OECD releases Pillar Two GloBE Rules Administrative Guidance and GloBE Information Return

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In brief

The OECD/G20 Inclusive Framework on BEPS (IF) released a number of documents relating to the Two-Pillar solution on 17 July 2023, one of which was a second set of Administrative Guidance on the Pillar Two GloBE Model Rules. This release (the guidance) follows the publication of the first set of Administrative Guidance in February 2023. The guidance covers a range of issues where stakeholders sought additional clarity, including the Qualified Domestic Minimum Top-up Tax (QDMTT) and Transitional UTPR Safe Harbours, the treatment of transferable tax credits, application of the Substance Based Income Exclusion (SBIE) and others. The guidance, including more detailed examples, will be incorporated into a revised version of the Commentary that will be released later this year. Also released as part of the OECD package was an updated version of the GloBE Information Return (GIR).

The takeaway: The guidance brings greater clarity on matters including transferable credits, the provision of two new safe harbours and the application of the QDMTT to entities other than constituent entities of an MNE Group. However, questions remain in terms of the benefits of some of the transitional reliefs, other unresolved transition issues, the practical application of the currency conversion rules, and of course whether countries will incorporate this latest guidance into their local GloBE rules implementation.

In detail

UTPR Safe Harbour

The guidance provides a new safe harbour designed to provide transitional relief from the UTPR in the ultimate parent entity (UPE) jurisdiction during the first two years in which the GloBE Rules come into effect (the Transitional UTPR Safe Harbour). Under the Transitional UTPR Safe Harbour, the UTPR Top-up Tax amount calculated for the UPE jurisdiction shall be deemed to be zero for each fiscal year during the transition period if the UPE jurisdiction has a corporate income tax rate of at least 20% based on the nominal statutory rate and accounting for sub-national taxes.

The transition period refers to the fiscal years which run no longer than 12 months that begin on or before 31 December 2025 and end before 31 December 2026. The guidance states that an MNE Group that qualifies for more than one transitional safe harbour may choose which safe harbour to apply for that jurisdiction. Importantly, the Transitional UTPR Safe Harbour does not turn off the “once out, always out” approach that applies, for example to the CbCR Safe Harbour (i.e., if a business has not qualified for the transitional CbCR Safe Harbour in a country in one year, it cannot use that safe harbour for that country in a subsequent year).

Observation: The guidance provides that the transition period under the Transitional UTPR Safe Harbour will not be extended. It is important for MNE Groups to determine whether they can qualify under more than one transitional safe harbour and possibly elect to apply the Transitional CbCR Safe Harbour in lieu of the Transitional UTPR Safe Harbour since the Transitional CbCR Safe Harbour may apply to fiscal years commencing on or before the end of the 2026 (i.e., one fiscal year after the Transitional UTPR Safe Harbour).

QDMTT Safe Harbour

The guidance contains a QDMTT Safe Harbour which operates by setting the Top-up Tax to zero for a jurisdiction when an MNE Group qualifies for the safe harbour in that jurisdiction. The safe harbour, when applicable, eliminates the need for an MNE Group to undertake a second calculation under the GloBE Rules after completing the QDMTT calculation. For a jurisdiction’s QDMTT to qualify for the QDMTT Safe Harbour it must meet three standards in addition to the existing QDMTT rules and guidance: (1) the QDMTT Accounting Standard; (2) the Consistency Standard; and (3) the Administration Standard.

The Accounting Standard requires that a jurisdiction base its QDMTT upon either the financial accounting standard of the ultimate parent entity (UPE) or a local financial accounting standard. If the local financial accounting standard is selected by the implementing jurisdiction, there are certain limitations in applicability (e.g., if the local financial statement year differs from the consolidated financial statement year, then the local financial statement cannot be used as the base for the QDMTT). Further, if the local financial accounting standard is selected by the jurisdiction, the MNE Group cannot deviate and use consolidated financial statements. The Consistency Standard requires that the QDMTT computations be the same as those required under the GloBE Rules, except where QDMTT guidance requires a deviation or allows for optionality. Lastly, the Administration Standard requires that the QDMTT jurisdiction continue to meet requirements of a continuous monitoring process with respect to the QDMTT.

Whilst the QDMTT Safe Harbour qualification is considered on a jurisdictional basis, it is acknowledged that in certain instances a jurisdiction may not be able to apply the QDMTT to certain enterprises or constituent entities (CEs). To cater for this, the Consistency Standard prescribes specific circumstances in which the non-application of a QDMTT is allowed and instead a Switch Off Rule applies such that the MNE group benefitting from the non-application of the QDMTT cannot benefit from the QDMTT Safe Harbour.

Observation: The QDMTT Safe Harbour applies a more stringent standard to a QDMTT than the general QDMTT guidance published in February, in that it requires the QDMTT to use the same computations as required under the GloBE Rules, except as specifically authorised by Administrative Guidance or the IF. The QDMTT Safe Harbour, however, allows a jurisdiction to legislate a QDMTT that uses a local financial accounting standard, which may yield different Top-up Tax results than those computed under the GloBE Rules – and potentially greater complexity between jurisdictions. Lastly, the need for a peer review process to determine whether a jurisdiction's QDMTT qualifies for the safe harbour introduces uncertainty as to how extensive a relief this will be.

Tax Credits including Transferable Credits

The guidance introduces Marketable Transferable Tax Credits (MTTCs) as a new category of tax credits (in addition to QRTCs) that are taken into account as part of GloBE Income rather than a reduction of Covered Taxes.

In respect of a purchaser of a tax credit, only the net benefit from the credit is included in GloBE Income (if an MTTC) or treated as a reduction of covered taxes (if a transferable credit other than an MTTC). To qualify as an MTTC, a tax credit must satisfy a legal transferability standard and a marketability standard, which are determined separately for tax credit originators and purchasers. In general, the legal transferability standard is met if the credit can be transferred by the originator or purchaser to an unrelated party. The marketability standard is generally met if the credit is transferred by the originator or from the purchaser at a price at least 80% of the net present value of the credit.

The guidance also clarifies certain ambiguities in the original Commentary and prior administrative guidance relating to tax credits. It modifies the timing for taking into account Qualified Flow Through Tax Benefits (QFTBs) and the definition of Qualified Ownership Interests (QOIs) through which QFTBs are received. The guidance also permits, in limited circumstances, alternative timing for including QRTCs as taxable income in GloBE Income. The guidance provides that tax credits that do not qualify as QRTCs or MTTCs but that are nonetheless treated for financial accounting purposes as income rather than tax reductions (for example tax credits refundable after 4 years) must be subtracted in full from the computation of GloBE Income or Loss. The guidance also clarifies that tax credits that do not qualify as QRTCs or MTTCs are treated as reductions to Covered Taxes, and Covered Tax refunds that are credited against another Covered Tax liability are treated as reductions to Adjusted Covered Taxes.

Observation: The introduction of MTTCs is a significant development in respect of transferable credits, confirming that, in many cases, those credits will be treated as additional income rather than a reduction of Covered Taxes by a transferring originator and will be taken into account by a purchaser only to the extent of the purchaser’s net benefit. Nevertheless, taxpayers should carefully consider whether their transferable tax credits satisfy the detailed definitions in the guidance, and it remains to be seen whether all countries will transpose this into their national laws.

Observation: The guidance does not modify the eligibility criteria or treatment (other than the timing of inclusion in income) for a QRTC, but it does call for consideration of further guidance to address transitional issues and deferred tax implications in respect of QRTCs and other tax credits.

Substance Based Income Exclusion (SBIE)

The guidance contains amendments to the original Commentary with respect to the application of the SBIE. Specific issues addressed are (1) interjurisdictional assets and employees, (2) simplification, (3) stock-based compensation, (4) leases, (5) impairment losses, and (6) reductions due to Article 7.2 (i.e., UPE subject to Deductible Dividend Regime.)

The guidance provides simplification provisions in the case of payroll and assets used in more than one jurisdiction, allowing for full carve-out where more than 50% of Eligible Employee or Eligible Tangible Assets are located in the CE jurisdiction, as well as claims for some, but not all, of the Eligible Payroll Costs and Eligible Tangible Assets for a jurisdiction. The guidance also confirms that adjustments for stock-based compensation when calculating Eligible Payroll Costs will not be affected by an Article 3.2.2 election.

A lessor will be allowed to include a portion of the carrying value of operating leases of Eligible Tangible Assets for the SBIE calculation if those assets are located in the same jurisdiction as the lessor. While this is beneficial from a lessor perspective, there are detailed requirements to compute the qualifying portion.

The guidance also clarifies the treatment of impairment losses when calculating the carrying value of Eligible Tangible Assets, aligning the treatment and timing of recognition of impairment losses for financial statement purposes with the SBIE. It has also been clarified that there will be a proportionate reduction in the Eligible Payroll

Costs and carrying value of Eligible Tangible Assets referable to an amount that has been excluded from the GloBE Income of a UPE pursuant to a Deductible Dividend Regime under Article 7.2.

QDMTT

The guidance supplements the February Administrative Guidance in respect of QDMTTs by providing clarifications and addressing specific issues identified therein. The guidance covers the application of the QDMTT mechanism for entities such as joint ventures, joint venture subsidiaries, minority owned constituent entities, flow through entities (FTEs) and flow-through UPEs, as well as for scenarios such as an eligible distribution tax system.

The guidance also includes new filing obligations for a QDMTT jurisdiction, specifically by allowing a QDMTT jurisdiction to collect the data points required to compute the GloBE tax liability in a format other than the GIR.

The guidance indicates that any direct or indirect challenge to the application of a QDMTT by the MNE Group based on constitutional grounds or under an international investment agreement (or based on a specific agreement with the government) means that the amount challenged shall not be treated as QDMTT payable. The Top-up Tax payable under the QDMTT will not reduce the GloBE Top-up Tax to zero and thus may be collected by another jurisdiction under the GloBE Rules.

Observation: This treatment appears to undercut the OECD's founding treaty in respect to the commitment by its (founding) members to act "in a manner consistent with their obligations in other international organisations or institutions in which they participate or under agreements to which they are a part."

Currency conversion

To ensure effective adoption of the GloBE Rules, the guidance addresses four specific issues in relation to currency conversion for the relevant calculations undertaken by MNE Groups. These issues are:

- The currency in which GloBE calculations and GIR disclosures should be made: MNE Groups will be required to perform the GloBE calculations and report amounts within the GIR in the presentation currency of the MNE Group's consolidated financial statements;

- The translation of amounts relevant to GloBE calculations into the presentation currency: MNE Groups must use the applicable foreign currency translation rules (i.e., the equivalent of IAS 21 or ASC 830, and other relevant parts) in the Authorised Financial Accounting Standard used to prepare their consolidated financial statements to compute the financial accounts net income and loss, or other relevant GloBE;

- The currency translation rules applicable for translating any Top-up Tax under the IIR or the UTPR Top-up Tax amount from the presentation currency into the currency in which the GloBE tax liability is payable: In this case, jurisdictions may choose a reasonable basis for conversion (examples are provided), but the guidance recommends adopting specific rules into legislation to give MNE Groups compliance certainty; and

- The differences between the presentation currency of an MNE Group and the currency in which certain GloBE thresholds are stated in domestic law: The relevant amount must be translated from the presentation currency to the currency used in domestic law based on the average exchange rate, generally the European Central Bank rate, for the December prior to the relevant calendar year (i.e., in which the relevant fiscal year starts). This rule is limited to determining whether a threshold has been exceeded, not for translation of the underlying amounts for purposes of the GloBE computations and aligns with the requirement provided for in previous guidance that GloBE monetary thresholds be annually rebased in Euros from local currencies.

- Currency translation rules for QDMTT computations: guidance was also provided for currency translation in QDMTT computations in three scenarios (1) where the QDMTT is determined using the accounting standard and presentation currency of the UPE, (2) where the QDMTT is determined using a local accounting standard and all relevant Constituent Entities use the same local functional currency, and (3) where there are multiple functional currencies used among a group of Constituent Entities in a QDMTT jurisdiction.

GloBE Information Return (GIR)—a separate but related release

Separate from the guidance, the IF also released the GIR. As outlined in our prior Tax Policy Alert, the information potentially required to be reported that was contained in the December 2022 GIR Consultation Document could have been incredibly burdensome, notably the detail required for the CE computation in Section 3.4 of the GIR.

The updated GIR provides for a transitional simplified jurisdictional reporting framework (Simplified Framework), as a temporary measure that allows for simplified reporting for all fiscal years beginning on or before 31 December 2028 (but not including a fiscal year that ends after 30 June 2030). Under the Simplified Framework, the MNE Group is generally not required to report adjustments to financial accounts net income and loss, current tax expense, or deferred tax expense on a CE-by-CE basis and all adjustments can be reported on a net basis. The Simplified Framework is only allowed for jurisdictions where either (1) no Top-up Tax liability arises or (2) Top-up Tax liability arises, but it does not need to be allocated on a CE-by-CE basis.

The IF has adopted a “targeted” dissemination approach for sharing information about each MNE Group, whereby:

- The UPE jurisdiction is provided with the entire GIR;
- Jurisdictions with taxing rights under the GloBE Rules are provided with relevant sections of the GIR; and
- All CE implementing jurisdictions are provided with general information and the corporate structure.

The Simplified Framework will not limit any rights of tax authorities to request additional information.

Observation: The Simplified Framework will be a welcome change, but questions remain whether future, more permanent changes may be made. If that does not become apparent relatively soon, then the benefits of the Simplified Framework could be negated as businesses feel the need to make ERP data collection system changes well before the end of the transitional period. It is also worth noting that the guidance makes clear that tax authorities can always request more detailed CE level data, so, again, the benefits of this provision may be reduced in practice.

PwC’s Tax Readiness Webcast: The current state of the OECD's two-pillar solution

While there is uncertainty around Pillar One (both on the timeline and on whether a critical mass is achievable), many countries have begun implementing Pillar Two, and the OECD IF continues to release substantive guidance in key areas. Join our CPE-eligible webcast for the latest updates on the OECD's two-pillar solution.

July 27, 2023 from 11:00 AM – 12:00 PM ET

Register today

Consult PwC’s Pillar Two country tracker to learn more about individual jurisdictional implementation of Pillar Two.

Let’s talk

For a deeper discussion of how Pillar Two might affect your business, please contact:

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