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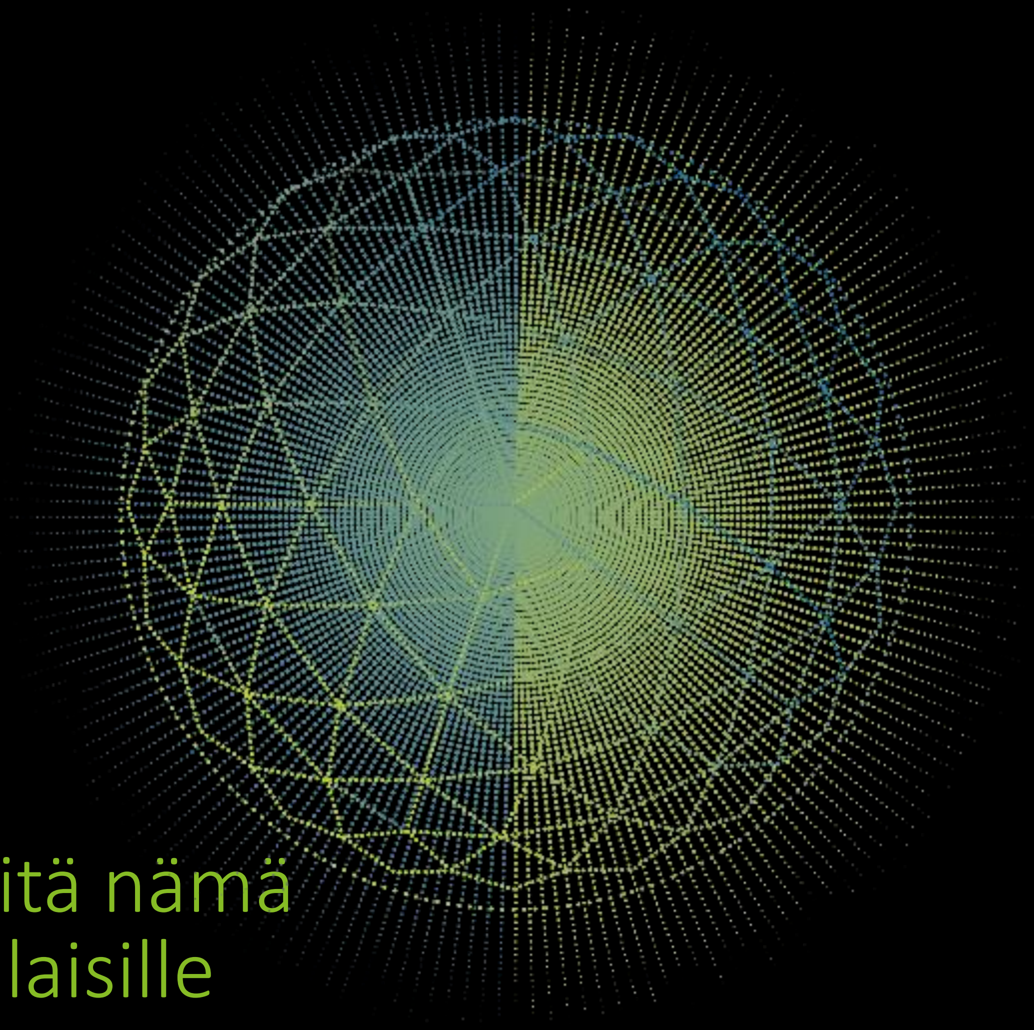

OECD:n Pilarit – Mitä nämä tarkoittavat suomalaisille konserneille?

MAKING AN IMPACT THAT MATTERS
since 1845

Our Team

					
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Taxing the digital economy

Pillar One and Pillar Two: OECD/G20 project involving 130+ countries

Agreement to examine proposals that involve two pillars in hopes of reaching consensus on new international tax rules, based in part on the view of countries that the Internet allows companies (even those not typically thought of as digital) to build their brand, develop an engaged customer base, and create value—even where they lack physical locations

Pillar One
Revision of the existing profit allocation and nexus rules: Realigning *who gets to tax*

Will require global consensus for implementation

Pillar Two
A global anti-base erosion (GloBE) proposal: Ensuring *enough tax is paid somewhere*

Could be implemented on a unilateral basis

Pillar 1 Blueprint

Key elements

Amount A	**New taxing right** A share of residual profit allocated to market countries using a formulaic approach	**In-scope businesses only**
Amount B	**Fixed ‘baseline’ return** for marketing and distribution functions based on the arm’s length principle	**All businesses**
Tax certainty	**Tax certainty** Through effective dispute prevention and resolution mechanisms	**All businesses**

The proposal does not yet have the political agreement of the Inclusive Framework countries

Allocation of residual profits to market / user jurisdictions (Pillar 1 – Amount A)

Scope = Which groups are impacted?

A **multinational group** must meet two **thresholds** for Amount A to apply
- Annual consolidated group revenue threshold (potentially EUR 750 million)
- *De minimis* foreign in-scope revenue

Two broad groups of in-scope business have been identified

Automated digital services

+ **Online advertising services**; online advertising services; sale of user data; **online search engines;** social media platforms; **online intermediation platforms;** digital content services; **online gaming**; standardized online teaching services; **cloud computing services**

– Customized professional services; **customized online teaching services**; online sale of goods or services other than automated digital services; **revenue from the sale of physical goods**; services providing access to the internet or other electronic network

Consumer-facing businesses

Generate revenue from **sale of goods and services 'of a type commonly sold to individual consumers'**

License of otherwise **exploit intangible property** connected to such goods or services

Exclusions include

Extractive industries and natural resources; construction, sale and letting of residential property, **consumer-facing businesses in the financial services sector,** international air and shipping businesses

Allocation of residual profits to market / user jurisdictions (Pillar 1 – Amount A)

Nexus = Which market jurisdictions are entitled for allocation?

	Automated digital services	Consumer-facing businesses
Local sales threshold In-scope revenues above a threshold	✓	✓
’Plus factor’ Indicating ’significant and sustained interaction’ with the market Cloud include • Local subsidiary or permanent establishment • Revenues above a higher threshold		✓

The Amount A nexus cannot be used for any other tax purpose (including VAT and customs duties)

Consideration is being given to using a higher sales threshold for large markets and a lower threshold for small, developing economies

Allocation of residual profits to market / user jurisdictions (Pillar 1 – Amount A)

Tax base = How is the taxable profit used as a basis for allocation calculated?

Profit before tax	• Derived from consolidated group financial accounts • Eligible accounting standard
Adjustments	• Minimal adjustments − dividends – income tax expenses − gains or losses on shares – expenses not deductible for public reason (e.g. penalties)
Segmentation	• Segmented basis where businesses display segmentation hallmarks − Mandatory for larger groups/where material distortions could arise − Smaller groups potentially able to opt in
Losses	• Pooled, either at group or segment level − Carry-forwarded/earn-out mechanism – no Amount A until historical losses utilized • Consideration being given to losses incurred prior to regime and 'profit shortfalls'

Allocation of residual profits to market / user jurisdictions (Pillar 1 – Amount A)

Quantum = How is the amount to be allocated determined?

1. **Profitability threshold:** determine the residual profit of the group in excess of an agreed profitability threshold
   - Based on ratio of profit before tax to revenue
2. **Reallocation percentage:** an agreed percentage of the residual profit that can be allocated to market countries
   - Remaining profits assumed attributable to activities not targeted by Amout A
3. **Allocate the relevant portion of residual profit to market countries**
   - Based on locally sourced in-scope revenues

Differentiation	Marketing and distribution profits safe harbour	Domestic business exemption

Allocation of residual profits to market / user jurisdictions (Pillar 1 – Amount A)

Double counting / elimination of double taxation = Which country is losing taxable profits due to the allocation?

Step 1: qualitative **activities test** to identify group entities making **'material and sustained contributions**' to residual profits based on a transfer pricing functional analysis

Step 2: quantitative **profitability test** to ensure paying entities can bear the Amount A tax liability

Step 3: amount A tax liability allocated to paying entities with a **market connection**

Step 4: remaining Amount A tax liability apportioned between other entities on a **formulaic pro-rata basis**

Amount A liability allocated to paying entities relieved via either **exemption method** or **credit method**

Compensation for baseline marketing and distribution activities (Pillar 1 – Amount B)

Key characteristics

Aims to **standardize** the remuneration of related party distributors that perform **'baseline marketing and distribution activities'** in a manner that is aligned with the arm's length principle.

Applies to potentially **all business sectors** and is **not subject to scope limitations**

The quantum of the fixed return is likely **to be based on comparable company benchmarking analyses**, under the Transactional Net Margin Method (TNMM), potentially varying by industry and/or region
- Amount B may be rebuttable by providing evidence that another transfer pricing method (e.g., a strong Comparable Uncontrolled Price) would be the most appropriate

Does not supersede previously-agreed **advance pricing agreements/mutual agreement procedure settlements**

Narrow scope for 'baseline marketing and distribution activities' – may be buy/sell distributors that take legal title to goods

Pillar 2

Pillar Two – global minimum tax

Two key elements: GloBE and Subject to tax rule

Income inclusion rule (IIR) and Undertaxed payments rule (UTPR)

Rules for ensuring **large multinational groups** pay a **minimum level of tax** **in each jurisdiction** in which they operate

Income inclusion Rule (IIR)

plus switch-over rule

Undertaxed payments Rule (UTPR)

(backstop)

Subject to tax rule (STTR)

Source country taxation of specific types of **intra-group payments**

Applies in **priority** to other Pillar Two rules

All rules operate as a 'top up' to a minimum rates – minimum rates not yet agreed

The proposal does not yet have the political agreement of the inclusive Framework countries

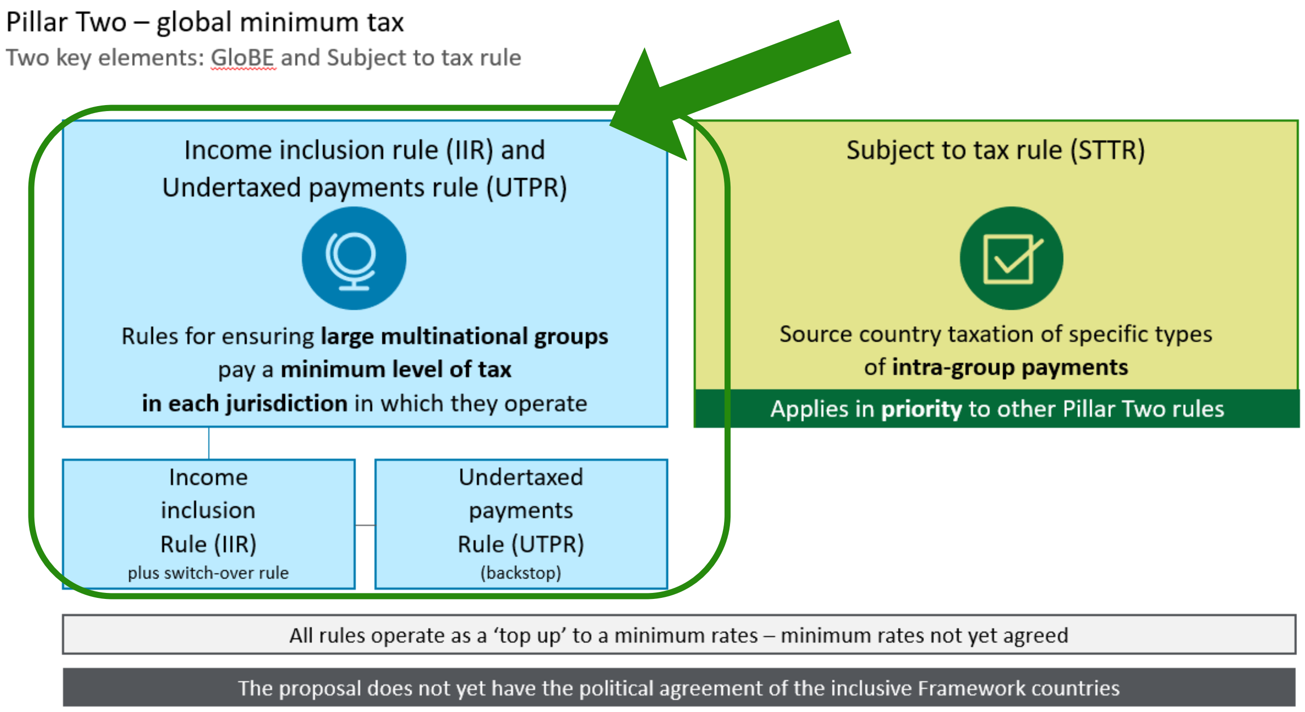
Pillar Two: GloBE

Scope

Multinational groups with consolidated group revenue below **EUR 750 million** (or equivalent) in the preceding fiscal year are **excluded from scope**

Excluded entities

All industries, but treatment of **international shipping industry** to be determined



Pillar Two: GloBE

Calculation of effective tax rate

(Adjusted) Covered taxes ÷ **(Adjusted) GloBE tax base** = **GloBE ETR - calculated annually in each country the group has entities**

Pillar Two: GloBE

Calculation of effective tax rate

Calculation of tax base (per tax year)

Group accounting entity-level profit or loss before tax → Limited number of book-to-tax adjustments → Tax base

Covered taxes are taxes on a group company's **income or profit**

- Domestic and foreign taxes on income are included
- Taxes paid under controlled foreign company (CGC) rules attributed to the country with the underlying income
- Taxes such as sales taxes, VAT, digital services taxes, are **not** covered taxes

Mechanical carry-forward rules to reduce the effects of temporary differences on volatility of effective tax rates

Losses

Carried forward in the same country indefinitely

Excess taxes

Possibly a seven-year look-back/carry-forward period

Pillar Two: GloBE

Formulaic substance-based carve-out

If the effective tax rate for a country is below the minimum rate, an amount of profit is **carved out**

Payroll component

Fixed percentage mark-up on **payroll costs** of **eligible employees performing activities** in the country

- Includes bonuses, pensions, benefits and employer social security contributions
- Includes independent contractors

Tangible asset component

Fixed percentage mark-up applied to items such as

- Depreciation
- Deemed depreciation of land

Pillar 2: Subject to tax rule

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Pillar Two: subject to tax rule

Rule applies only to **payments between connected parties**

- Based on **common control**
- Payments to **excluded entities** (investment funds, government entities etc.) will be out of scope

Rule applies only to **defined categories of payments**

Interest

Royalties

Other payments

Rent or **payment** for use of right to use **moveable property**

Consideration for supply of **marketing, procurement, agency** or **other intermediary services**

Franchise fees or other payments for use of intangibles in combination with services

Guarantee, brokerage or **financing fees**

Insurance/reinsurance premiums

Subject to a **low profit margin exclusion**

Pillar Two: Subject to tax rule

Rule triggered when the **’adjusted nominal tax rate’** is below the agreed minimum rate

- Based on **nominal statutory tax rate** applicable to company receiving the payment
- Adjusted for features of the local tax system (e.g. preferential regime rates)
- The minimum rate may differ from the minimum rate for GloBE

Materiality thresholds

- Potentially based on: **size of the group**; **ratios** of covered payments to total expenditure; or **tiered thresholds** based on the value of covered payments (tiers based on GDP of source country)

Administrative approaches being explored:

- An **annualized charge**, assessed post year-end;
- Withholding tax, with certification system providing for reduced rates: and/or
- **Interim contingent withholding taxes**, set at a lower level **with an annual balancing payment**.