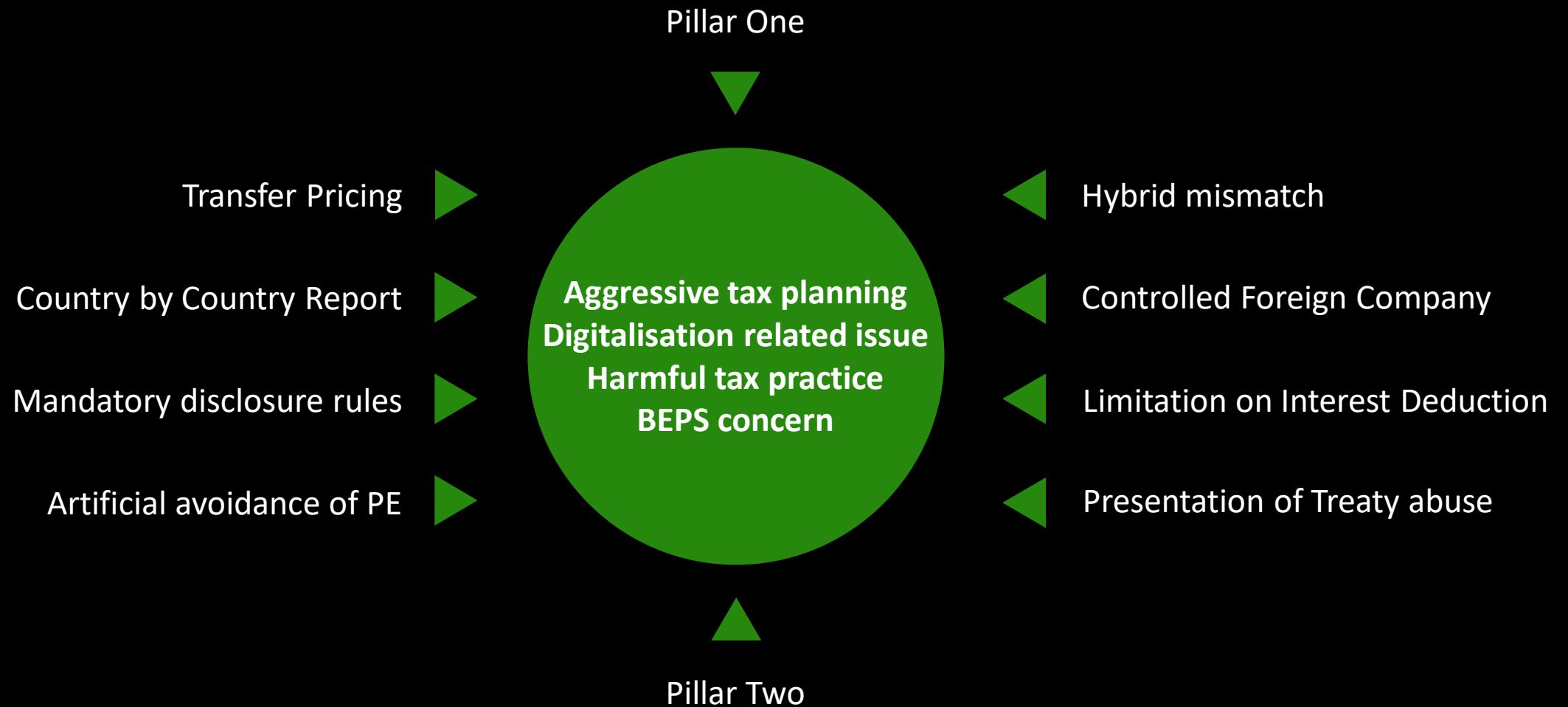




G20/OECD Inclusive Framework on BEPS: Reports on Pillar One and Pillar Two Blueprints



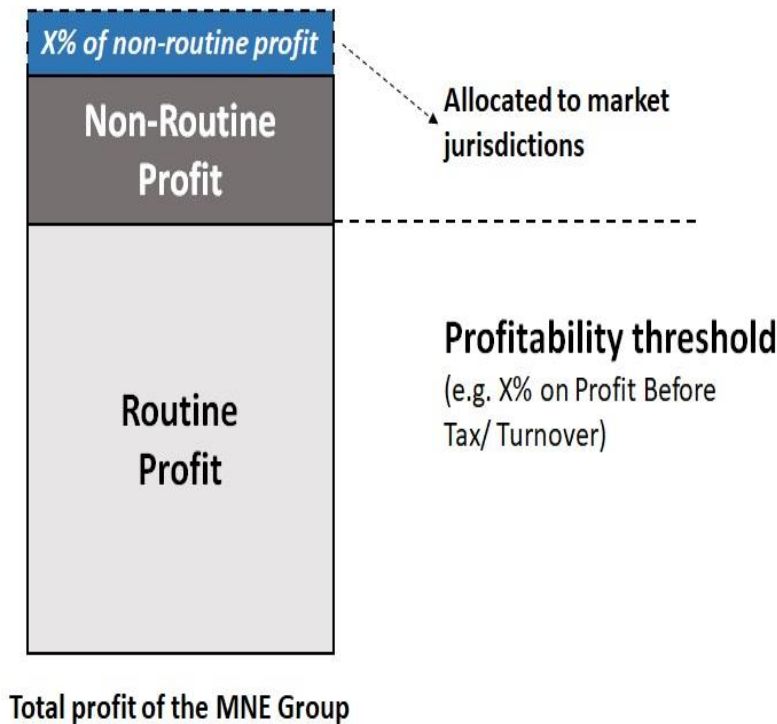
Introduction



Pillar One Approach

New nexus and profit allocation rules
Three tier mechanism proposed

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
Amount C	Additional return where marketing, distribution, other activities in a country go beyond the Amount B baseline, along with improved dispute resolution	All businesses

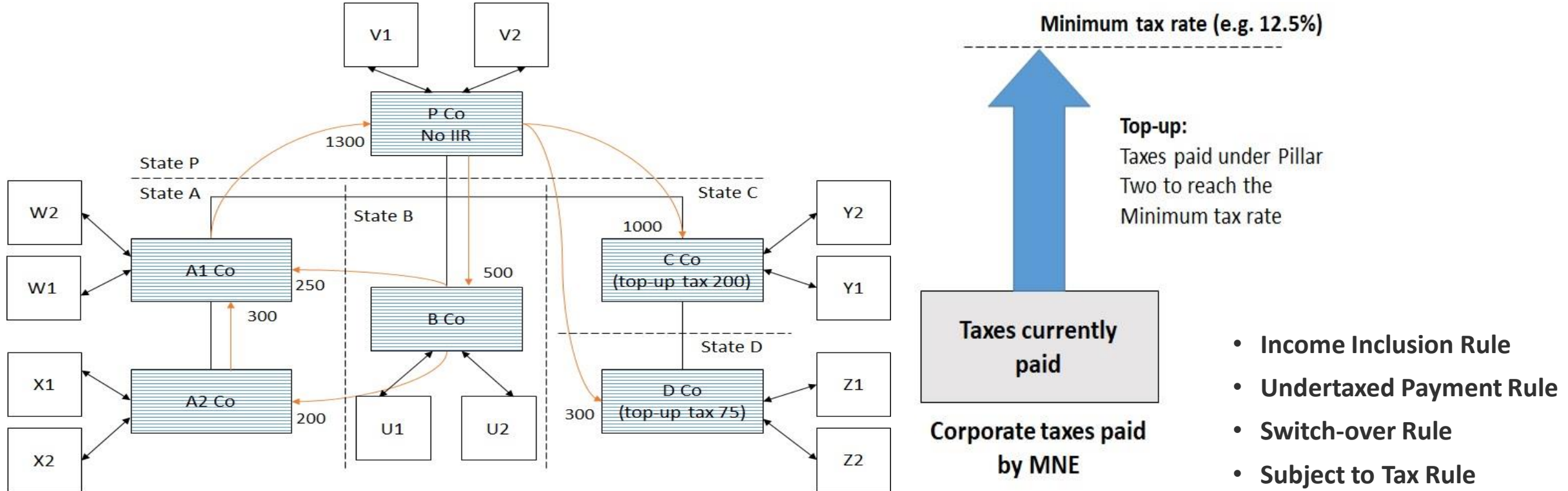


Pillar One salient features

- MNE group with global revenue of Euro 750mn
- Automated digital services (ADS) and Consumer Facing Business (CFB)
- Assessment of income at group level and distribution of taxing rights to market jurisdictions
- New MLI and changes to the domestic laws

A	B 800	C
100 D	150 E	150 F

Pillar Two approach



- Pillar Two is focused on the *remaining BEPS challenges* and proposes a systematic solution designed to ensure that **large internationally operating businesses pay a minimum level of tax** regardless of where they are headquartered or the jurisdictions they operate in.
- Pillar Two leaves jurisdictions free to determine their own tax system, including whether they have a corporate income tax and where they set their tax rates, but also **considers the right of other jurisdictions to apply the rules contained in this report where income is taxed at an effective rate below a minimum rate**



Scope of the GLoBE Rules

Scope of GloBE Rules

- MNE Groups having total consolidated group revenue €750 million or above, in the immediately preceding fiscal year, are subject to application of the GloBE rules.
- The consolidated group revenue threshold is applied to all those CEs that are owned and controlled by the same UPE
- Excluded entities
 - Investment Fund
 - Pension Fund
 - Governmental Entity
 - International Organisation
 - Non-profit Organisation
 - Certain UPEs subject to tax neutrality regimes

GloBE Rules

Income Inclusion Rule (IIR)

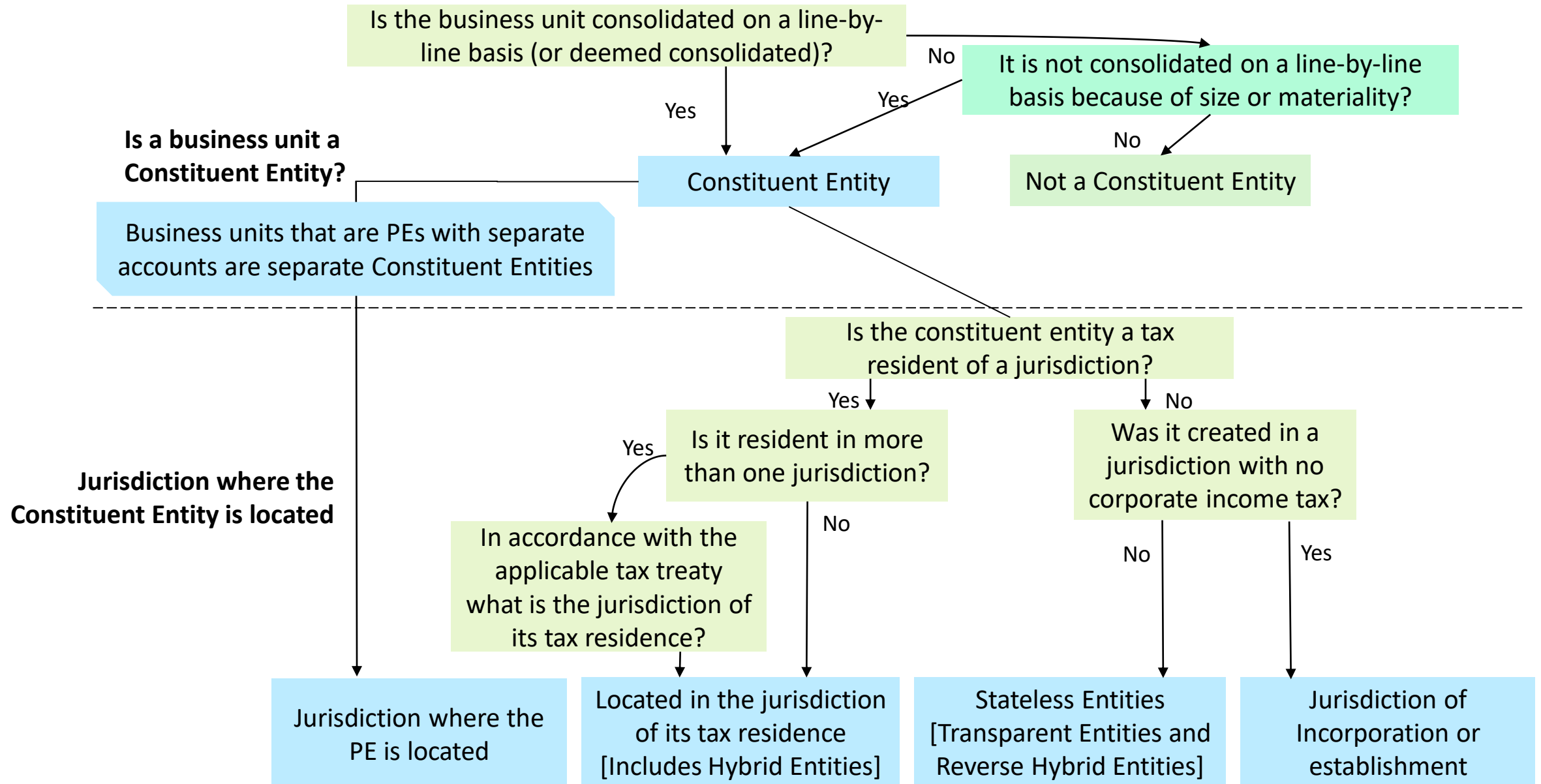
Undertaxed Payment Rule (UTPR)

Switch-over Rule (SOR)

Subject to Tax Rule

Concepts and threshold adopted from CbCR mechanism

Constituent Entity

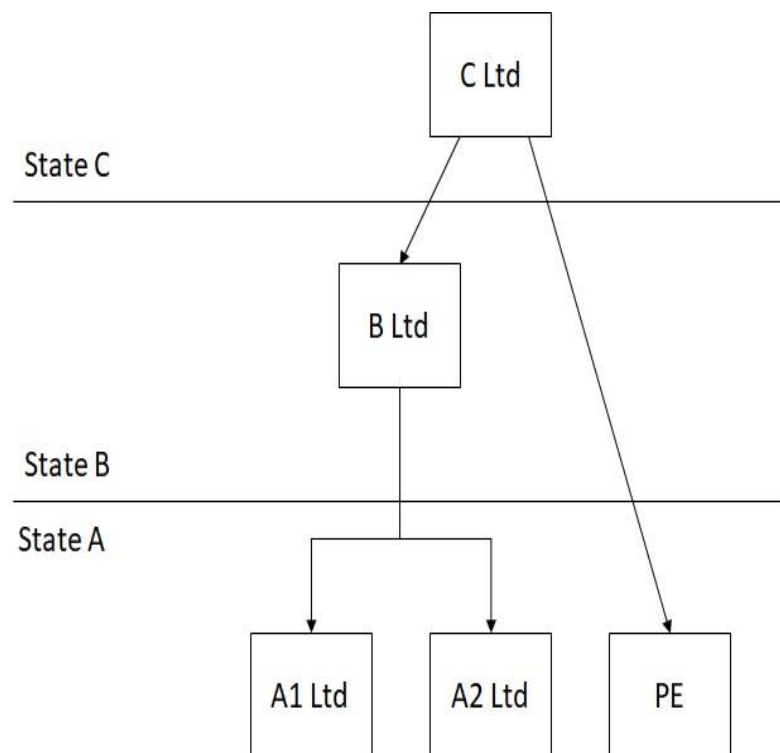




Income Inclusion Rule (IIR)

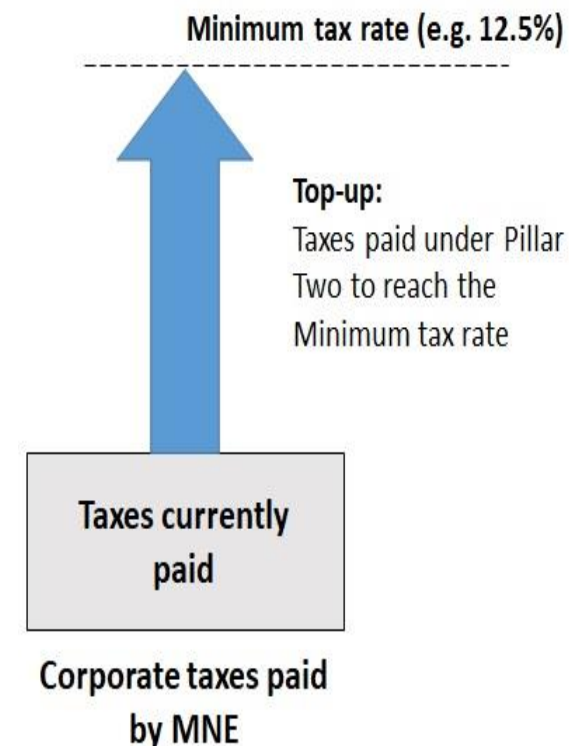
Computation of ETR – Jurisdictional Blending

Determination of IIR top-up tax payable by shareholder



Scenario 1	Total	A1 Ltd	A2 Ltd	PE
Covered Taxes	351	100	120	131
GloBE Income	3900	1200	1400	1300
ETR %	9.00	8.33	8.57	10.08

Scenario 2	Total	A1 Ltd	A2 Ltd	PE
Covered Taxes	250	50	150	50
GloBE Income	2500	1200	1400	-100
ETR %	10.00	4.17	10.71	

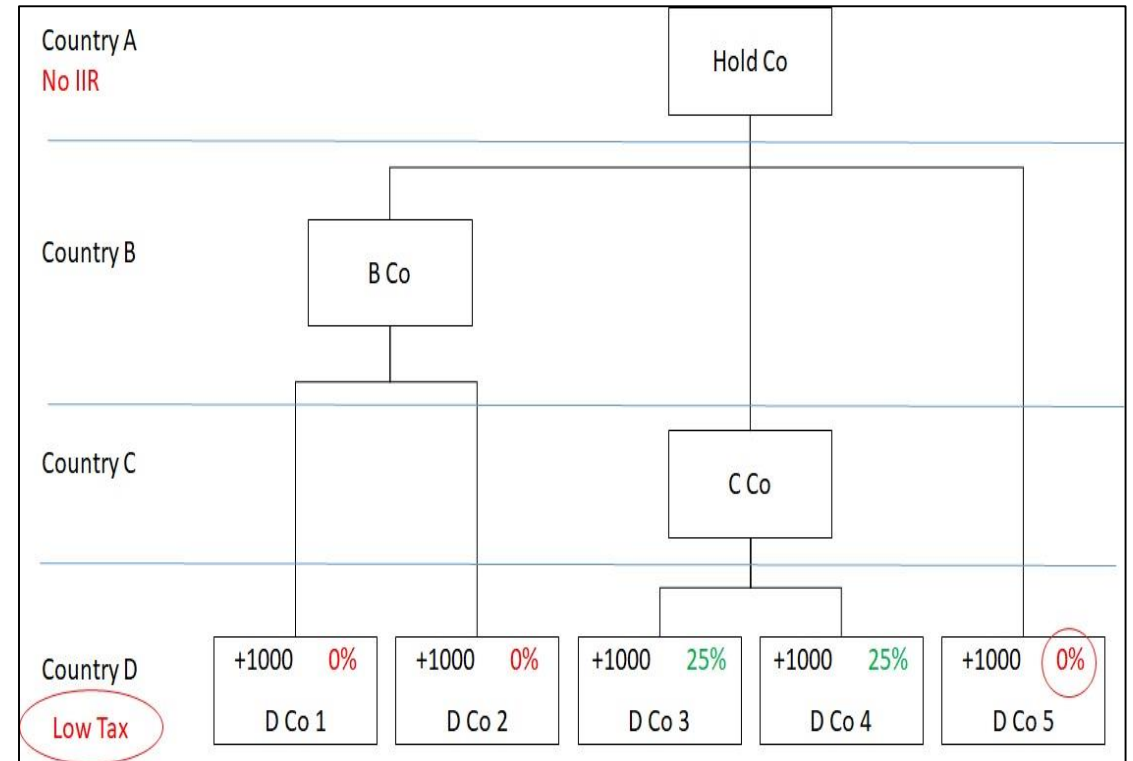
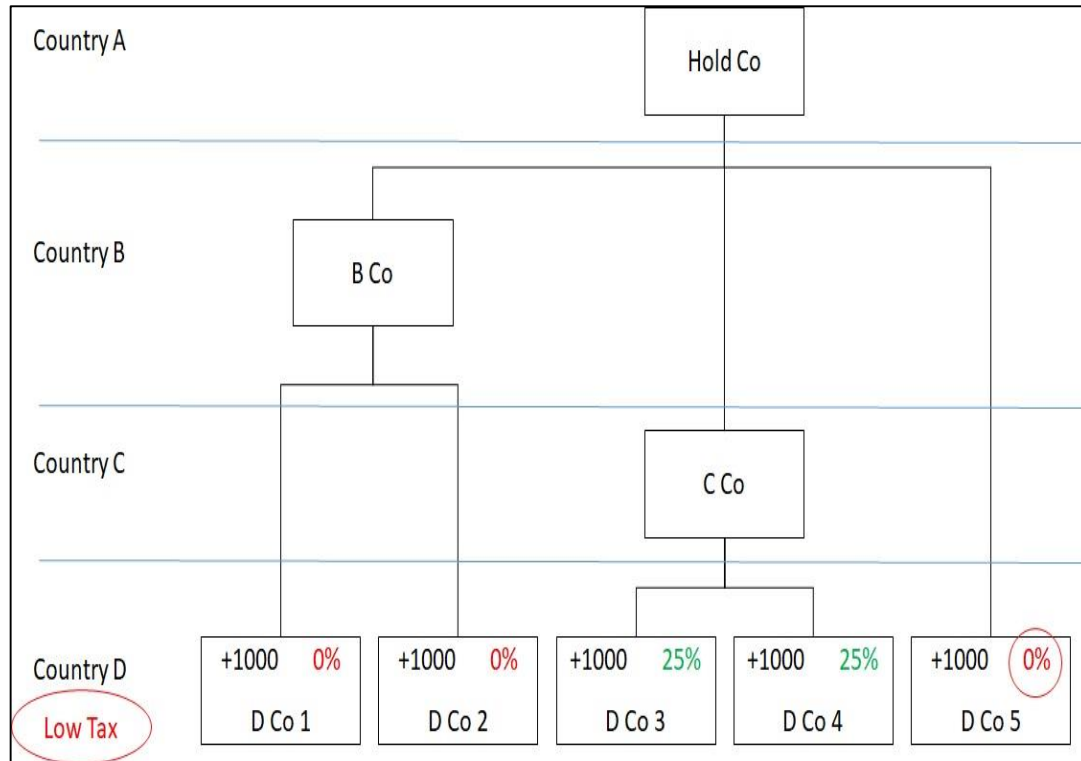


A Parent (including a Partially Owned Intermediate Parent) that owns (directly or indirectly) an equity interest in a foreign low-taxed Constituent Entity at the end of a reporting period shall be subject to a top-up tax under the IIR in respect of its proportionate share of the income of that Constituent Entity for that period.

Application of IIR

Top-down approach

This approach gives priority to the application of the income inclusion rule in the jurisdiction of the Constituent Entity that is at or near the top of the ownership chain in the MNE Group, starting with the UPE. In the event the UPE is not located in a jurisdiction that has implemented the IIR, then responsibility for applying the IIR falls to the CE that is directly owned and controlled by that UPE, and so on, down the chain of ownership.



ETR – Some theory

- The jurisdictional ETR computation requires assignment of the income and taxes among the jurisdictions in which the MNE operates and to which it pays taxes.
- Assignment of taxes to follow assignment of income
 - Covered taxes paid by a CE with respect to dividends distributed by another CE are assigned to the jurisdiction of the CE that paid the dividend.
 - Tax paid under CFC regime is assigned to the CFC jurisdiction as it is in respect of such income

Covered Taxes inclusions

- Any tax on an entity's income or profits
- Tax on distributed profits
- Taxes imposed in lieu of a generally applicable income tax
- Taxes on retained earnings and corporate equity
- Taxes based on multiple components
- Taxes on distributed profits
- Taxes paid under CFC rules

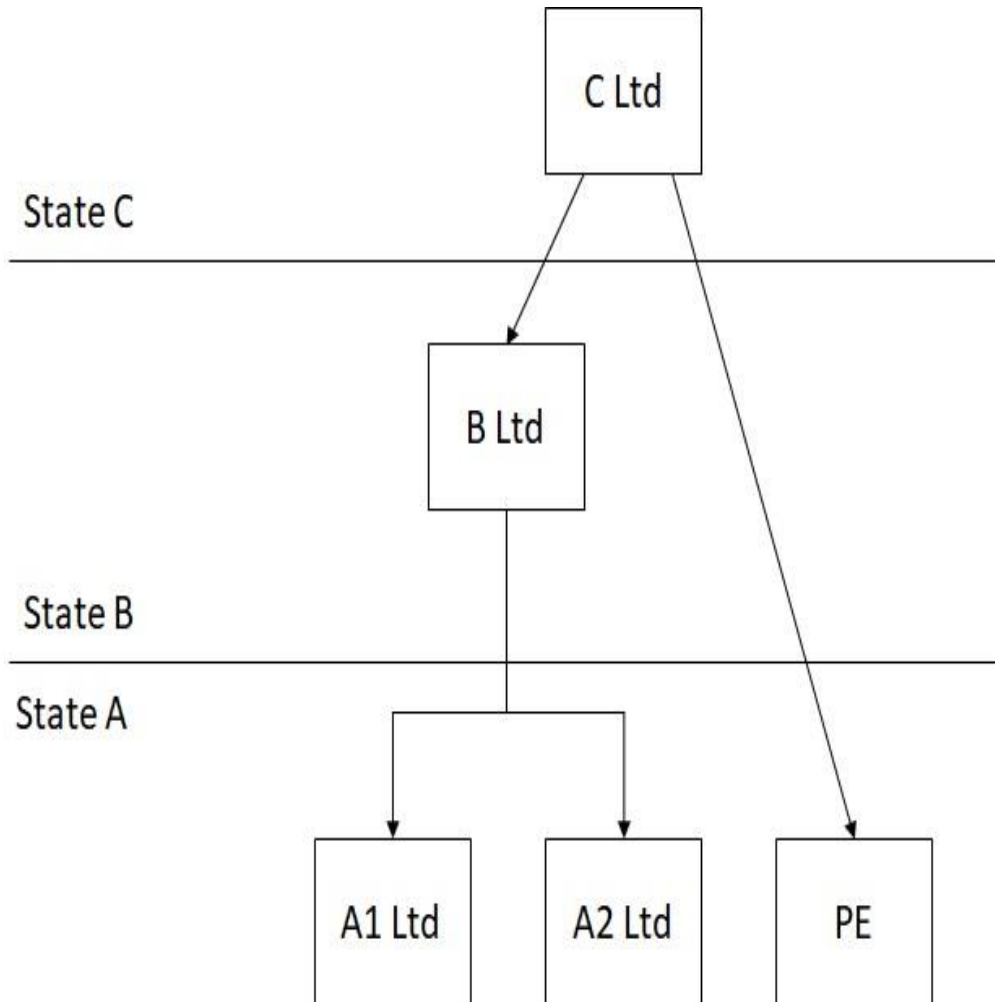
Covered Taxes exclusions

- Consumption and sales taxes
- Excise taxes
- Digital services taxes
- Stamp and other transfer taxes
- Payroll taxes and social security contributions
- Property taxes



Switch Over Rule

Switch Over Rule



- C Ltd. is the Ultimate Parent Entity (UPE)
- As per State C Income Inclusion Rule, C Ltd. has the obligation to pay IIR top-up tax on the income earned by PE
- Article 23 of the tax treaty between State C and State A adopts “exemption method”
- In terms of the treaty State C is not authorized to levy tax on the income earned by PE in State A. State A has exclusive taxing right.
- Conflict between IIR and tax treaty
- Switch Over Rule addresses this conflict



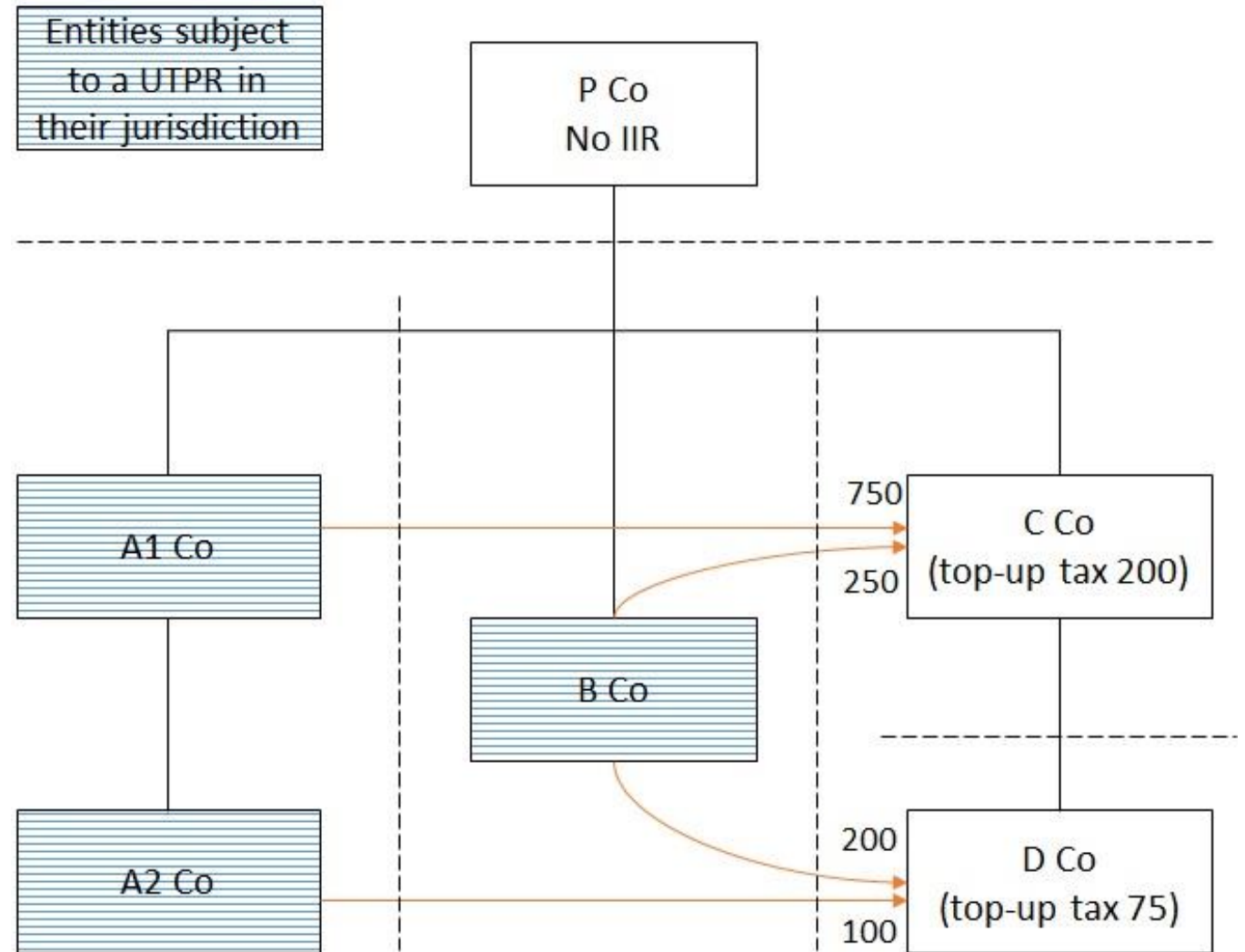
Undertaxed Payment Rule

Undertaxed Payment Rule

Example One – First Allocation Key

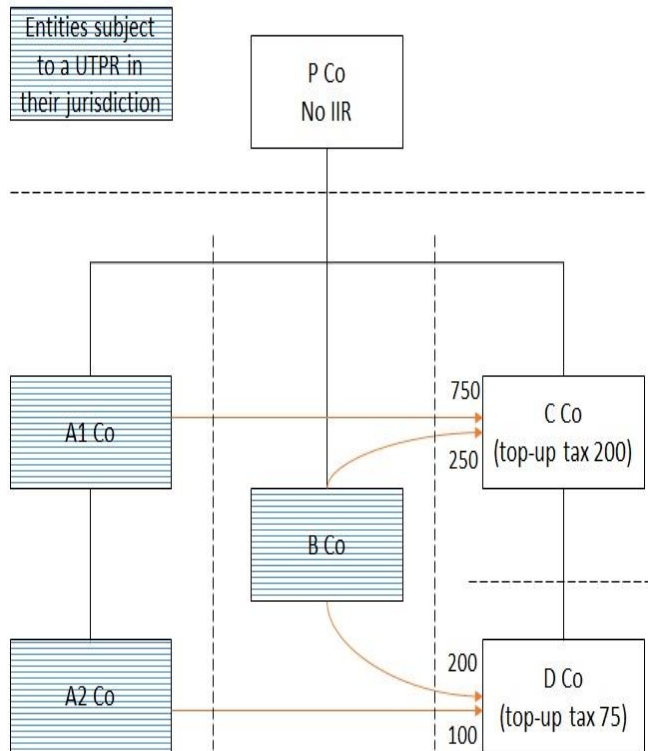
- No IIR in State P
- The ETR in Country C and Country D are below the minimum rate
- Top up tax payable in respect of C Co. and D Co. is 200 and 75 respectively

UTPR acts as a backstop to IIR



Undertaxed Payment Rule

Example One – First Allocation Key



Allocation of top up tax in relation to C co's profits

UTPR Taxpayers	Amount of direct payments made to C Co	Proportion of direct payments
A1 Co	750	750/1000 = 75%
B Co	250	250/1000 = 25%
Total	1000	100%

UTPR Taxpayers	Proportion of direct payments	Allocated top-up tax
A1 Co	75%	75% x 200 = 150
B Co	25%	25% x 200 = 50
Total	100%	200

Allocation of top up tax in relation to D co's profits

UTPR Taxpayers	Amount of direct payments made to D Co	Proportion of direct payments
A2 Co	100	100/300 = 33.33%
B Co	200	200/300 = 66.66%
Total	300	100%

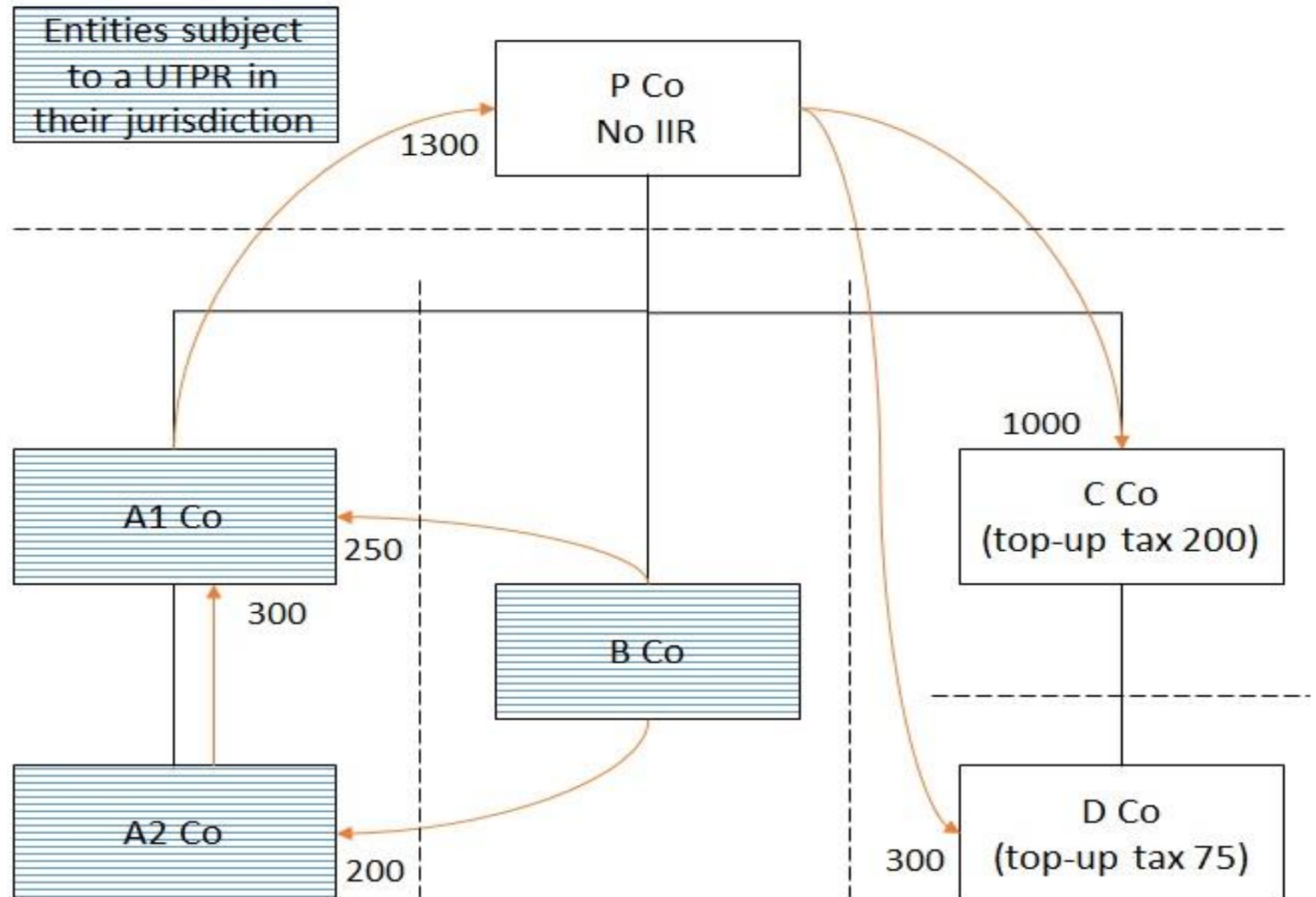
UTPR Taxpayers	Proportion of direct payments	Allocated top-up tax
A2 Co	33.33%	33.33% x 75 = 25
B Co	66.66%	66.66% x 75 = 50
Total	100%	75

Influence of domestic tax rate on UTPR top up tax

Undertaxed Payment Rule

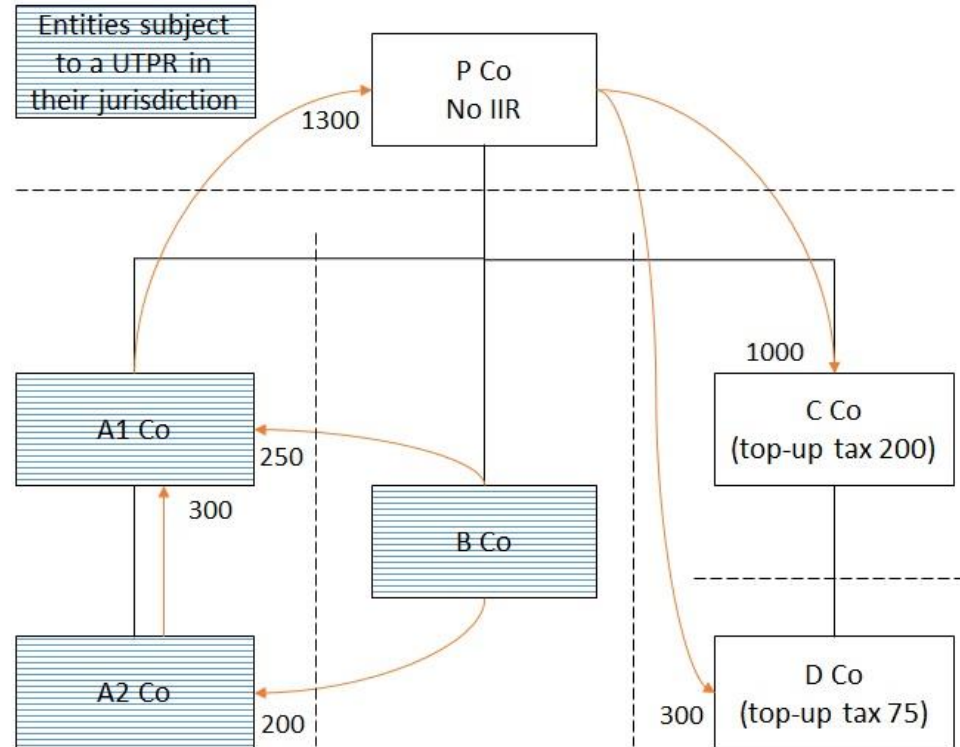
Example Two – Second Allocation Key

- No IIR in State P
- The ETR in Country C and Country D are below the minimum rate
- Top up tax payable in respect of C Co. and D Co. is 200 and 75 respectively
- There are no direct payments by group entities to C Co. and D Co.



Undertaxed Payment Rule

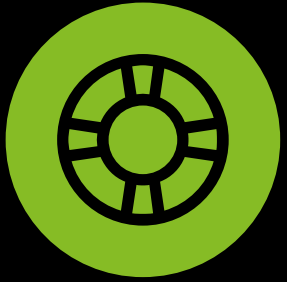
Example Two – Second Allocation Key



UTPR Taxpayers	Related party Income	Related party expenses	Amount of net intra-group expenditure
A1 Co	$300 + 250 = 550$	1300	$550 - 1300 = (750)$
A2 Co	200	300	$200 - 300 = (100)$
B Co	-	$250 + 200 = 450$	(450)

UTPR Taxpayers	Amount of net intra-group expenditure	Proportion of net intra-group expenditure
A1 Co	(750)	$750/1300 = 58\%$
A2 Co	(100)	$100/1300 = 8\%$
B Co	(450)	$450/1300 = 34\%$
Total	(1300)	100%

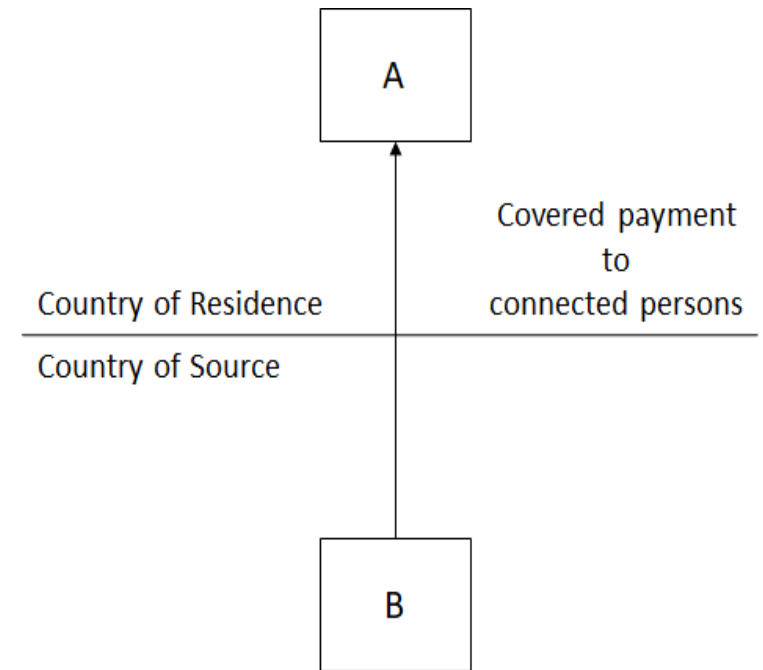
UTPR Taxpayers	Proportion of net intra-group expenditure	Allocated top-up tax
A1 Co	58%	$58\% \times 275 = 159.5$
A2 Co	8%	$8\% \times 275 = 22$
B Co	34%	$34\% \times 275 = 93.5$
Total	100%	275



Subject to Tax Rule

Subject to Tax Rule [STTR] - scope

- Targets cross-border intragroup payments (**connected persons**) that exploit certain treaty provisions
- Enables source jurisdiction to protect itself against base eroding payments to no or low tax jurisdictions and bring back taxing rights
- Scope of STTR :
 - Applied to cross-border payments between connected persons (excludes payments made to or by individuals)
 - Covered payments - These include interest, royalties and the following other payments (**related to mobile risk, asset or capital**):
 - a. A franchise fee or other payment for the use of or right to use intangibles in combination with services;
 - b. Insurance or reinsurance premium;
 - c. A guarantee, brokerage or financing fee;
 - d. Rent or any other payment for the use of or the right to use moveable property;
 - e. Consideration for the supply of marketing, procurement, agency or other intermediary services
- **Excludes payments** falling within those categories where the payment generates a low return (**low-return payments**). Cost plus basis, and where the margin is no higher than an agreed percentage.
 - **Excluded entities** - investment funds; pension funds; governmental entities (including sovereign wealth funds); international organisations, and non-profit organisations
 - **Materiality threshold** - based on one or a combination of the size of the MNE group, a tiered EUR-value of covered payments, and the ratio of covered payments to total expenditures. (**Further technical work**)



STTR to be implemented through a separate standalone treaty provision



Implementation and Rule co-ordination

Implementation and Rule co-ordination

Rule order:

- STTR applies even if the MNE Group is subject to the IIR or the UTPR. By taking the tax charged as a consequence of the STTR into account in calculating the ETR of the payee, the GloBE rules effectively give priority to the application of the STTR.
- IIR applies in priority to the UTPR under the GloBE rules. Includes SOR
- UTPR

Implementation

- STTR and SOR - Require changes to existing bilateral tax treaties. Could be adopted through MLI under BEPS 15 or a new multilateral convention
- IIR and UTPR - Can be implemented by way of changes to domestic law

Effective co-ordination of the GloBE rules

- Model legislation and guidance
- Multilateral review process
- New Multilateral convention

Dispute prevention and resolution

Pillar One and Two

High Level Comparison

Parameter	Pillar One	Pillar Two	
		GloBE	STTR
Threshold	Eur 750mn	Eur 750mn	Materiality to be determined
In scope businesses	ADS + CFB	All	
Specific exclusions	Financial services, Natural resources, Construction, International airlines and shipping	International Shipping (?)	
Excluded entities		Pension Fund, Investment Fund, SWF etc.	
Determination of income at	Group level (UPE)	Group level (at the top or nearer to the top)	
Assessment of income at	Group level (UPE)	Jurisdictional and entity level	Entity level
Compliance at	Group level (UPE)	Jurisdictional and entity level	Entity level

The provisions of the bilateral tax treaties are getting amended through MLI. We have DST/EL for digital businesses. GAAR/SEP provisions are already there in the law. Is there an overdose of anti-abuse provisions? Is Pillar 2 solution required at this stage?

(Select one of the options flashing on the right panel to respond)

- Yes, the complete tax system should be reformed once and for all
- No, but the collective thinking of 137 countries in the Inclusive Framework should be respected
- Yes, but it should not increase the compliance burden for on the tax payers
- No, Pillar 2 is not required at this stage. We should wait for the effect of other anti-abuse measures to be realised



Appendix

GLOBE Tax Base

calculated by reference to consolidated financial accounts

Determine tax base in accordance with financial accounting standard

- The starting point for determining the GloBE tax base is the profit (or loss) before income tax as determined using the relevant financial accounting standard.
- GloBE tax base to be calculated on the basis of the financial accounting standard used by the parent in the preparation of its consolidated financial statements.
- The acceptable financial accounting standards are IFRS and any equivalent financial accounting standard

Some adjustments to the tax base

- Exclude **dividends received from a corporate entity**, except dividends on stock in corporations in which the MNE Group owns a low percentage of the equity interests (portfolio dividend), and profit (or loss) attributable to an investment in an entity accounted for using the equity method of accounting.
- Exclude intercompany items to the extent the transaction is between group members in the same jurisdiction, cross border transactions to be taken at ALP
- Exclude gains and losses arising under fair value accounting for stock to the same extent gain or loss on actual sale of the stock would be excluded.
- Exclude stock-based compensation expense for a jurisdiction to the extent it is allowed as a deduction in the local tax base of the jurisdiction of the entity that employed or contracted with the party receiving the stock-based compensation
- No deduction for bribes, kickbacks (and other illegal payments), fines, penalties (limit of Eur 50,000)
- Policy holder's earning of an insurance company
- Adjustment for Pillar One Outcomes

Application of IIR

IIR Credit and Utilisation of IIR Credit by UPE / Shareholder

Excess Tax - Excess taxes are defined as the amount of covered taxes reflected as due and payable in the tax returns of Constituent Entities in respect of a year in excess of the minimum tax rate on the aggregate GloBE tax base for a jurisdiction for that year.

IIR tax credit - Excess taxes in a jurisdiction create an IIR tax credit to the extent of IIR tax paid in the preceding years in respect of the same jurisdiction that has not given rise to an IIR tax credit. An IIR tax credit can be used to reduce the shareholder's IIR tax liability in respect of any jurisdiction arising in the year the IIR tax credit was created or any subsequent year.

IIR tax credit can be used by the shareholder across jurisdictions.

IIR tax will lapse if not converted into IIR credit within prescribed time

IIR tax credit can be carried forward without any restriction.

	State B		State C	
	Subsidiary B		Subsidiary C	
	Year 1	Year 2	Year 1	Year 2
Income	1,000	400	1,000	1,000
Local tax paid	0	100	100	20
Minimum tax (10%)	100	40	100	100
IIR Tax (top up to 10%)	100	0	0	80
IIR tax credit used	0	0	0	60
IIR Tax Paid	100	0	0	20
Excess taxes (local tax – min tax)	0	60	0	0
Local tax carry-forward (excess tax – IIR tax credit created for year)	0	0	0	0
UPE – State A				
IIR tax paid (aggregate)	100	40	0	20
IIR tax credit	0	60	0	0

Potential IIR credit

IIR on timing differences gets mitigated

Application of IIR

Local tax carry forward, Loss Carry forward and post-filing adjustment

Local tax carry-forward - Excess taxes in a jurisdiction that do not create an IIR tax credit create a local tax carry-forward that may be carried forward an agreed number of years and treated as tax expense for that jurisdiction in a subsequent year in which the local tax paid by the Constituent Entities falls below the minimum tax rate on their aggregate income.

Post-filing adjustments to tax liability - For purposes of computing the GloBE ETR of the income assigned or allocated to a jurisdiction, post-filing increases (or decreases) to a Constituent Entity's liability for a covered tax are treated as adjustments to the entity's tax expense or carry-forwards in the year in which the tax increase (or decrease) is finally determined.

Loss carry-forward

Pre-regime loss carry forward

Subsidiary A	Year 1	Year 2	Year 3
Income	1,000	1,000	1,000
Minimum tax (10%)	100	100	100
Local tax paid (Jurisdiction A)	140	80	50
Excess taxes	40	0	0
Local tax carry-forward used	0	20	20
Local tax carry forward remaining	40	20	0
GloBE Tax (top up to 10%)	0	0	30

Timing differences get mitigated

Formulaic substance-based carve-out

- Carve-out amount = sum of the **payroll component** and the **tangible asset component**.
- If the carve-out amount exceeds the GloBE income in the relevant period, the excess amount cannot be carried-forward to reduce future GloBE income.
- The policy rationale behind a formulaic carve-out based on expenditures for payroll and tangible assets is to exclude a fixed return for substantive activities within a jurisdiction from the scope of the GloBE rules.
- Conceptually, excluding a fixed return from substantive activities focuses GloBE on “excess income”, such as intangible-related income, which is most susceptible to BEPS risks
- **Payroll component** = [x]% of the eligible payroll costs of eligible employees
- Eligible payroll costs include expenditures for salaries and wages as well as for other employee benefits or remuneration such as medical insurance, payments to a pension fund or other retirement benefits, bonuses and allowances payable to eligible employees and stock-based compensation. Eligible payroll costs also includes payroll taxes (or other employee expense-related taxes such as fringe benefits taxes), as well as employer social security contributions.
- **Tangible asset component** = sum of:
 - [x]% of the depreciation of property, plant and equipment
 - [x]% of the deemed depreciation of land
 - [x]% of the depletion of natural resources
 - [x]% of the depreciation of a lessee’s right-of-use tangible asset.

Carve out to remain focused on situations where BEPS concerns are high (intangibles etc.)

IIR - Simplification Options

- Many MNEs stressed that simplification measures are needed to reduce the complexity and administrative burden associated with complying with the GloBE rules, particularly in the context of jurisdictional blending
- IF has explored the following simplification measures to deal with this:
 - a. Country-by-country reporting ETR safe-harbour**
 - If the jurisdictional ETR based on the CbC report was above a certain threshold, which could be set above the agreed minimum rate, then no further work would be required for that jurisdiction.
 - b. De minimis profit exclusion;**
 - excluding jurisdictions from the GloBE rules which have less than a certain percentage of the MNE Group's pre-tax profit.
 - c. Single jurisdictional ETR calculation to cover several years;**
 - in the case that the ETR of a particular jurisdiction exceeded a certain threshold rate (in the base year or any subsequent year) then the MNE would not be required to compute the ETR for that jurisdiction for the next 3-5 years (the grace period).
 - d. Tax administrative guidance**
 - tax administrations would publish guidance (developed within an Inclusive Framework process) that set out jurisdictions deemed to be low-risk and then MNEs would not be required to perform the ETR calculation for those jurisdictions
- These simplification measures could be applied at the election of the taxpayer and could be layered on top of one-another such that multiple simplification measures could be applied simultaneously.

Undertaxed Payment Rule - Theory

- UTPR taxpayer - Any CE that is located in a jurisdiction that has implemented the UTPR in accordance with the GloBE rules (a UTPR Jurisdiction). Applies in respect of the income of low-tax CEs
- The IIR has priority over the UTPR
- Serves the following hybrid purpose:
 - as a backstop to the IIR and reduces the incentives for tax driven inversions by providing a mechanism for making an adjustment in respect of any remaining top-up tax in relation to profits of a CE that is not in scope of an applicable IIR.
 - Addresses base erosion through deductible intra-group payments.
- Applies to the profits of a low-tax CE where such low-tax CE is controlled by another foreign Constituent Entity that is not subject to an IIR in accordance with the GloBE rules
- Uses the same mechanics as the IIR for determining the MNE's jurisdictional ETR and the amount of top-up tax allocable under the rule.
- 1st allocation key – Proportion of direct payments to the low-tax CE during the relevant period.
- 2nd allocation key – Proportion of net intra group payments
- *Cap on top-up tax to be allocated = Domestic covered tax rate applicable in the jurisdiction of the UTPR Taxpayer * gross amount of payment*
- No top-up tax is allocated under the UTPR to low-tax Constituent Entities.
- Balance top-up tax liability to be carried forward for recovery / adjustment in future year
- **Domestic law mechanism** - The GloBE rules do not prescribe the mechanism by which UTPR adjustment must be made. This is a matter of domestic law implementation that is left to the jurisdictions that choose to adopt the UTPR. The adjustment could be through a limitation or a denial of a deduction for payments made to related parties or could be in the form of an additional tax.
- **Information requirement** - necessary to ensure that the UTPR Taxpayers and the MNE will provide the information necessary to compute and allocate the top-up tax

Compliance and administration of the UTPR

- **Certification requirements in instances where the UTPR should not apply**
 - Certification that no adjustment required under UTPR due to prior application of IIR
 - Certification that no adjustment required because ETR is at or above the agreed minimum rate
 - Certification that intra-group payments cannot result in allocation of top-up tax
- **Standardised self-assessment UTPR return to be filed by the taxpayer with the tax administrations:** Could contain information like:
 - A list of all jurisdictions in which the MNE has CEs and the MNE's jurisdictional ETR in each of these jurisdictions, as well as the balances in the pools of carry-forwards for losses, local taxes and IIR tax credits;
 - Total amount of top-up tax arising in that period for jurisdictions where the MNE's jurisdictional ETR is below the agreed minimum rate, which would be computed based on the net income and taxes paid in each jurisdiction where the MNE operates;
 - Total amount of intra-group payments made by each UTPR Taxpayer to each low-tax CE;
 - Total amount of top-up tax imposed in the year as a result of the first allocation key;
 - If there is top-up tax remaining after this first allocation, the net intra-group expenditure of each UTPR Taxpayer
- **Local filing of the relevant information** - UPE could prepare the certifications or standardised self-assessment returns and provide them to each tax administration in jurisdictions where it has a CE, on behalf of its Constituent Entity, as it would be in a better position to compile the same. UTPR Taxpayer would however remain responsible to the local tax administration for providing any document/information

Subject to Tax Rule

Operation and effect

Adjusted nominal rate trigger

- Triggered when a payment is subject to a (an adjusted) nominal tax rate in the payee jurisdiction that is below the minimum rate, after adjusting for certain permanent changes.
- Central publicly available database of adjusted nominal tax rates for jurisdictions (further work)

Using a top-up approach

- Allow the payer jurisdiction to apply a top-up tax to bring the tax on the payment up to an agreed minimum rate; (e.g. if agreed minimum rate is 12%, adjusted nominal rate is 7%, top-up rate for withholding would be 5%)
- The top-up rate could be set at a rate that is lower than the minimum rate agreed for the income inclusion and undertaxed payments rules. (gross taxation concerns)
- Where treaty already provides taxing rights to the source country (ordering rule)

Treaty obligation of the country of residence

- Article 23A to be switched off, when the source country exercises taxing right under STTR

Subject to Tax Rule

Administrative concerns

Further work is being done on:

- applying the top-up tax as an ex-post annualised charge;
 - On recipient
 - Payer
 - Administrative / collection concerns
- a certification system providing for reduced rates of withholding tax; and
- the application of contingent withholding taxes set at a level that would generally result in an annual ex-post balancing payment by the taxpayer (rather than a repayment).

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