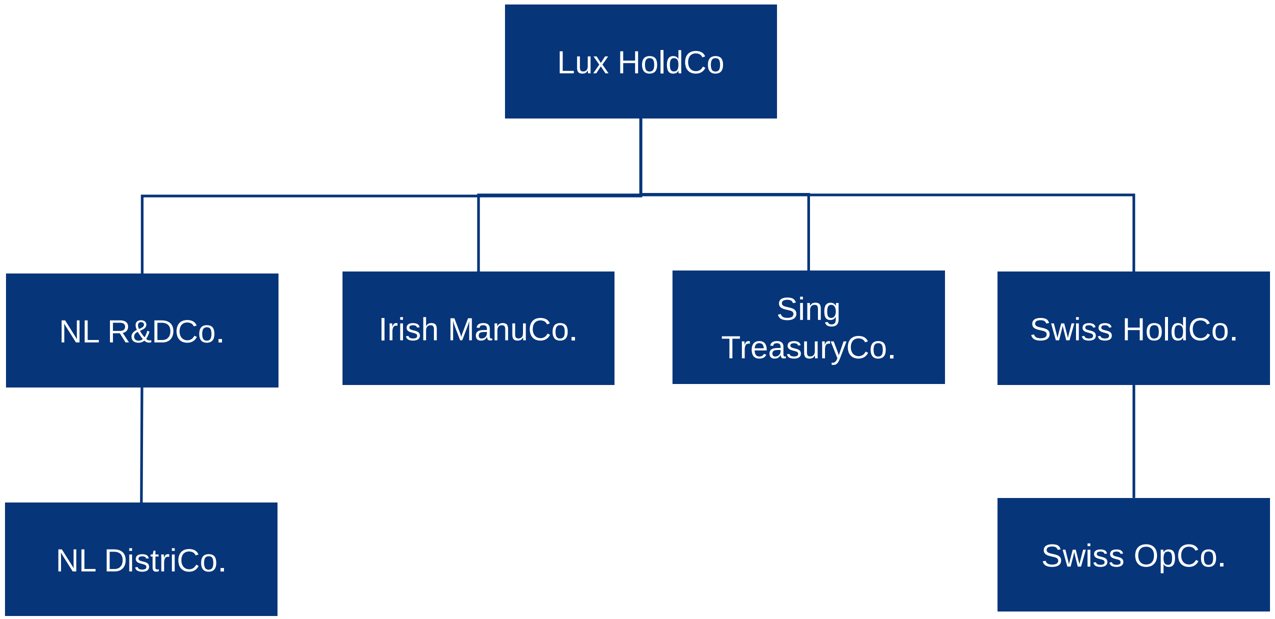




## Only one paying entity provides relief



# **Pillar Two** – Case study




## Preliminary high-level impact assessment

Exposure to GloBE rules (IIR & UTPR)

1) Are there group entities resident in jurisdictions with an ETR below 15% based on CbCR?

2) Is your head office jurisdiction's ETR at least 15% and is it committed to Pillar Two?

Exposure to STTR (top-up withholding tax)

3) Do you have intragroup interest or royalty payments to low-taxed entities (nominal minimum rate of [7.5%-9%])?

# Pillar Two – Case study

## Preliminary high-level impact assessment

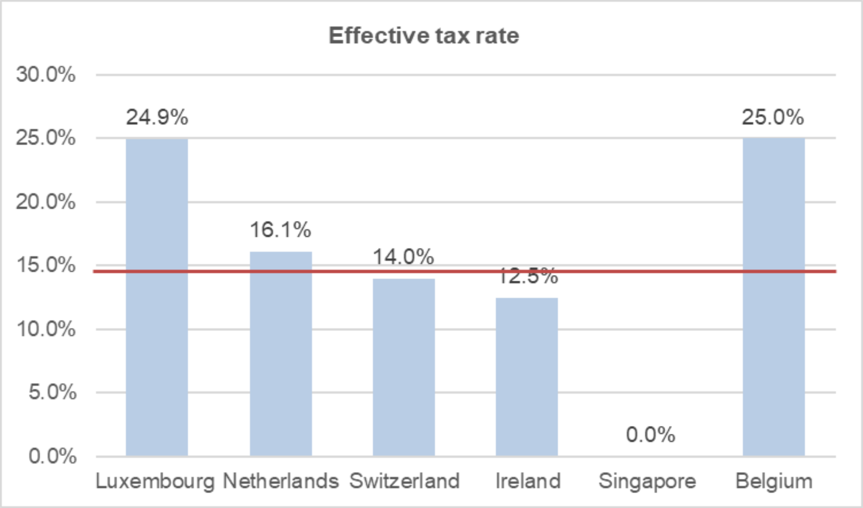
1) **Are there group entities resident in jurisdictions with an ETR < 15% based on CbCR?**
   - NB: Pillar Two ETR computation ≠ CbCR ETR → this is **high level check only!**

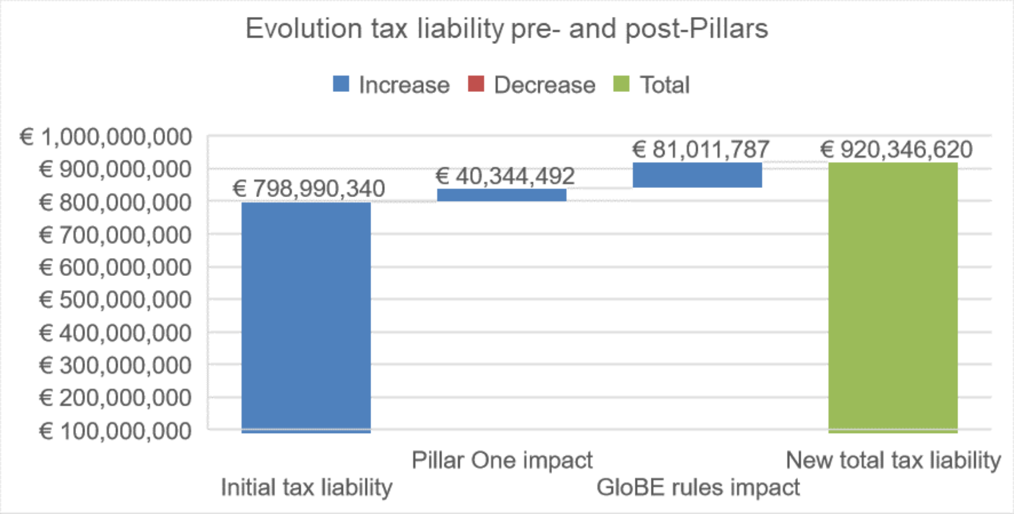
| | CbCR data | | | | | |
|---|---|---|---|---|---|---|
| **Tax Jurisdiction** | **Profit (Loss) Before Income Tax** | **Income Tax Accrued – Current Year** | **Pillar One impact on tax base** | **Pillar One impact on tax liability** | **ETR** | **GloBE Top-up taxation (high-level expected amount)** |
| Luxembourg | € -6,000 | € - | € 67,498,500 | € 16,832,630 | 24.9% | € - |
| Netherlands | € 1,875,000,000 | € 279,000,000 | € -202,495,500 | € -9,224,910 | 16.1% | € - |
| Switzerland | € 2,999,931,000 | € 419,990,340 | € -67,498,500 | € -9,449,790 | 14.0% | € 29,324,325 |
| Ireland | € 800,000,000 | € 100,000,000 | € 67,498,500 | € 8,437,313 | 12.5% | € 21,687,463 |
| Singapore | € 200,000,000 | € - | € - | € - | 0.0% | € 30,000,000 |
| Belgium | € - | € - | € 134,997,000 | € 33,749,250 | 25.0% | € - |
| **TOTAL** | € 5,874,925,000 | **€ 798,990,340** | € 6,673,915,340 | **€ 40,344,492** | | **€ 81,011,787** |
| | | | | | | **€ 920,346,620** |

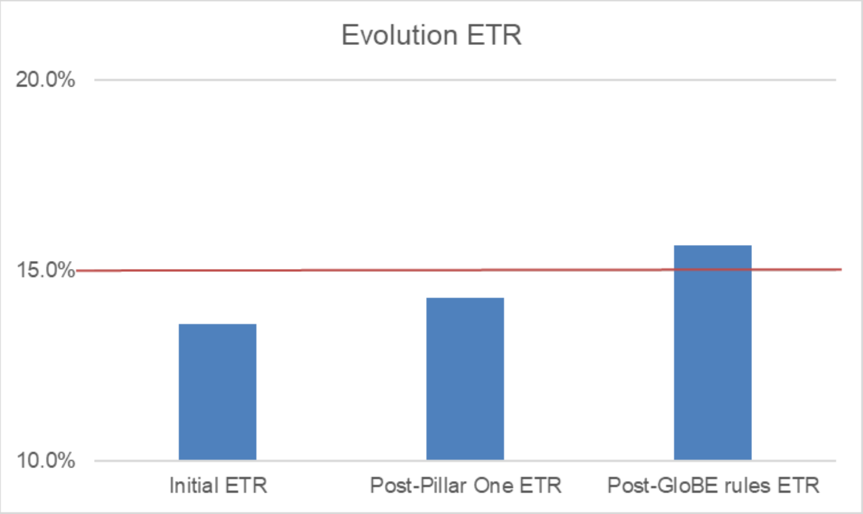
## Preliminary high-level impact assessment

2) **Is your head office jurisdiction's ETR at least 15% and is it committed to Pillar Two?**

- Relevant to estimate whether "simple" IIR vs. more complex UTPR top-up taxation is more likely
- In the example: Luxembourg is committed and has a sufficient ETR



# **Pillar Two** – Case study

## Preliminary high-level impact assessment

**3) Do you have intragroup interest or royalty payments to low-taxed entities (nominal minimum rate of [7.5%-9%])?**

- **Nominal** rate, not ETR!
- In the example below: 70% royalty exemption under Dutch IP regime + unremitted interest income in Singapore untaxed

| Tax Jurisdiction | Related party revenue | Type of income | Tax rate | Risk that the rule applies | Top-up WHT if STTR applied |
|---|---|---|---|---|---|
| Luxembourg | € 50,000 | Dividends | 25% | | € - |
| Netherlands | € 3,500,000,000 | Royalties | 9% | | € - |
| | € 1,500,000,000 | Royalties | 25% | | € - |
| Switzerland | € 20,000 | Dividends | 14% | | € - |
| Ireland | € 10,000,000,000 | Sales | 13% | | € - |
| Singapore | € 2,000,000,000 | Interest | 0% | | € 180,000,000 |
| Belgium | € - | | 25% | | € - |

# Pillar Two – Case study

## Preliminary high-level impact assessment

| | CbCR data | | | | | | |
|---|---|---|---|---|---|---|---|
| **Tax Jurisdiction** | **Profit (Loss) Before Income Tax** | **Income Tax Accrued – Current Year** | **Pillar One impact on tax base** | **Pillar One impact on tax liability** | **STTR impact** | **Effective tax rate** | **GloBE Top-up taxation (high-level expected amount)** |
| Luxembourg | € -6,000 | € - | € 67,498,500 | € 16,832,630 | € - | 24.9% | € - |
| Netherlands | € 1,875,000,000 | € 279,000,000 | € -202,495,500 | € -9,224,910 | € - | 16.1% | € - |
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| Singapore | € 200,000,000 | € - | € - | € - | € 180,000,000 | 90.0% | € - |
| Belgium | € - | € - | € 134,997,000 | € 33,749,250 | € - | 25.0% | € - |
| **TOTAL** | € 5,874,925,000 | **€ 798,990,340** | € 6,673,915,340 | **€ 40,344,492** | **€ 180,000,000** | | **€ 51,011,787** |
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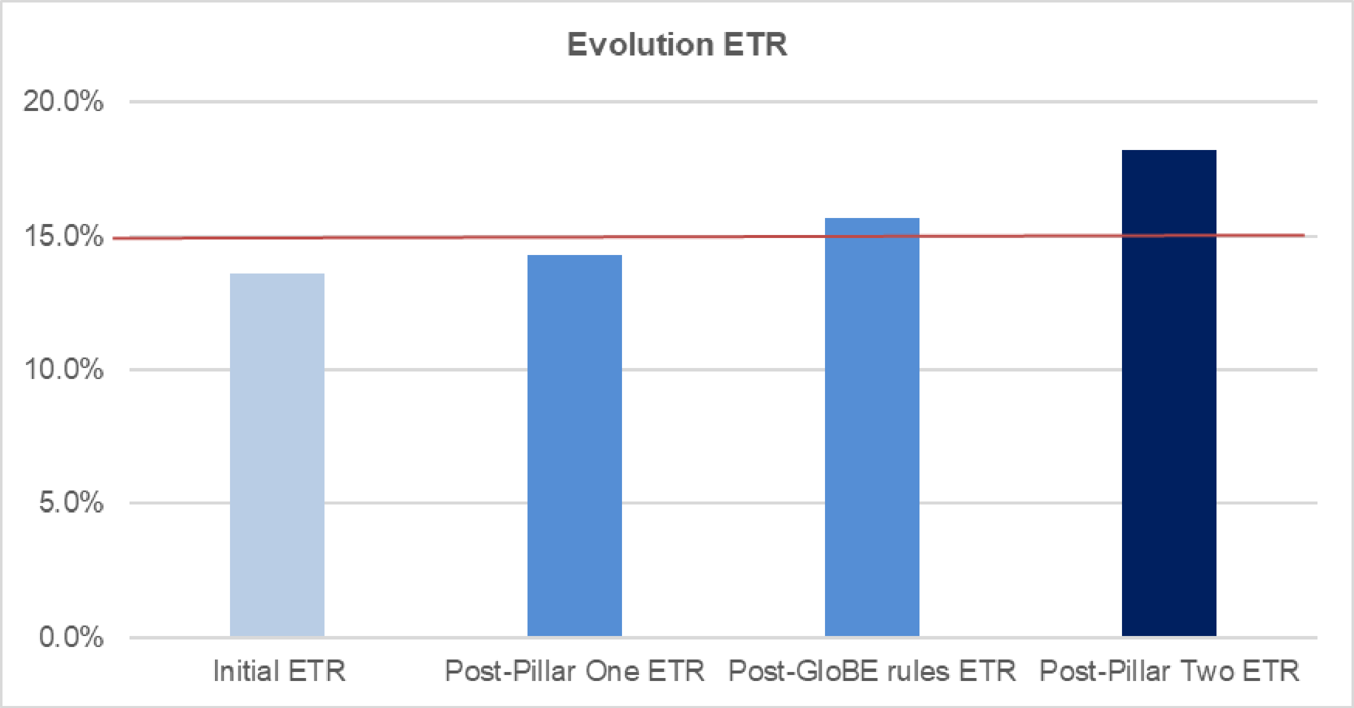
# **Pillar Two** – Case study

## Preliminary high-level impact assessment



# 4 Next steps

# EU implementation

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## Pillar One & Pillar Two implementation

Cyprus/Ireland/Estonia/Hungary: still no commitment

→ Could block EU Directives (veto-right)

→ Enhanced cooperation possible?

→ Pillar 2: top-up tax could be a problem under EU law

## Digital Levy(?)

'Will be designed in such a way that it is **independent** of the forthcoming global agreement on the international tax reform'

→ Corporate income tax top-up to be applied to all companies conducting certain digital activities in the EU?

→ Tax on digital transactions?

# Next steps

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**9-10 July 2021**

G20 meeting of finance ministers endorsed political consensus

**20 July 2021**

EU Digital Levy proposal? Postponed

**October 2021**

Target date for technical agreement

**Q4 2021 / Q1 2022**

EU directive likely

**1 January 2023**

Target date for entry into force of taxing right on Amount A (Pillar One) and at least Income Inclusion Rule (Pillar Two)

# 5 Closing remarks

# What you can do to prepare?

## Actions & Discussion Items: Pillar One

- Check in which market jurisdictions the group earn(s) revenue > € 1m where goods or services are used or consumed
- Monitor final compromise – thresholds of € 20bn global turnover and profitability in excess of 10% are, however, unlikely to further evolve
- Assess preferred filing jurisdiction
- Review marketing / distribution business models and business segmentation and consider adjusting return of "routine" marketing / distribution functions
- Model the impact (high-level now; refined towards year-end further to final compromise) & set up compliance processes

# What you can do to prepare?

## Actions & Discussion Items: Pillar Two

Check in which jurisdictions the group has an ETR below 15% (initially, high-level based on CbCR) and which jurisdictions have a nominal rate <9%

Monitor final compromise – simplification measures and carve-outs are still being negotiated

- Substance-based carve-out and impact on OECD BEPS Action 5 regimes are attention points

Assess reaction of your headquarter jurisdiction

Model the impact (amount and location of top-up taxation) & set up compliance processes

Medium-term / longer-term questions and opportunities

- Maintain presence in certain low-/no-tax jurisdictions? Concentrate certain activities?
- Planning to get as close as possible to 15% ETR globally

# Have a question? Want to learn more? Get in touch!


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