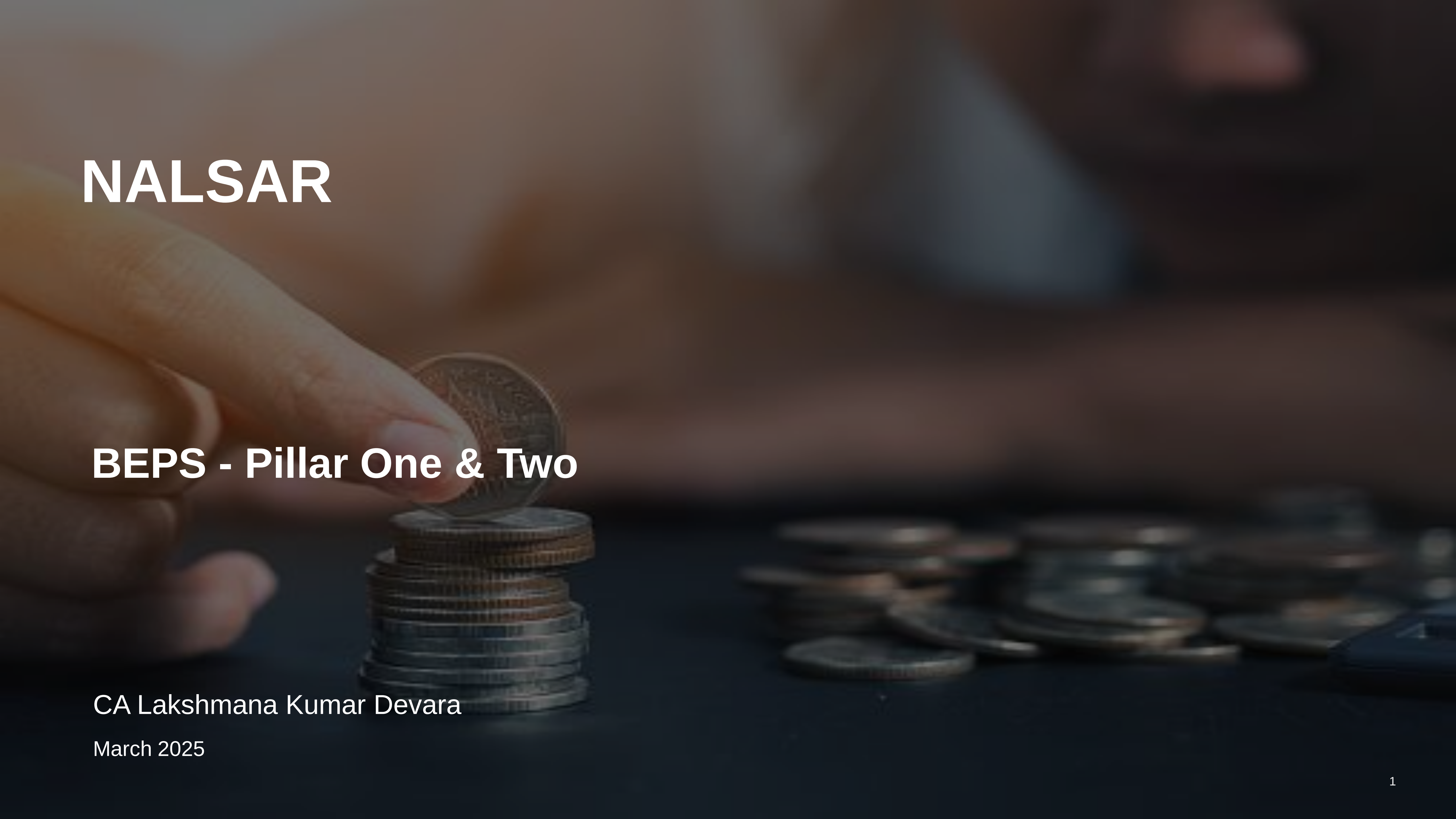

NALSAR

BEPS - Pillar One & Two

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March 2025

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Section

1

Background of BEPS

OECD BEPS - In a nutshell

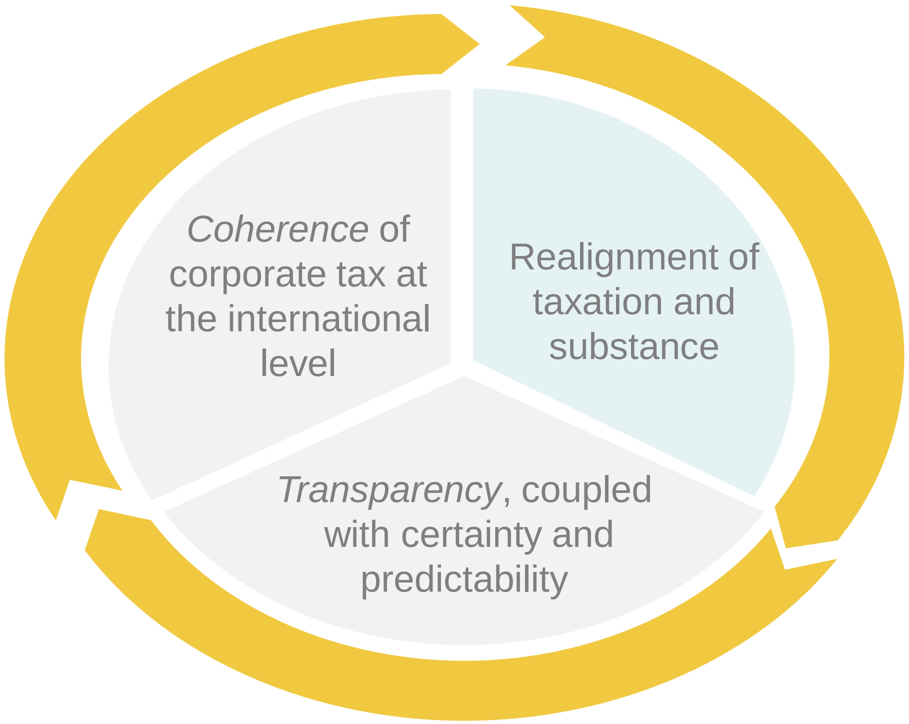
On 19 July 2013 the OECD released an Action Plan on BEPS which was presented to the meeting of G20 Finance Ministers in Moscow

The purpose of the Action Plan is “to prevent double non-taxation, as well as cases of no or low taxation associated with practices that artificially segregate taxable income from activities that generate it.”

The report indicates that “no or low taxation is not per se a cause for concern, but it becomes so when it is associated with practices that artificially segregate taxable income from the activities that generate it.”

The Action Plan covered 15 specific Actions which were broadly to be achieved within a two year time frame (i.e. by the end of 2015). On 5 October 2015, OECD released its final set of recommendations on all the 15 Action Points

15 Actions organized around *three* main pillars

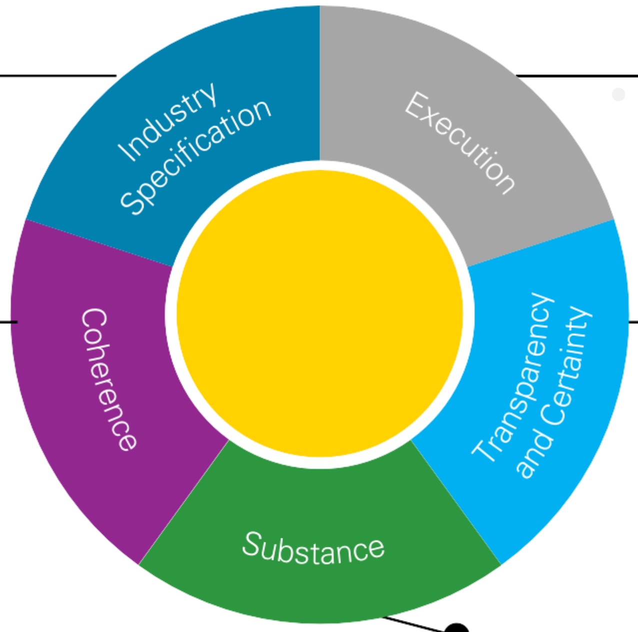


BEPS 1.0

- Action 1 : Address the tax challenges of the digital economy

- Action 15: Development of a multilateral instrument for amending bilateral treaties

- Action 2: Neutralise the effects of hybrid mismatch arrangements
- Action 3: Strengthen CFC rules
- Action 4: Limit base erosion via interest deductions and other financial payments
- Action 5: Counter harmful tax practices more effectively, taking into account transparency and substance



- Action 11: Establish methodologies to collect and analyse data on BEPS and actions addressing it
- Action 12: require taxpayers to disclose their aggressive tax planning arrangements
- Action 13: Re-examine transfer pricing documentation
- Action 14: Making dispute resolutions more effective

- Action 6: Prevent treaty abuse
- Action 7: Prevent the artificial avoidance of permanent establishment status
- Action 8: Consider transfer pricing for intangibles
- Action 9: Consider transfer pricing for risks and capital
- Action 10: Consider transfer pricing for other high-risk transactions

BEPS 1.0 (Action Points covered under MLI 1.0)

Hybrid Mismatches (Action 2)

Treaty Abuse (Action 6)

Artificial Avoidance of PE (Action 7)

Dispute resolution (Action 14)

Minimum standard (some components)

BEPS 2.0

08 Oct 2021

- The OECD & G20 Inclusive Framework (IF)* released an updated statement setting forth key components for an agreement on a two-pillar solution developed as a part of BEPS 2.0 Project.

Pillar One

Re-allocates taxing rights on residual profits to market jurisdictions

Aim: To achieve a fairer distribution of profits and taxing rights among jurisdictions with respect to the largest MNEs

Pillar Two

Provides jurisdictions with a right to impose "top up" tax, where other jurisdictions do not tax income or subject an income to low tax

- Global Anti-Base Erosion ("GloBE") Rules
  - Income Inclusion Rule ("IIR")
  - Undertaxed Profits Rule ("UTPR")
- Treaty based rule: Subject to tax rule ("STTR")

Aim: To limit tax competition by ensuring that MNEs pay a minimum level of tax in each jurisdiction that they operate

* The G20 includes the European Union and 19 individual countries: Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, South Korea, Mexico, Russia, Saudi Arabia, South Africa, Turkey, the United Kingdom, and the United States.

Section

2

Pillar One - Amount A & Amount B

Pillar One

- Allocation of profits to market jurisdictions irrespective of any physical presence in those jurisdictions. Amount to be taxed in the market jurisdictions = **Amount A + Amount B.**
- **Amount A** - Profits to be allocated to market jurisdictions.

  For in-scope MNEs (that derives at least 1 million euros in revenue from that jurisdiction), 25% of residual profit (defined as profit in excess of 10% of revenue) will be allocated to market jurisdictions with nexus using a revenue-based allocation key.

  The excess profits allocated to a market jurisdiction are capped when the market jurisdiction already taxes those profits. This adjustment is referred to as the Marketing and Distribution Safe Harbour Adjustment (MDSH). The MDSH operates generally as a multi-step calculation that identifies the excess profits with reference to a minimum level of profit calculated as the greater of a local jurisdiction RODP based on in-scope MNEs RODP or 3% of the revenue sourced to market jurisdiction.

- **Amount B** - Remuneration for baseline marketing and distribution activities.

  The development of standard remuneration for in-county “baseline” marketing and distribution activities has been deferred pending further technical work.

Note: Determination of Tax base - The relevant measure of profit or loss of the in-scope MNE will be determined by reference to financial accounting income, with a small number of adjustments. Losses will be carried forward.

Pillar One - Amount A - Overview of Process Map

Pillar One -
nount A - Face she

Step 1.
Scope determination

Step 2.
Nexus & revenue sourcing

Step 3.
Tax base determination

Step 4.
Allocation of Amount A

Step 5.
Elimination of double taxation

Pillar One - (Amount A - MLI 2.0 and its construct)

11 Oct 2023

#	Reference	Scope	Relevant Annexures	Remarks
1	Part 1 (Article 1)	Application and Personal Scope	-	
2	Part II (Article 2&3)	General Definitions and Covered Group	Annex B & C	What is a Covered Group ?
3	Part III (Article 4 to 8)	Allocation and Taxation of Profits	Annex D	How does the profit and tax allocation happens ?
4	Part IV (Article 9 to 13)	Elimination of Double Taxation	-	
5	Part V (Article 14 to 37)	Administration and Certainty	Annex E,F & G	
6	Part VI (Article 38 to 40)	Treatment of Specific Measures Enacted by Parties	Annex A & H	Impact on measures already enacted by countries?
7	Part VII (Article 41 to 53)	Final Provisions		

MLI - for Amount A

Pillar One - Amount A

- **Article 3 - Covered Group**

  A Group is in scope of Amount A if for the Period it has Adjusted Revenues greater than €20 Billion and a pretax profit margin greater than 10%.

  If in the two preceding Periods before the Period, the Group was not a Covered Group (i.e., it did not satisfy the revenue and profit before tax criteria), it will not be considered a Covered Group for the Period unless it satisfies the following additional criteria.

  (i) Prior Period Test - the Group has a pretax profit margin greater than 10% in at least two out of the four Periods immediately preceding the Period; and

  (ii) Average Test - the average of the pretax profit margin for the five-year Period ending with the Period is greater than 10%.

- **Article 2 - Adjusted Revenue (Part of General Definitions)**

  Adjusted Revenues" means the revenues, exclusive of value added taxes, goods and services taxes, sales taxes, or other similar taxes on consumption, that are reported in the Consolidated Financial Statements of a Group for a Period (or that would have been so reported if the Ultimate Parent Entity prepared Consolidated Financial Statements), modified to.

  include the Group's share of revenue derived from a Joint Operation or a Joint Venture, in the same proportion as the Group's share of profit or loss derived from the Joint Operation or the Joint Venture. No adjustment shall be made if the Joint Venture is the Ultimate Parent Entity of another Covered Group in the Period;

Pillar One - Amount A

- **Article 2 - Amount A Profit (Part of General Definitions)**

  “Amount A Profit” means the amount determined for a Covered Group for a Period by:

  subtracting 10 per cent of the Adjusted Revenues of the Covered Group for the Period from the Adjusted Profit Before Tax of the Covered Group for the Period; and

  multiplying the amount calculated in subdivision (i) by 25 per cent;

- **Article 5 - Allocation of Profits to the Market Jurisdiction**

  Profit allocation to a Jurisdiction in which a Covered Group has a nexus shall be determined by:

  Amount A Profit X Adjusted Revenue from Source Jurisdiction / Adjusted Revenue of the Covered Group

  If the Profits from the Source jurisdiction is > €50 Million, then subtract Marketing and Distribution profits Safe Harbour adjustment (MDSH) from sub-paragraph (a)

Where the market jurisdictions already have existing taxing rights over the Covered Group’s residual profits, should not receive a second taxing right of the Covered Group's residual profits

Pillar One - Amount A

- **Article 5 - Allocation of Profits to Market jurisdiction**

MDSH Shall be the lower of :

✓ Profits allocated to the Jurisdiction under (a) above; and

✓ the <u>jurisdictional offsetting profits</u> of the Covered Group in the Jurisdiction;

Adjusted jurisdictional excess profits X Jurisdictional offset percentage

Normal level of profit
- Local Jurisdictions RODP based on in-scope MNE's RODP; or
- 3% of Revenue of Market jurisdiction

Adjusted elimination profit (or loss) for the Covered Group in the Jurisdiction for the Period*

<u>Less</u>: Higher of:

(a) Jurisdictional Depreciation and Payroll [X] Elimination Threshold RODP* or

(b) 3% of Adjusted revenues of the Jurisdiction

- 90% (low depreciation and payroll jurisdiction)
- 25% (lower income jurisdiction)
- 35% (Other income cases)

Note:
1. Elimination Profit (or Loss) of a Covered Group for a Period in a Jurisdiction is the sum of the entity elimination profit (or loss) of each Group Entity located in that Jurisdiction and the taxable presence elimination profit (or loss) of each Taxable Presence located in that Jurisdiction for the Period, reduced by the relevant elimination net losses in that Jurisdiction
2. *Elimination Threshold RODP of a Covered Group* = Covered Group's Adjusted Revenues for the Period X 10% / Accounting depreciation and Accounting payroll of the Covered Group

Pillar One - Amount A

- **Article 7 - Sourcing Principles**

  Categorise group revenue & identify applicable source rule viz.,:

  ✓ Category - Finished goods; Source rule - Place of delivery to final customer

  ✓ Category - Online advertising; Source rule - Location of viewers

- **Article 8 - Nexus**

  A Covered Group shall be treated as having nexus in a Jurisdiction for a Period if it derives revenue in that Jurisdiction

  ✓ EUR 1 million; or

  ✓ in the case of a Jurisdiction with a Gross Domestic Product of less than EUR 40 billion with respect to the Period, EUR 250 000.

- **Article 9 - Relief for Amount A Taxation**

  The fundamental design objectives of Amount A under Pillar One which, unlike Pillar Two, is not primarily designed to give rise to new tax revenues, but rather to seek to reallocate the residual profits of Covered Groups to certain qualifying jurisdictions.

  Therefore, while certain market jurisdictions are expected to gain tax revenues, Relieving Jurisdictions will be obliged to provide relief for Amount A taxation.

  Concept of Specified jurisdiction and Relieving jurisdiction are defined in Article 11.

Pillar One - Amount A (Illustration on allocation and taxation of profits)

Particulars	Reference	Amount (in Euro Billion)	Percentage (%)	Details
Adjusted Revenue of the Covered Group	A	80		
Profit Before Tax	B	15	18.75%	PBT is in excess of 10%
Routine Profits (10% Threshold for applying Pillar 1)	C=A*10%	8	10%	
Excess Profits	D = C-B	7	8.75%	
Amount A Profit = Excess profits *25%	C*25%	1.75		

	Country X	Country Y	Country Z	Total
Revenue from each country	50	20	10	80
Allocation of share of Residual Profits (or) Excess Profits	1.09	0.44	0.22	1.75

Pillar One - Amount B

Further work on the interdependence of Amount B and Amount A under Pillar One will be undertaken prior to the signing and entry into force of the Multilateral Convention.

19 Feb 2024

- OECD/G20 Inclusive Framework (IF) on BEPS released the report on Amount B of Pillar One providing a simplified and streamlined approach to the application of the arm's length principle to Baseline marketing and distribution activities, with a particular focus on the needs of low-capacity countries

Salient features:

- Unlike other BEPS 2.0 measures, Pillar One Amount B is not subject to a revenue threshold and can be applicable to many multinational businesses.
- The Report is incorporated into the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations 2022 (OECD TP Guidelines).
- OECD will publish a list of the jurisdictions that choose to apply Amount B. Amount B will be treated as providing an arm's-length outcome only in jurisdictions that choose to apply the approach. Jurisdictions that choose to apply Amount B, can do so in any of the following ways:
  - ✓ Taxpayer safe harbour: Tested parties resident in the jurisdiction have the option to elect to apply Amount B where they have transactions that meet the scope criteria.
  - ✓ Mandatory: Tested parties and the tax administrations are required to apply Amount B where transactions meet the scope criteria.

Amount B may not be respected or relied upon in counterparty jurisdictions that choose not to adopt Amount B . Thus, a Group could be required to prepare a benchmarking analysis for Jurisdiction X, apply Amount B in Jurisdiction Y and if this results in double taxation, to the extent its available, rely on a MAP to eliminate double taxation.

Pillar One - Amount B

Transactions in scope (wholesale distribution) Refer Note 1 & 2:

(a) Buy-sell marketing and distribution transactions

(b) Sales agency and commissionaire transactions

TP Method suggested:

(a) TNMM with Return on Sales (RoS) as Profit Level Indicator (PLI); or

(b) CUP method on exception basis

TP Margins suggested:

a) Based on Industry Grouping & Other factors.

b) Margin ranges from 1.50% to 5.50%

Elimination of Double taxation: **Refer Note 3:**

Report acknowledges Double taxation upon application of simplified and streamlined approach by one jurisdiction and suggests MAP as a solution.

Notes:

1. Distribution of non-tangible goods and services and marketing, trading, or distribution of commodities are excluded from the scope of Amount B.
2. Also, the tested party should not
    - Make any unique and valuable contributions, should not assume economically significant risks etc.
    - Must not incur annual operating expenses lower than 3% or greater than 20-30% of the tested party's annual net revenues. [Operating expenses refers to total costs excluding cost of goods sold]
3. In a MAP or resulting arbitration procedure, when one or more of the jurisdictions have not elected to apply or accept Amount B, they must justify their positions on the appropriate corresponding adjustments using the remaining provisions of the OECD TP Guidelines and not the Amount B approach.

Section

3

Pillar Two (GloBE Rules)

Pillar Two - Documents Issued by OECD & Timelines

Dec 2021

Pillar Two Model Rules

Mar 2022

- Commentary or Explanatory statement

Dec 2022

- Safe Harbour and Penalty Relief
- GloBE Information Return Consultation Document

Feb & July 2023

- First Admin Guidance &
- Second Admin Guidance

Sep 2023

- Convention for implementing STTR
- Explanatory statement

Dec 2023

Third Admin Guidance

Apr 2024

- Updated Commentary to the Model GloBE Rules
- Examples (updated)

Jun 2024

- Fourth Admin Guidance

Jan 2025

- Fifth Admin Guidance
- GloBE Information Return

Source: https://www.oecd.org/en/topics/sub-issues/global-minimum-tax/global-anti-base-erosion-model-rules-pillar-two.html

Pillar Two - An overview

14 Dec 2021

- Pillar Two: Global Anti-Base Erosion Rules ('GloBE Rules')

  Taxpayers that either have no foreign presence or that have less than EUR 750 million in consolidated revenues are not in scope of the Model Rules. Also, do not apply to government entities, international organisations and non-profit organisations, pension, investment or real estate funds

  Taxpayers in scope of the rules calculate their effective tax rate for each jurisdiction where they operate, and pay top-up tax for the difference between their effective tax rate per jurisdiction and the 15% minimum rate. Any resulting top-up tax is generally charged in the jurisdiction of the ultimate parent of the MNE. A de-minimis exclusion applies where there is a relatively small amount of revenue and income in a jurisdiction.

  The Pillar Two Model Rules also contemplate the possibility that jurisdictions introduce their own domestic minimum top-up tax based on the GloBE mechanics, which is then fully creditable against any liability under GloBE, thereby preserving a jurisdiction's primary right of taxation over its own income.

  Though more than 140 countries have announced their intent to adopt Pillar 2.0, their timelines for implementation vary

Pillar Two - An overview

14 Dec 2021

- Scope of Pillar Two: Global Anti-Base Erosion Rules ('GloBE Rules')

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.

Two out of four Fiscal Years

- The current Fiscal Year is excluded from the Four Year calculation

Consolidated revenue of the Group

- Intra-group transactions are excluded from consolidated revenue

Excluded entities

- Government bodies and international organizations
- Non-profits
- Investment entities owned by ≥ 95% by excluded entities

Recently created MNEs - where only last two year data is available ?

Fiscal period < 12 months ?

Pillar Two - An overview

- Mechanics of IIR, UTPR and DTT

Aim

- To limit tax competition by ensuring that MNEs pay a minimum level of tax in each jurisdiction that they operate in by
  - providing a co-ordinated system of taxation
  - imposing a top-up tax on profits arising in a jurisdiction **whenever the effective tax rate (**determined on a jurisdictional basis) is **below the minimum rate of 15%**

How

- Provides jurisdictions with a right to **impose top-up tax**, where other jurisdictions do not tax income or subject income to low tax

Rules employed

1. **Global Anti-Base Erosion (“GloBE”) Rules**:
   - Income Inclusion Rule (“IIR”)
   - Undertaxed Profits Rule (“UTPR”)
2. **Treaty based rule**
   - Subject to Tax Rule (“STTR”)

Pillar Two Model Rules also contemplate the possibility that jurisdictions introduce their own domestic minimum top-up tax (DTT) based on the GloBE mechanics, which is then fully creditable against any liability under GloBE, thereby preserving a jurisdiction’s primary right of taxation over its own income.

Pillar Two - An overview

UTPR can also be applied by the jurisdiction of the payer. UTPR gives governments the power to deny deductions (for payments to group companies or third parties on items viz., depreciation, interest etc.) **or** <u>take similar actions to collect taxes that otherwise would not be collected under the IIR</u>.

Domestic Laws

Rule 1 (IIR)

- Inclusion of the income of a low-taxed constituent entity (CE) in the tax base of the Ultimate Parent Entity (UPE) or Intermediary Parent Entity (IPE) if that income is not taxed at the minimum 15% ETR.
- Country-by-Country basis

Rule 2 (UTPR)

- Secondary rule, applied as backstop in case IIR could not be applied by UPE or IPE. Payable by entities which adopt UTPR
- Top-up Tax is allocated to countries with constituent entities based on tangible assets/employees

Rule 3 (DMT)

- DMT gives countries the option of collecting and keeping any top-up taxes that would otherwise flow overseas.
- Applies before IIR and UTPR; and fully creditable against the GloBE top-up taxes (i.e., IIR and UTPR)

Treaty based

Rule 4 (STTR)

- Treaty based rule, allows countries to impose source taxation on covered related party payments (viz interest, royalties, services) that are otherwise fully or partially exempt under a tax treaty to bring the total tax cost up to 9%.
- Applies on standalone basis before GloBE Rules. Can be off-set against the GloBE top-up taxes

Pillar Two - Flow chart

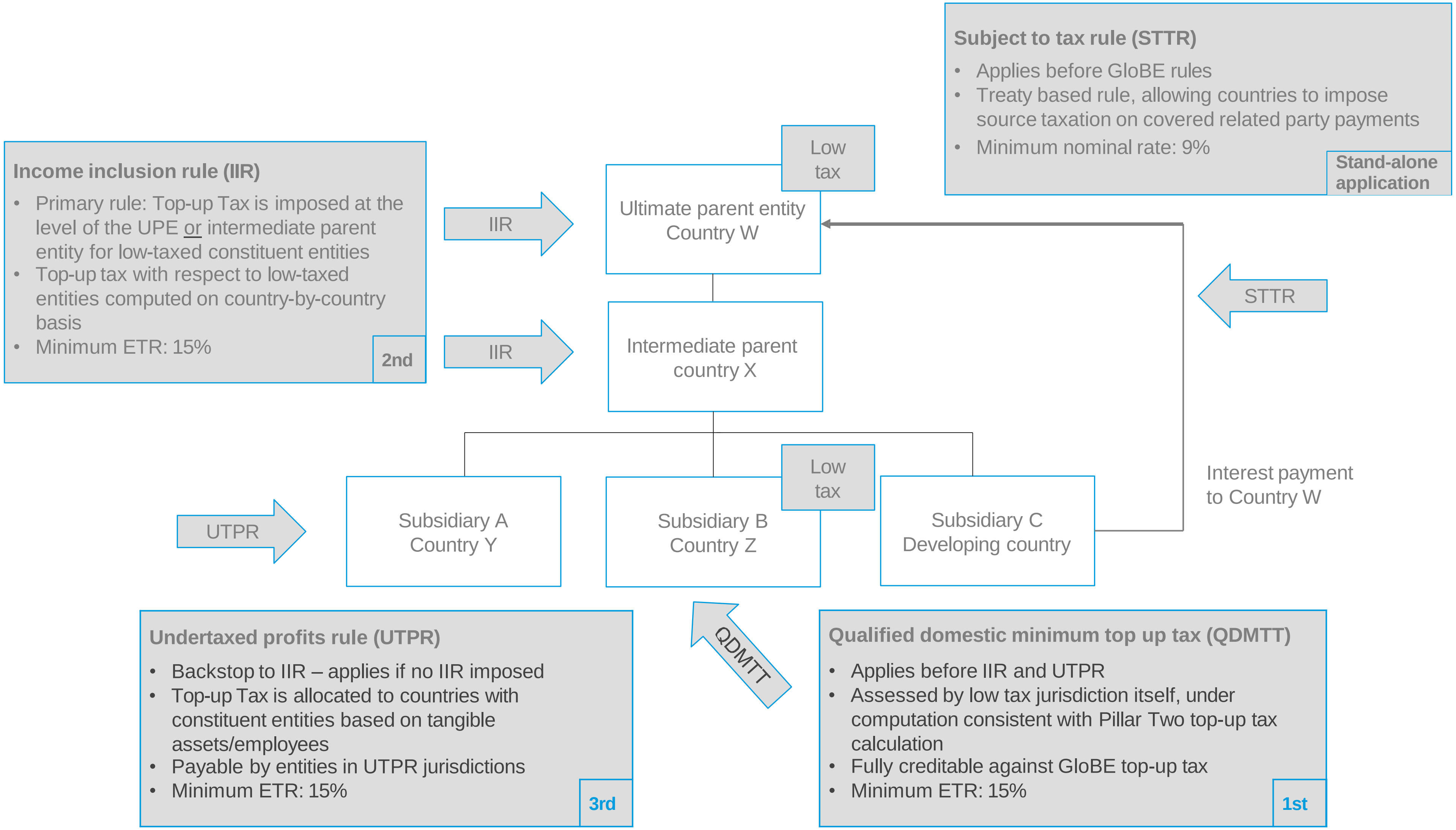


Image source: RSM June 2023 ITAX FORUM

Pillar Two - Definitions

Ultimate Parent Entity:

- (a) an Entity that:
  - ✓ i. owns directly or indirectly a Controlling Interest in any other Entity; and
  - ✓ ii. is not owned, with a Controlling Interest, directly or indirectly by another Entity; or
- (b) the Main Entity of a Group that is within Article 1.2.3.

Constituent Entity:

- (a) any Entity that is included in a Group; and
- (b) any Permanent Establishment of a Main Entity that is within paragraph (a).

POPE:

- POPE is a CE (other than UPE) of an MNE group that owns an ownership interest in another CE of the MNE group **and** has more than 20% of its profits owned (directly/indirectly) by individuals/entities outside the MNE group.
- When a POPE exists in the ownership chain of an LTCE, POPE jurisdiction has the primary right to tax, even before the UPE jurisdiction and the parent entities above it shall adjust their share of additional taxes based on what the POPE pays.
- If a POPE has control over another entity, it is also considered a POPE. If the lower POPE is a 100% subsidiary of the higher POPE, the higher POPE's jurisdiction enjoys the taxing rights. Otherwise, the lower POPE's jurisdiction has the main taxing right, and credits are given to the higher POPE's jurisdiction based on their respective ownership shares.

Pillar Two - Mechanics of GloBE 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 applicable to income of each Constituent Entity

Step 4 - Effective Tax Rate & Top-up Taxes

- Calculate the ETR 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

Key notes:

1. Top-up Tax is imposed on **excess profits*** in a jurisdiction to the extent the ETR of the jurisdiction is below 15%

2. **Excess profits in a jurisdiction**
   = Net GloBE Income for the jurisdiction - Substance-Based Income Exclusion ("SBIE") for the jurisdiction

Source: OECD's fact sheets on "Overview of the Key Operating Provisions of the GloBE Rules"

Pillar Two - Overview of QDMTT

Jurisdictional ETR

- ETR calculation for each jurisdiction. This is done by aggregating the adjusted covered taxes of all CEs in a jurisdiction and dividing it by the aggregate GloBE Income of all CEs in that jurisdiction. Some exceptions viz.,
  - ✓ Minority-owned CEs (MOCEs)
  - ✓ JVs and JV subsidiaries, which are together considered as separate JV MNEs

Aggregate of adjusted covered taxes of all CEs in a jurisdiction ÷ Aggregate GloBE Income of all CEs in that jurisdiction

Pillar Two - Overview of QDMTT

1. Computational adjustments for computing the 'GloBE income' of a Low Tax Constituent Entity (LTCE)

- Computation of GloBE income/loss is driven by Article 3 of the model GloBE Rules
- Starting point is the Financial Accounting Net Income / Loss followed by the below adjustments:
  - ✓ Adjustments as per Art. 3.2.1
  - ✓ One adjustment as per Administrative Guidance 2.4.
  - ✓ Adjustments as per Art. 3.2.2 to 3.2.11.
  - ✓ Exclusion of shipping income and allocation of income of PEs and flow-through entities.
- The objective of these adjustments is to align the financial accounting income with tax income so that the ETR reflects uniformity.
- Also, Refer Annexure 1

2. Computational adjustments for computing the 'Adjusted covered taxes' of a LTCE

- Calculation of adjusted covered taxes is driven by Article 4 of the model GloBE Rules
- Starting point is the current tax expenses recorded in financial statements followed by the below adjustments:
  - ✓ Additions as per Art. 4.1.2.
  - ✓ Reductions as per Art. 4.1.3.
  - ✓ Allocation of covered taxes from one CE to another as per Art. 4.3.
  - ✓ Net deferred tax adjustment as per Art. 4.4.
  - ✓ GloBE Loss Election for GloBE Loss Deferred Tax Asset under Art. 4.5.
- The objective of these adjustments is to take only those taxes into ETR computation which pertain to income included in GloBE computation so that a meaningful comparison can be made.

Pillar Two - Overview of QDMTT

Substance-Based Income Exclusion ("SBIE")

- SBIE reduces profit subject to top-up tax, based on payroll and carrying value of tangible assets.
- Payroll and tangible assets are indicators of substantive activities and the rules acknowledge that the income generated from these physical factors is unlikely to result from profit shifting.

1. Payroll carve-out

- 5% of payroll costs of eligible employees
- Transitional relief: 9.8% for FY beginning in 2024 reduced each year until 5% in 2033

2. Tangible assets carve-out

- 5% of carrying value of eligible tangible assets
- Transitional relief: 7.8% for FY beginning in 2024 reduced each year until 5% in 2033

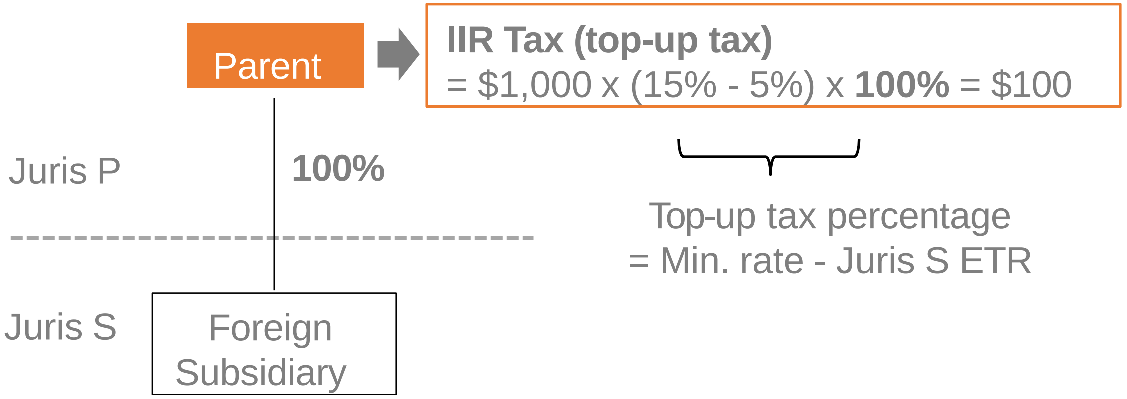
Pillar Two - Illustration for computing QDMTT

Particulars	Reference	S Co1	S Co2	S Co3
Income computed as per Globe Rules	A	2000	1000	1000
Covered Taxes at respective jurisdictions	B	100	250	200
Jurisdiction level ETR	C=B/A	5%	25%	20%
Top-up tax percentage	D = 15%-C	10%	0%	0%
Tangle Assets & Payroll	E	5000	-	-
Substance based carve out	F=E*5%	250	-	-
Excess profits	G=A-F	1750	-	-
Top-up tax	H=G*D	175	-	-

Pillar Two - Overview of IIR

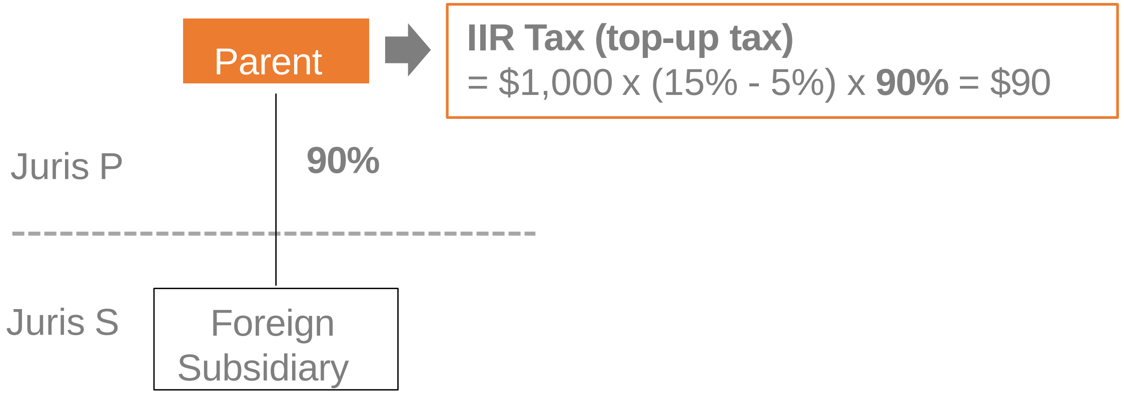
- IIR is applied by the parent jurisdiction on the parent entity. In a multi-tiered holding structure in which parent entities of a low tax subsidiary are located in different jurisdictions, the GloBE model rules will determine which parent jurisdiction applies the IIR.
- The parent entity will pay top-up tax determined based on its share of the low-tax profits of its foreign subsidiaries and branches.

Scenario 1: Parent entity owns 100% of foreign subsidiary



- $1,000 of low-tax profits
- SBIE amount = $0
- ETR = 5%

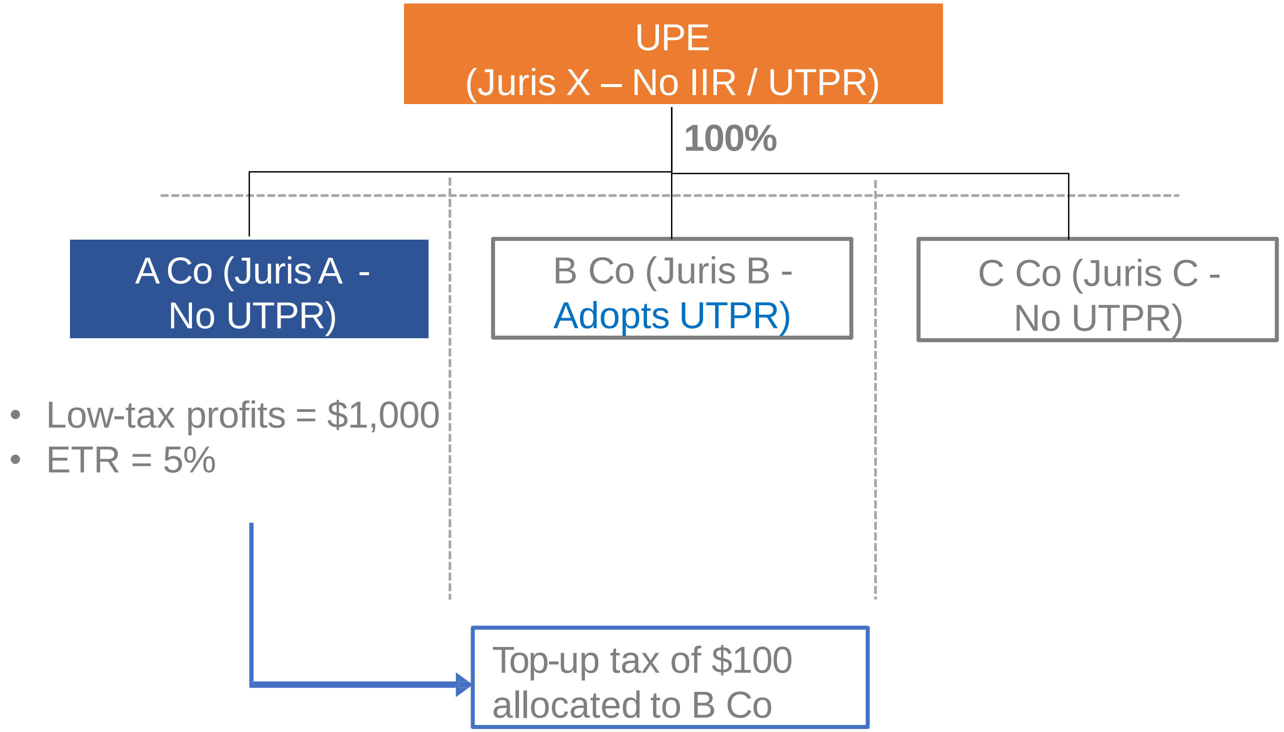
Scenario 2: Parent entity owns 90% of foreign subsidiary



- $1,000 of low-tax profits
- SBIE amount = $0
- ETR = 5%

Pillar Two - Overview of UTPR

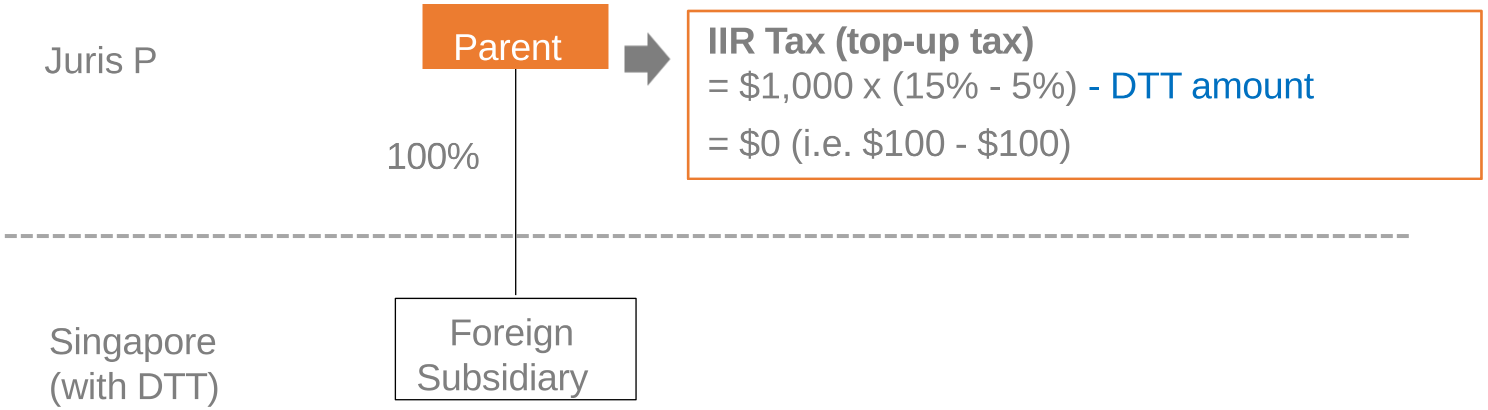
- UTPR serves as a backstop to the IIR. It applies to the extent the top-up tax on the UPE’s share of low- tax profits is not fully collected under the IIR.



A Co has $1,000 of low-tax profits (Assume ETR = 5% and min. rate = 15%)	
Step 1: Compute top-up tax, using the same rules as IIR	Top-up tax = $1,000 x (15% - 5%) = $100 (not collected under IIR)
Step 2: Allocate top-up tax to group entities in each UTPR jurisdiction based on agreed allocation key* * Number of employees and net book values of tangible assets of group entities in each UTPR jurisdiction	**Allocate top-up tax of $100 to B Co.** (Top-up tax is not allocated to UPE, A Co and C Co as UPE Jurisdiction and Jurisdictions A and C do not adopt UTPR.)

Pillar Two - Mechanics of IIR with DTT

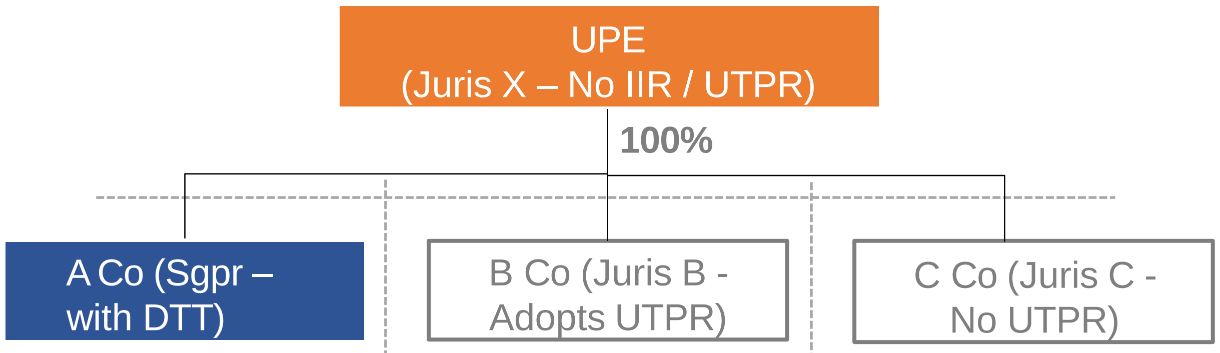
- DTT amount is deducted against IIR top-up tax



- $1,000 of low-tax profits
- SBIE amount = $0
- ETR = 5%
- DTT top-up tax percentage = 10% (i.e. 15% - 5%)
- DTT amount = $100 (i.e. $1,000 x 10%)

Pillar Two - Mechanics of UTPR with DTT

- DTT amount is deducted against UTPR top-up tax

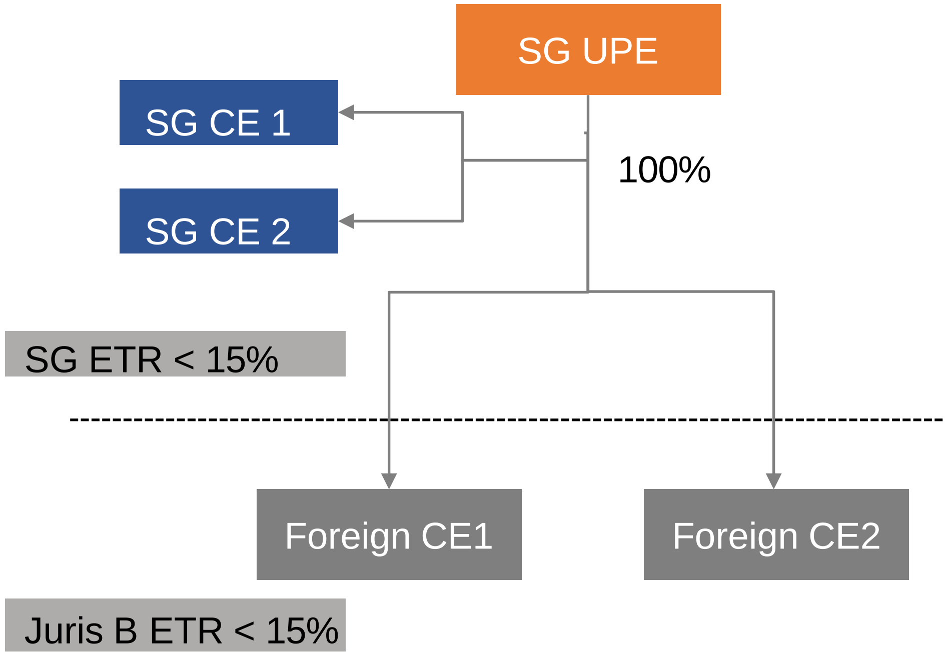


- Low-tax profits = $1,000
- ETR = 5%
- DTT amount = $100
  (i.e. $1,000 x 10%)

A Co has $1,000 of low-tax profits (Assume ETR = 5% and min. rate = 15%) Singapore implements DTT which is a QDMTT	
Compute top- up tax, using the same rules as IIR and deduct the DTT amount	UTPR Top-up tax in Juris B = $1,000 x (15% - 5%) - DTT amount = $0 (i.e. $100 - $100) **No UTPR top-up tax paid in Juris B**

Pillar Two - Impact on MNEs when SG implements IIR and DTT

Singapore implements IIR & DTT
(FY beginning on or after 1 Jan 2025)



Example 1: Foreign CEs are held directly by SG UPE

FY 2024

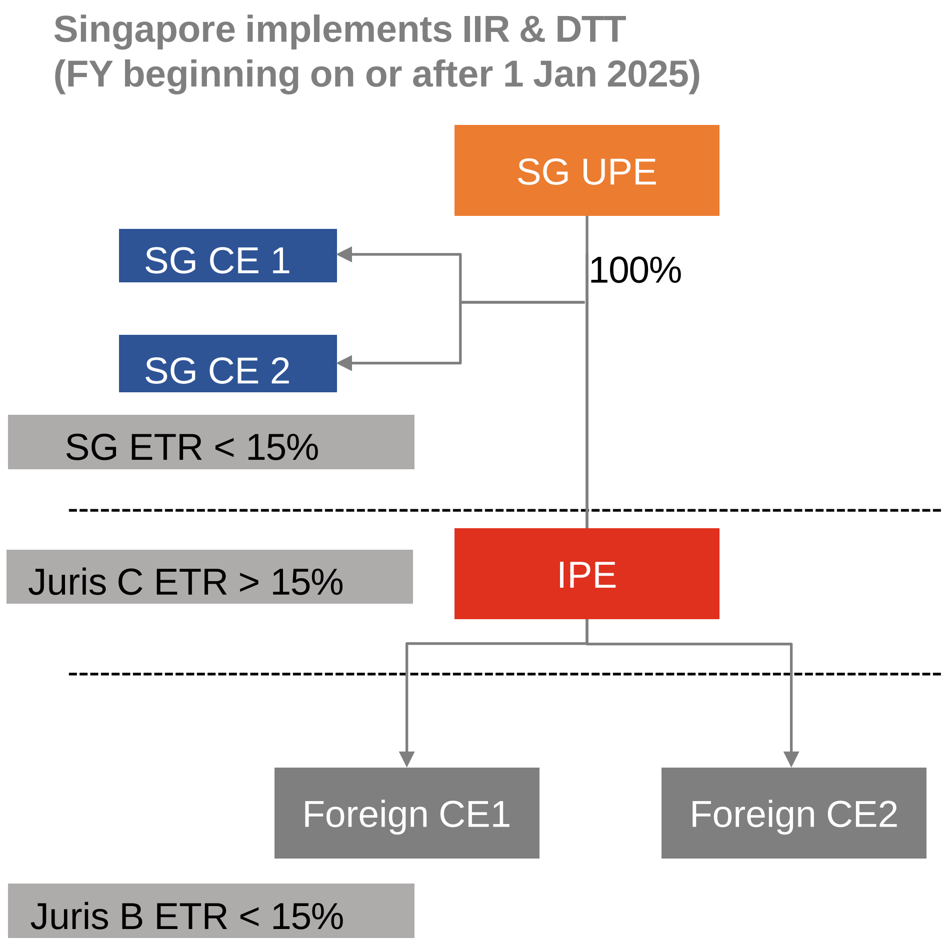
SG: No IIR top-up tax (for low-taxed foreign CEs) and no DTT payable (for low-taxed SG CEs)

FY 2025

SG:

1. SG MNE group pays **DTT** on profits of low-taxed SG CEs to IRAS
2. SG UPE pays **IIR top-up tax** on profits of low-taxed foreign CEs to IRAS

Pillar Two - Impact on MNEs when SG implements IIR and DTT



Example 2: Foreign CEs are held by Intermediate Parent Entity ("IPE") in Juris C which adopts IIR for FY beginning on and or after 1 Jan 2024

FY 2024

- **SG:** No IIR top-up tax and no DTT payable to IRAS
- **Juris C:** IPE pays **IIR top-up tax** on profits of low-taxed foreign CEs 1 and 2 to tax authority of Juris C

FY 2025

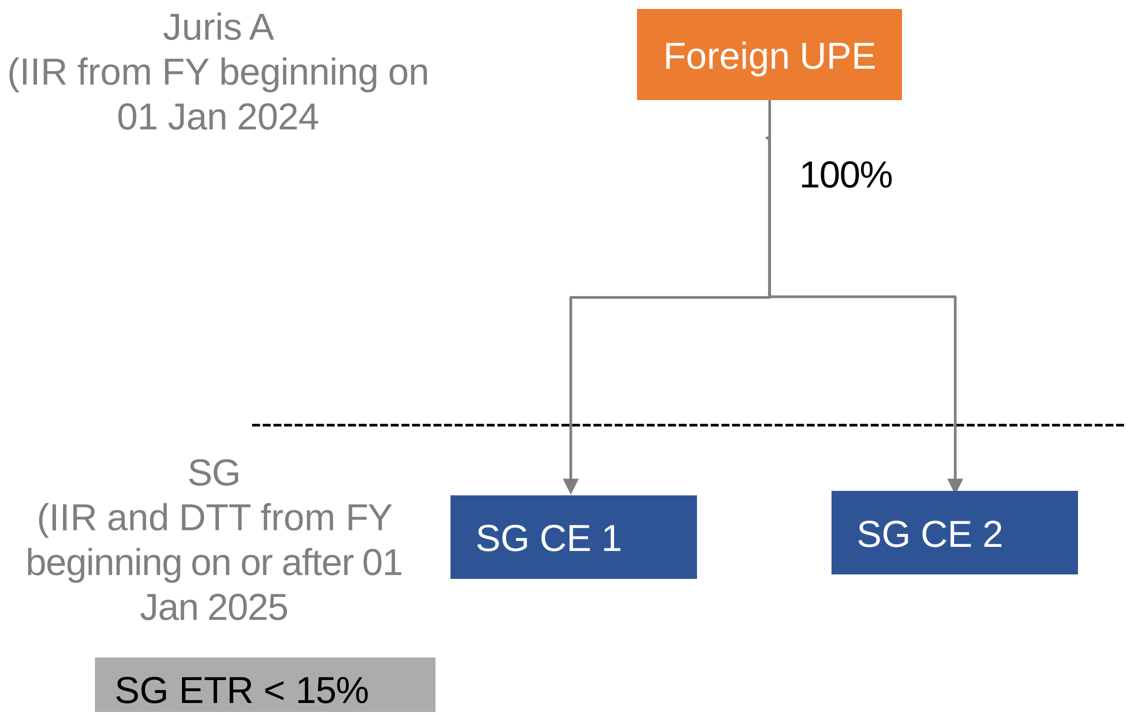
- **SG:**

1. SG MNE group pays **DTT** on profits of low-taxed SG CEs and the SG UPE (if applicable) to IRAS
2. SG UPE pays **IIR top-up tax** on profits of low-taxed foreign CEs 1 and 2 to IRAS

- **Juris C:** No IIR top-up tax payable by IPE (switched off by IIR top-up tax paid by SG UPE)

Pillar Two - Impact on MNEs when SG implements IIR and DTT

Singapore implements IIR & DTT
(FY beginning on or after 1 Jan 2025)



Example 3: Foreign HQ MNE group operating in Singapore

FY 2024

- **SG:** No DTT payable
- **Juris A**: Foreign UPE pays **IIR top-up tax** on profits of low-taxed SG CEs to tax authority of Juris A

FY 2025

- **SG:** Foreign MNE group pays **DTT** on profits of low-taxed SG CEs to IRAS
- **Juris A**: Foreign UPE pays **IIR top-up tax** on profits of low-taxed SG CEs (reduced by DTT paid in SG) to tax authority of Juris A

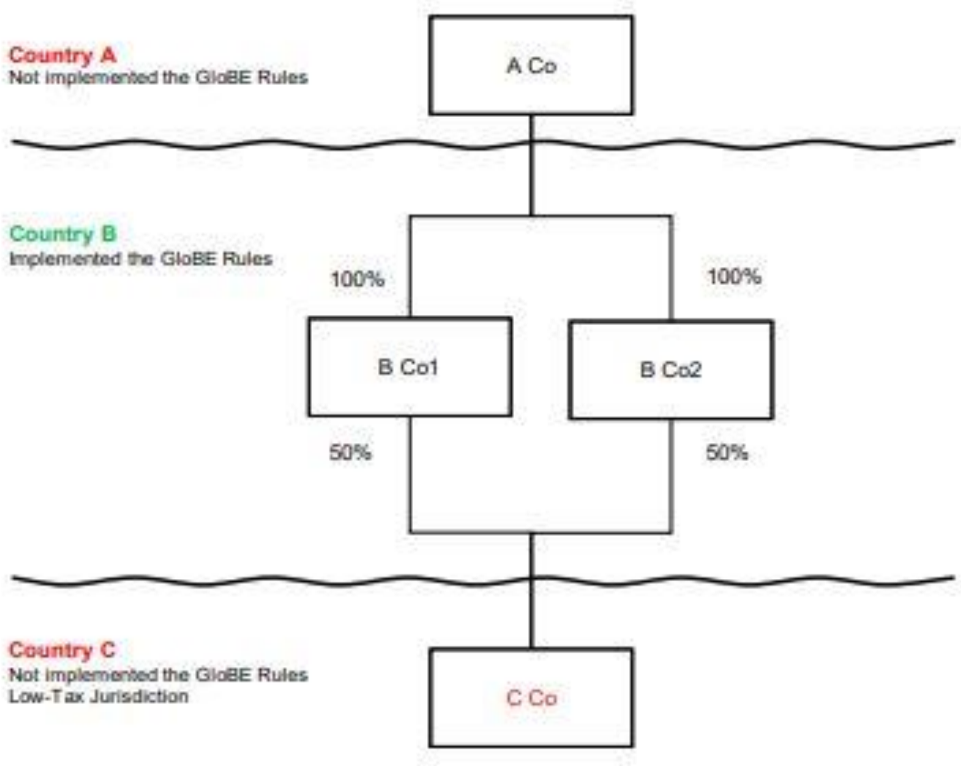
Pillar Two - Top down approach of IIR

Top-down approach of IIR:

- Under the IIR, TUT are collected by the jurisdiction of the UPE from the UPE.
- The TUT is collected in proportion to the ownership interest of the parent entity in the low-taxed CE (LTCE).
- IIR follows a top-down approach, i.e., it is first applied at the UPE level and then flows down along the ownership chain. In other words, if a UPE is not subject to IIR, then the next intermediate parent entity will pay the TUT associated with the LTCE.
- The only exception to this is in the case of a Partially Owned Parent Entity (POPE).

Pillar Two - Top down approach of IIR

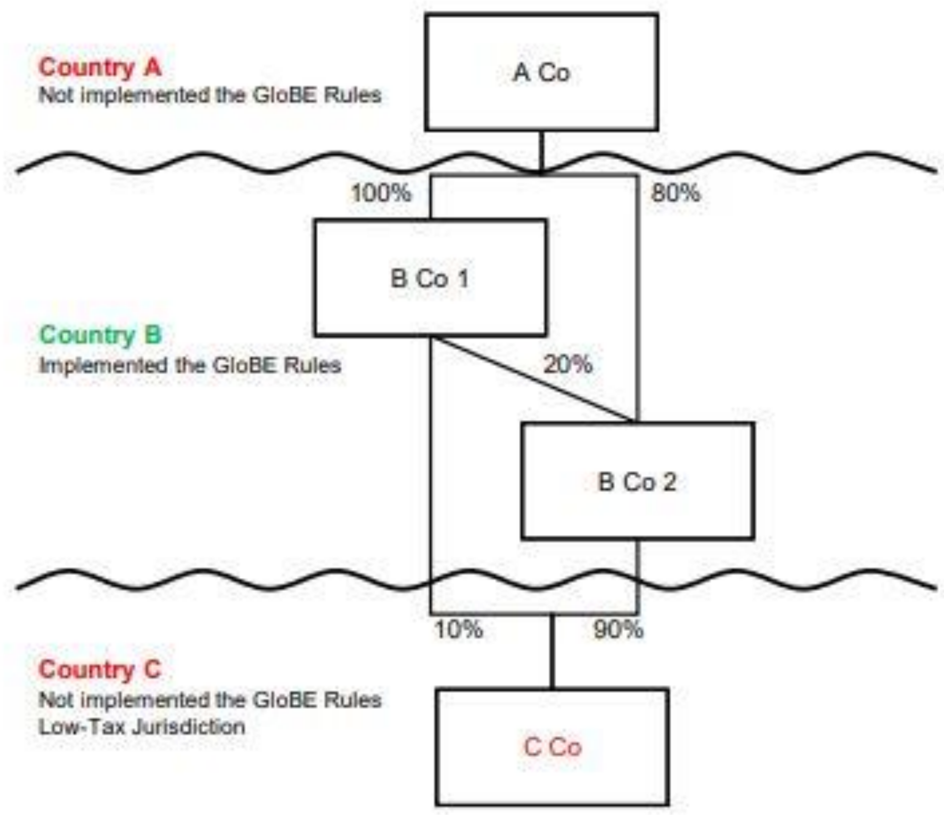
Top-down approach of IIR:



- Question: Who shall apply the IIR ?
- Answer: B Co1 and B Co2 shall apply the IIR based on their allocable share of the Top-up Tax (50% each) of C Co. B Co 1 and B Co 2 pay the Top-tax under the IIR equal to the full amount of C Co's Top-up Tax.

Pillar Two - Top down approach of IIR

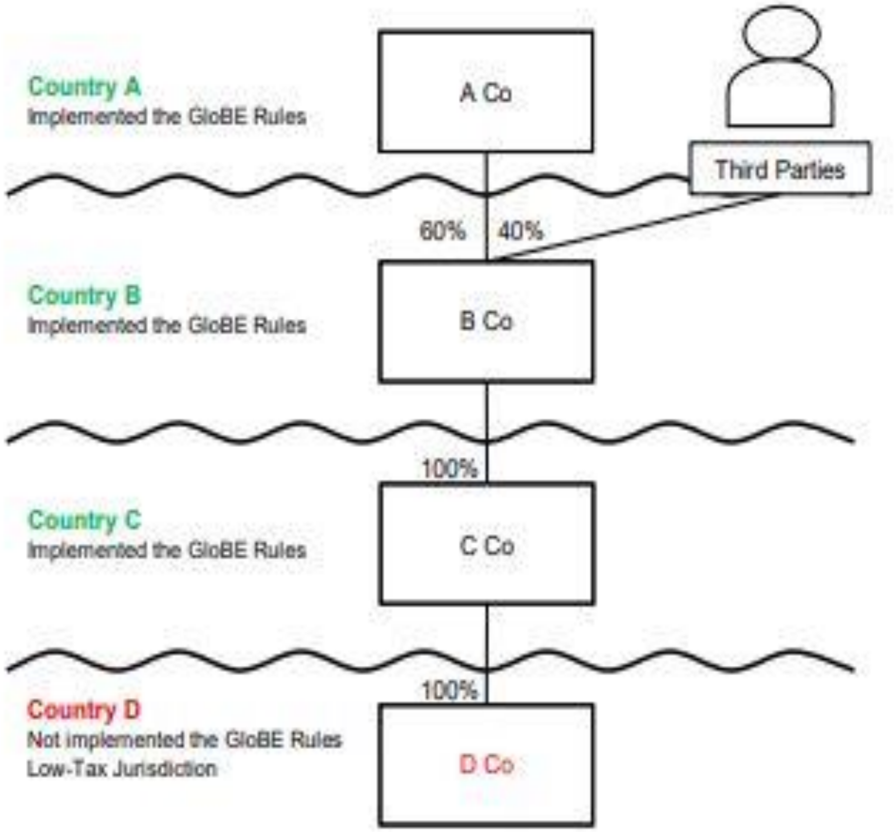
Top-down approach of IIR:



- Question: Who shall apply the IIR ? B Co1 or B Co2 or both ?
- Answer:
  - ✓ Rules does not prevent the lower-tier Entity (B Co 2) from applying the IIR because B Co 1 does not own a Controlling Interest in B Co 2.
  - ✓ Both B Co 1 and B Co 2 are required to apply the IIR under Article 2.1.2 based on their Allocable Share of the Top-up Tax
  - ✓ B Co 2's Allocable Share of C Co's Top-up Tax is 90% (direct holding)
  - ✓ B Co 1's Allocable Share of the Top-up Tax is 28% (10% due to its direct ownership and 18% due to its indirect ownership)
  - ✓ B Co 1 to reduce the Top-up Tax attributable to its indirect ownership in C Co

Pillar Two - Top down approach of IIR

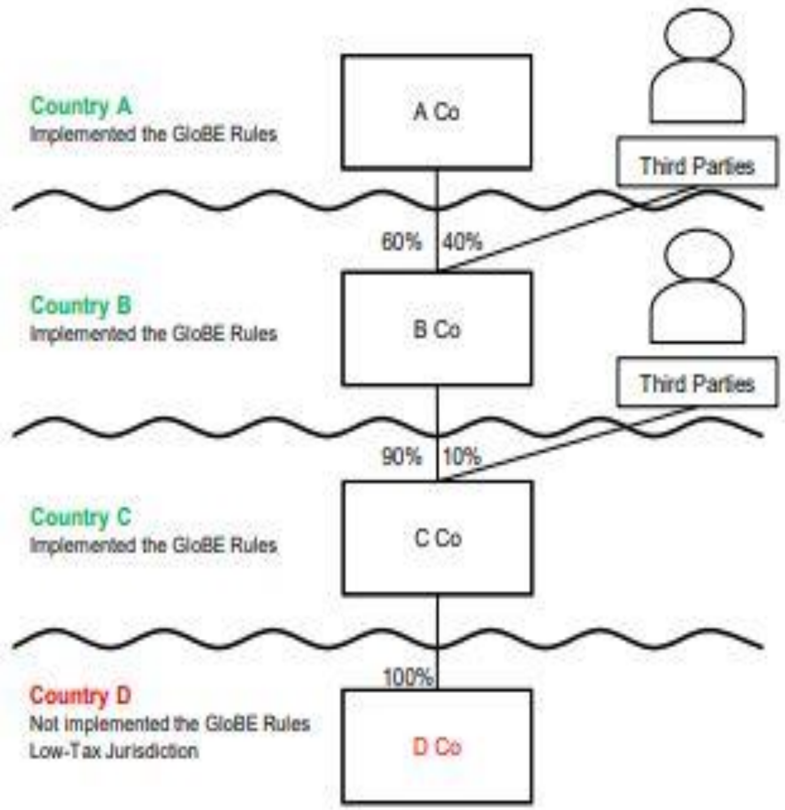
Top-down approach of IIR (in case of POPE):



- Question: Who shall apply the IIR ? A Co, B Co or C Co or all three entities? Note - B Co is a POPE, C Co is also a POPE but D Co is not a POPE as it does not own a controlling ownership in any Constituent entity
- Answer:
  - ✓ POPE is required to apply the IIR based on its Allocable Share of the Top-up Tax of the LTCE notwithstanding that the UPE or an Intermediate Parent Entity is also required to apply the IIR.
  - ✓ Thus, B Co and C Co are required to apply. However, the Rules restricts C Co from applying the IIR because it is wholly owned by another POPE (B Co).
  - ✓ The existence of POPE (B Co) does not preclude the UPE (A Co) from also applying a Qualified IIR. However, the offset mechanism of IIR shall also be taken into consideration.

Pillar Two - Top down approach of IIR

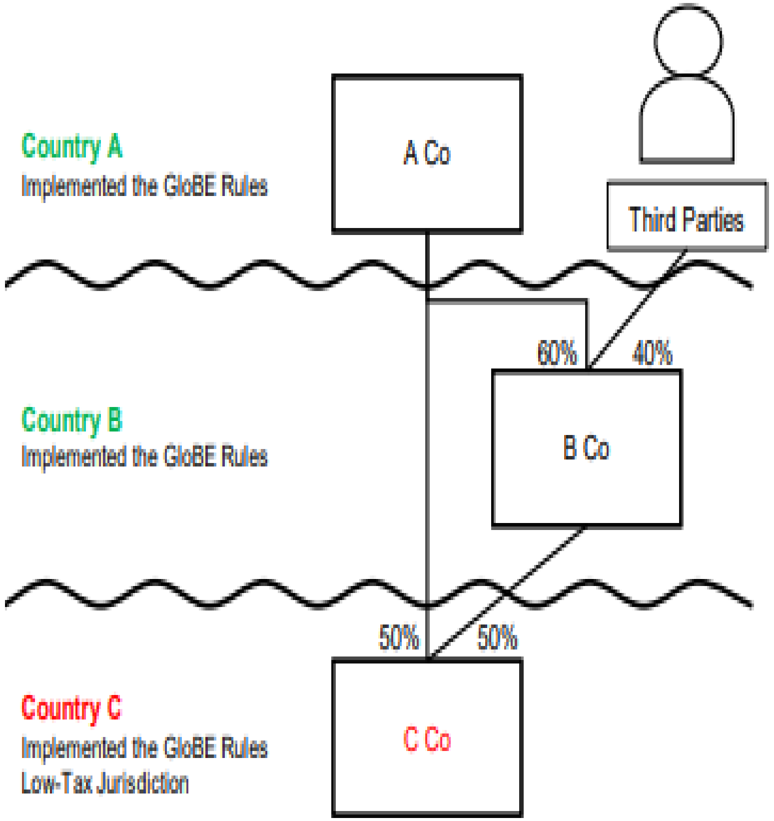
Top-down approach of IIR (in case of POPE):



- Question: Who shall apply the IIR ? A Co, B Co or C Co or all three entities? Note - B Co is a POPE, C Co is also a POPE but D Co is not a POPE as it does not own a controlling ownership in any Constituent entity
- Answer:
  - ✓ POPE is required to apply the IIR based on its Allocable Share of the Top-up Tax of the LTCE notwithstanding that the UPE or an Intermediate Parent Entity is also required to apply the IIR.
  - ✓ Thus, B Co is required to apply, and C Co is also required to apply as it is not wholly owned by another POPE (B Co).
  - ✓ C Co applies IIR to collect 100% of Top-up tax of D Co. B Co shall also apply IIR, but the offset mechanism of IIR shall also be taken into consideration

Pillar Two - Top down approach of IIR

Offset mechanism of IIR in case of POPE:

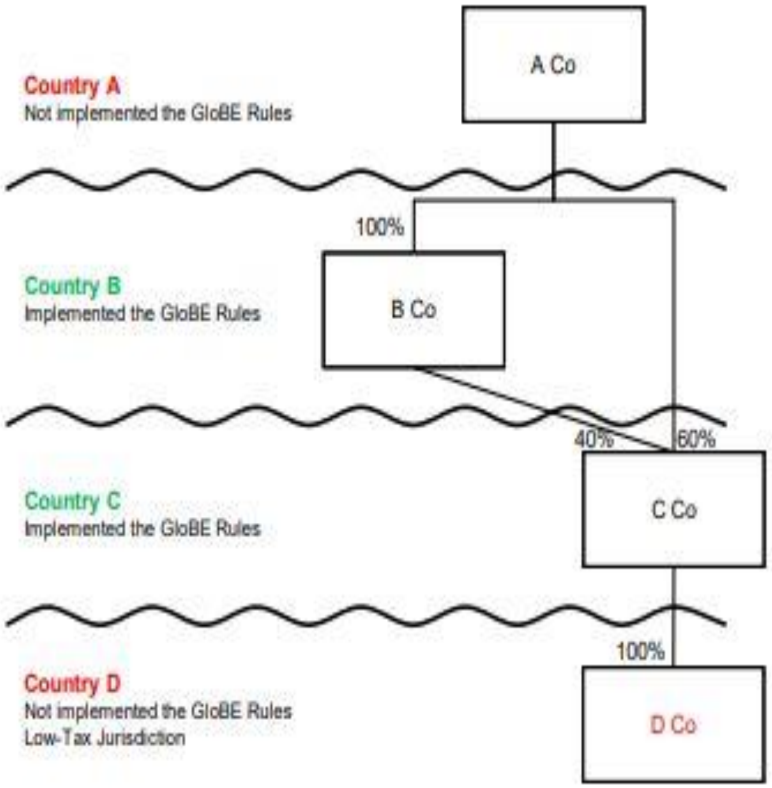


- Question: Top-up tax computed in case of C Co is Euro 10 Mn. Who shall apply the IIR and how would the offset mechanism work?
- Answer:
  - ✓ A Co, being the UPE shall apply IIR. B Co, being the POPE shall also apply the IIR
  - ✓ The offset mechanism works as under:

Entity	Direct Ownership Interest in C Co	Indirect Ownership Interest in C Co	Inclusion Ratio	Allocable Share of Top-up Tax	IIR offset	Final Top-up Tax liability
B Co	50%	-	0.5	EUR 5 million	-	EUR 5 million
A Co	50%	30% (60%*50%)	0.8	EUR 8 million	EUR 3 million	EUR 5 million

Pillar Two - Top down approach of IIR

Offset mechanism of IIR in case of IPE:

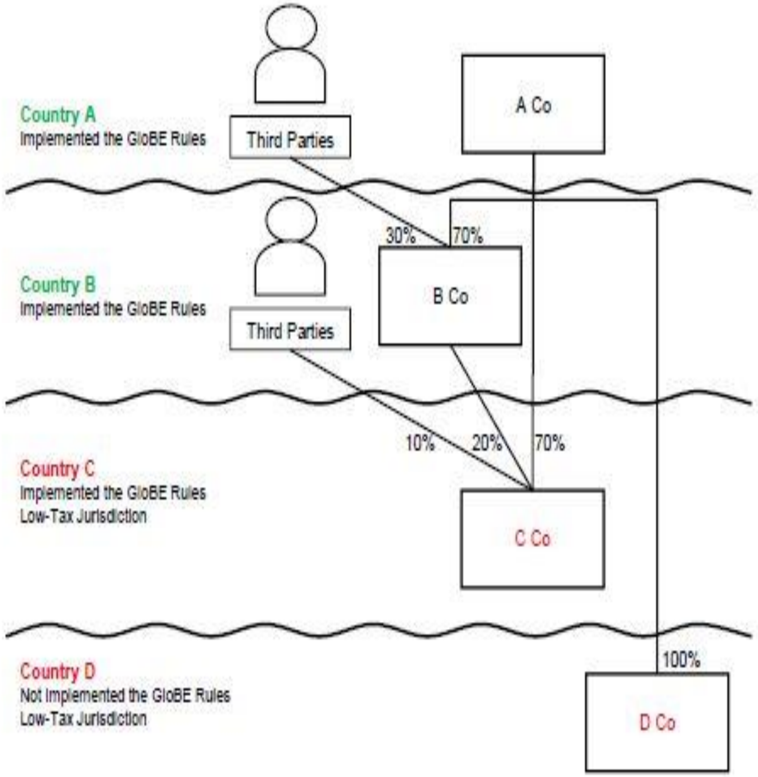


- Question: Top-up tax computed in case of D Co is Euro 10 Mn. Who shall apply the IIR and how would the offset mechanism work?
- Answer:
  - ✓ A Co, though it is the UPE cannot apply IIR as it has not implemented GloBE Rules.
  - ✓ B Co and C Co being the IPEs shall apply the IIR [Had A Co adopted the GloBE Rules, the liability of B Co and C Co for collecting the IIR would get switched off]
  - ✓ The offset mechanism works as under:

Entity	Direct Ownership Interest in D Co	Indirect Ownership Interest in D Co	Inclusion Ratio	Allocable Share of Top-up Tax	IIR off-set	Final Top-up Tax liability
A Co	-	100% (60%+40%)	-	-	-	
B Co	-	40%	0.4	EUR 4 million	EUR 4 million	EUR 0
C Co	100%	-	1	EUR 10 million	-	EUR 10 million

Pillar Two - Allocation of Top-up tax under IIR with offset mechanism

Offset mechanism of IIR in case of POPE:



- The Top-up Tax computed for Country C and Country D for the Fiscal Year are 1,000 and 500 respectively.
- The Financial Accounting Net Income of C Co and D Co reflected in the Consolidated Financial Statements of A Co is 18,000 and 0, respectively. C Co's GloBE Income is 20,000 and D Co's GloBE Income is 35,000.
- The difference between C Co's GloBE Income and the income reflected in the Consolidated Financial Statements is attributable to 2,000 of expenses that are not taken into account in computing GloBE Income or Loss. The difference between D Co's GloBE Income and its income reflected in the Consolidated Financial Statements is attributable to the fact that all of its transactions were conducted with Group Entities located outside of Country D.

Entity	Consolidated income	GloBE Income	Difference
C Co	18,000	20,000	2,000
D Co	0	35,000	35,000

Pillar Two - Illustration for allocation of Top-up tax under IIR

- Question: Top-up tax allocation for A Co and B Co ?
- Answer:

✓ A Co and B Co have implemented Globe Rules. Thus, IIR allocation happens at both the Jurisdictions with an offset mechanism.

✓ The offset mechanism works as under:

- B Co's Allocable Share of the Top-Up Tax of C Co (20%)
- A Co's Allocable Share of the Top-Up Tax of C Co (84%) with an offset for 14% of indirect holding
- A Co's Allocable Share of the Top-Up Tax of D Co (100%)

	A Co	B Co	Non-Group	Total
Allocable Share of C Co Top-up Tax	840	200	100	1,140
Article 2.3 Offset	(140)	-	-	(140)
Allocable Share of D Co Top-up Tax	500	-	-	500
Total Top-up Tax allocated	1,200	200	100	1,500

Pillar Two - MLI for Subject To Tax Rule (STTR)

a) The introduction of the STTR top up of 1.5% (i.e., now 4% in the source country) would not require additional credit to be granted in the residence state.

b) The STTR takes priority over the GloBE Rules and is creditable as a covered tax.

Key aspects of STTR

- **Connected Persons**

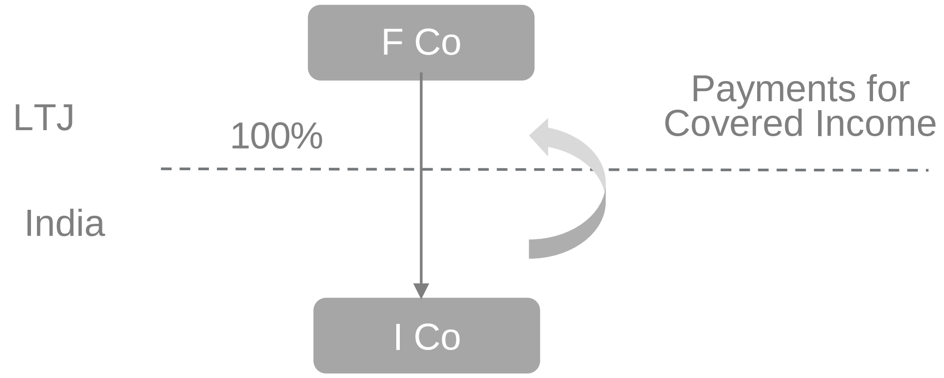
  one has control of the other or both are under the control of the same person or persons (In case of companies - 50% of vote and value of shares).

- **Covered Income**

  i. interest;
  ii. royalties;
  iii. payments for distribution rights for a product or service;
  iv. insurance or reinsurance premiums;
  v. payments of guarantee or financing fees;
  vi. rental payments for industrial, commercial or scientific equipment; and
  vii. payments for services.

- **Exclusions**

  i. Individuals, Non-profit org, State or International org etc.
  ii. Aggregate of covered income received in a FY <1 Mn Euro or 2,50,000 Euro for jurisdictions with GDP below 40 Bn. Euro



F Co jurisdiction CT rate is 5%
F Co - I Co DTAA provides for a source WHT of 2.5%
I Co can now impose an additional tax under STTR of 1.5%

Pillar Two - MLI for Subject To Tax Rule (STTR)

15 Sep 2023

Key aspects for consideration:

- While covered income include both active as well as passive income, it does not cover Dividend income.
- Impact to be seen on countries which provides for a lesser than 10% rate on royalty Income (viz., Mauritius, UEA etc.)
- Provisions of the Article 7, instead of STTR, would apply where the covered income is effectively connected with or attributable to a PE in the source state

MLI for STTR

- The Multilateral Convention to Facilitate the Implementation of the Pillar Two Subject to Tax Rule was adopted on 15 September 2023 by the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS).
- OECD/G20 Inclusive Framework have also released an explanatory statement on the same

Pillar Two - Safe Harbour Provisions

Safe Harbour Provisions: GloBE Rules (read with the Administrative Guidance issued so far) provide for following safe harbour provisions:

1. **Transitional country-by-country report (“CbCR”) Safe harbour**
2. **Permanent Simplified Calculations Safe harbours**
3. **QDMTT Safe harbour**
4. **Transitional UTPR Safe harbour**

Pillar Two - Safe Harbour Provisions

Safe Harbour Provisions:

1. **Transitional CbCR Safe harbour –**

- Transitional CbCR Safe Harbour is valid only during the transitional period, i.e., for fiscal years beginning before 31 December 2026 and not ending after 30 June 2028.
- During that period, MNE can rely on information in a Qualified CbCR which is prepared using Qualified Financial Statements for adopting GloBE Rules.
- A Jurisdiction qualifies for this safe harbour if satisfies any of the following tests:

(i) De Minimis Test - Total revenue < EUR 10 million; and Profit (loss) before income tax < EUR 1 million

(ii) Simplified ETR Test - Has a minimum ETR of 15%(2024), 16%(2025) and 17%(2026).

(iii) Routine Profits Test - This test is satisfied when PBT is equal to or less than SBIE.

Pillar Two - Safe Harbour Provisions

Safe Harbour Provisions:

2. **Permanent Simplified Calculations Safe harbours -**

   - Permanent Safe Harbour rules are provided in Article 8 of the model GloBE Rules and is available to a jurisdiction as an annual election.
   - The Simplified Calculation framework for permanent safe harbour is not yet notified but it will be based on meeting any of the following three tests viz., (i) (i) De Minimis Test, (ii) Simplified ETR Test, and (iii) Routine Profits Test.
   - The distinction between the **Transitional CbCR Safe harbour** vis-à-vis Permanent Simplified Calculations Safe harbour computation mechanism of the three tests. In case of Transition safe harbour, the computation is based on the information available in Qualified CbCR, whereas in case of Permanent Simplified Calculations Safe harbour, as the name suggests, the computation is based on simplified calculations which are yet to be notified i.e., alternative simplified calculations.

Pillar Two - Safe Harbour Provisions

Safe Harbour Provisions:

3. **QDMTT Safe harbour**

- A QDMTT should also contain safe harbours that align with the safe harbours agreed under the GloBE Rules, including the transitional safe harbours.
- Otherwise, the MNE Group will be forced to undertake the detailed income and covered taxes computations solely for purposes of the QDMTT where the Inclusive Framework has determined there is little risk of top-up tax liability.
- A QDMTT safe harbour applies if a CE meets (i) QDMTT Accounting Standard, (ii) the Consistency Standard, and (iii) the Administration Standard

Pillar Two - Safe Harbour Provisions

Safe Harbour Provisions:

4. **Transitional UTPR Safe harbour**

   - While UTPR is designed to operate as a backstop to the IIR, the operation of the rule order under GloBE rules means that the UTPR effectively operates as the primary mechanism for imposing top-up tax in the UPE jurisdiction where that jurisdiction has not introduced a QDMTT.
   - Provides transitional UTPR Safe Harbour only for UPE jurisdictions with a corporate income tax rate of at least 20%.
   - Transition Period means the Fiscal Years which run no longer than 12 months that begin on or before 31 December 2025 and end before 31 December 2026.

Section

4

Pillar Two Implementation Worldwide

Pillar Two Implementation Worldwide

#	Name of the Region	Name of the Country	QDMTT	IIR	UTPR	Remarks
1	Europe	UK, Austria, Belgium, Croatia, Cyprus, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Luxembourg, Netherlands, Poland, Portugal, Romania, Slovenia, Spain, Sweden, Switzerland	01 Jan 2024	01 Jan 2024	01 Jan 2025	Final law in force
		Estonia, Latvia, Lithuania, Malta	Opted for six year extension	Opted for six year extension	Opted for six year extension	Opted for six year extension

Pillar Two Implementation Worldwide

#	Name of the Region	Name of the Country	QDMTT	IIR	UTPR	Remarks
2	America	United States	NA	NA	NA	The U.S. has not yet implemented the rules, and its status is uncertain.
		Canada	01 Jan 2024	01 Jan 2024	01 Jan 2025	Final law in force
		Mexico	NA	NA	NA	Has expressed its intent o apply

Pillar Two Implementation Worldwide

#	Name of the Region	Name of the Country	QDMTT	IIR	UTPR	Remarks
3	Asia	China	No announcement yet	No announcement yet	No announcement yet	No public announcement regarding implementation.
		India	No announcement yet	No announcement yet	No announcement yet	No public announcement regarding implementation.
		Japan	No announcement yet	01 Apr 2024	No announcement yet	Proposal to effect QDMTT and UTPR from 01 Jan 2026
		Indonesia	01 Jan 2025	01 Jan 2025	01 Jan 2026	Final law in force
		Thailand	01 Jan 2025	01 Jan 2025	01 Jan 2025	Final law in force.
		South Korea	01 Jan 2024	01 Jan 2024	01 Jan 2025	Final law in force.
		Singapore	01 Jan 2024	01 Jan 2025	Not announcement yet	No announcement regarding UTPR implementation.
		Malaysia	01 Jan 2025	01 Jan 2025	Not announcement yet	No announcement regarding UTPR implementation.

Pillar Two Implementation Worldwide

#	Name of the Region	Name of the Country	QDMTT	IIR	UTPR	Remarks
4	Middle East	UAE	01 Jan 2025	No announcement yet	No announcement yet	No announcement regarding IIR and UTPR implementation.
		Kuwait	01 Jan 2025	No announcement yet	No announcement yet	No announcement regarding IIR and UTPR implementation.
		Qatar	01 Jan 2025	No announcement yet	No announcement yet	No announcement regarding IIR and UTPR implementation.

Pillar Two Implementation Worldwide

#	Name of the Region	Name of the Country	QDMTT	IIR	UTPR	Remarks
5	Africa	South Africa	01 Jan 2024	01 Jan 2024	No announcement yet	No announcement regarding UTPR implementation
		Nigeria	No announcement yet	No announcement yet	No announcement yet	No announcement yet

#	Name of the Region	Name of the Country	QDMTT	IIR	UTPR	Remarks
6	Other Regions	Australia	01 Jan 2024	01 Jan 2024	01 Jan 2025	Final law in force.

Note: Given the dynamic nature of tax legislations, it is essential to follow the up-to-date information by relying on official government sources and OECD publications.

Disclaimer

- *The contents mentioned in the slide is only for training purposes and should not be considered as an advice or opinion*
- *Illustrations explained in this slide are taken from the official website or presentations of OECD, IRAS etc.*

Thank You

Annexure 1 - Pillar Two - Adjustments for GloBE Income of LTCE

FANIL + Adjustments (+/-) − ISI = Globe Income

FANIL - Financial Accounting Net Income or Loss
ISP - International Shipping Income

Annexure 1 - Pillar Two - Adjustments for GloBE Income of LTCE

#	Adjustments	Reference
1	Net Tax Expense	Para 3.2.1
2	Excluded Dividends	Para 3.2.1
3	Excluded Equity Gains or Losses	Para 3.2.1
4	Included Revaluation Method Gains or Losses	Para 3.2.1
5	Gains or Losses from Disposition of Excluded Assets / Liabilities	Para 3.2.1
6	Asymmetric Foreign Currency Gain / (Loss)	Para 3.2.1
7	Policy Disallowed Expenses	Para 3.2.1
8	Prior Period Errors & Changes in Accounting Policies	Para 3.2.1
9	Accrued Pension Expense	Para 3.2.1
10	Treatment of Debt Releases	Para 2.4 of Adm. Guidance
11	Stock-Based Compensation adjustment	Para 3.2.2
12	Arm's Length Adjustment	Para 3.2.3
13	Qualified Refundable Tax Credit Adjustment	Para 3.2.4
14	Fair Value Gain / Loss Adjustment	Para 3.2.5
15	Aggregate Asset Gain Election Adjustment	Para 3.2.6
16	Intragroup Financing Arrangement (IFA) Expense	Para 3.2.7
17	Intragroup Transaction Election Adjustment	Para 3.2.8
18	Insurance Company Tax Adjustment	Para 3.2.9
19	Tier One Capital Equity Adjustment	Para 3.2.10
20	GloBE M&A Adjustments	Para 3.2.11