

# The OECD Proposal for a new tax order

Comments on the Public Consultation Document in respect of the  
Global Anti-Base Erosion Proposal ("GloBE") under Pillar Two



Do the proposals represent a new inclusive global grand bargain that will finally stem the tide of unilateral actions in our uncertain world?

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## Summary

The 2015 BEPS project updated international tax rules to deal with abusive base erosion and profit shifting tax avoidance. It left taxing rights of sovereign states untouched. Pillar One focused on defining a new nexus and reallocation of taxing rights focused on addressing digital business models with little or no onshore presence.

Pillar Two takes a massive step forward beyond addressing digital taxation and proposes a global minimum effective tax regime comprising of four component – income inclusion rule, undertaxed payments rule, switch-over rule and subject to tax rule. These co-ordinated set of rules are intended to address “ongoing risks from structures that allow MNEs to shift profit to jurisdictions where they are subject to no or very low taxation”.

Like the Four Horsemen of the Apocalypse, however, do these proposals spell the death knell of the post-war international income tax framework as we have come to know it - where bilateral treaties allocate taxing rights to avoid double taxation and countries abide by a set of commonly acceptance of OECD soft-law principles? Or do they represent a new inclusive global grand bargain that will finally stem the tide of unilateral actions in our uncertain world?

In the following, WTS Global takes you into deep into Pillar 2 with insights and analysis from our experts.

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## I Overall comments and fundamental issues

In this section we provide our overall comments in respect of the Consultation Document, and highlight our **key considerations** including feedback from industry and practitioners whom to we have spoken that constitutes overarching observations or fundamental issues. Our comments in Section I. start at the broad Policy and Principles level, followed by issues of Practical Implementation and finally technical comments that will flow smoothly into specific responses to your questions in the Consultation Document in the Section II.

### A Policy and Principles

#### A1 Lack of Global Coherence May Lead to a Conflict of Rules and Double Taxation

Our comments start at the broad policy and principles level because we believe the spirit of the Inclusive Framework is to foster open and objective debate and not limit this consultation exercise to technical details of Pillar 2.

The Pillar 1 and 2 proposals come at a time when the tax world is in the throes of implementing the base erosion and profit shifting project (**BEPS**) changes, digesting the recently finalized regulations from the US Tax Cuts and Jobs Act (**TCJA**) and wrestling with digital disruption, not just new rules such as the digital services tax but also having to invest in the digitalization of systems, tax compliance processes and tax administration.

These are common challenges facing tax administration, tax advisors and taxpayers. Therefore, to the common refrain of double taxation and heavy compliance costs imposed on industry, it must be added that it is in the common interest of all stakeholders, including tax administrators, for there to be a coherent, administrable and practicable set of international taxation norms.

Whilst it is desirable to head off growing tendencies toward unilateral actions notwithstanding, we humbly submit that it is just as important that there shall be global coherence in international taxation framework and principles.

The post-war international income taxation framework has largely been constituted by some 3,000 bilateral

treaties and commonly agreed norms such as permanent establishment and transfer pricing based upon on OECD guidance. BEPS has gone a long way toward updating the framework and the underlying principles to address abuses such as cash box Intellectual property holding entities and double non-taxation. The US tax reform of 2017 has opened up significant areas of divergence with BEPS. Pillar 1 adds to these differences by introducing new norms such as digital nexus and allocation of "market taxing rights" beyond the arm's length principle that has yet to be reconciled with the BEPS Actions 7 and 8-10 principles. The GloBE will add another layer of complication and divergence. For example, there are overlaps and gaps between GloBE and TCJA's Global Intangible Low-Taxed Income (GILTI) provisions. The issue of how the Pillar 1 unified approach and Pillar 2 operate vis-à-vis each other is also a consideration. Take for example royalty payments, which are made to the global group parent as the owner of the Intellectual Property. The way we understand the unified approach, at least parts of that royalty income will be part of the deemed residual profit, which should be allocated to market jurisdictions, where it will be taxed according to the respective local tax law. Nevertheless, the group companies originally paying the royalty to the group parent somehow must determine, whether their royalty payments will be subject to the – yet to be determined – minimum level of effective tax.

The crux of the problem is that these overlapping measures, if left uncoordinated and unreconciled, can lead to conflicts between the different Pillars and with pre-existing EU and BEPS measures, resulting in double taxation. For instance, should countries already operating an effective minimum tax system be carved out or be regarded as a safe-harbour in lieu of the GloBE? Should the US legislate 15% as suggested in the examples in the Consultation paper on top of GILTI's 13.125%? The current dispute resolution mechanisms in international taxation have some way to go before achieving the efficacy exposed by BEPS Action 14. Therefore, these overlaps should be discussed and reconciled before GloBE is introduced rather than they be left to Competent Authority resolution. The reconciliation process can be complex and involve prolonged negotiations. For instance, should the GloBE trump any domestic rules or should it be a requirement of the global consensus that any domestic tax measures contrary to the GloBE be abolished?

A further policy observation is that the GloBE runs counter to the common Controlled Foreign Corporation policy of excluding income from active businesses and the general global trend of international taxation moving towards a more territorial basis of taxation.

### **A2 Too Broad a Mandate Makes Global Consensus Harder to Achieve and Implement**

The broadening of the mandate of Pillars 1 and 2 to cover issues left unaddressed by BEPS makes it harder to achieve and implement a workable global consensus than a more narrowly focused initiative to address perceived abuses by a small group of digital companies. It unnecessarily increases the compliance burden and costs for the vast majority of compliant taxpayers who are not engaged in aggressive tax planning.

More generally, before the impact of BEPS Action 1 and Pillar 1 are fully understood, countries may be unsure if they are net winners or losers from the overlapping measures. Constituents who may have been willing to support targeted measures against the most serious abuse may hesitate to endorse broad measures that impose administrative and compliance costs across a wide swathe of otherwise compliant taxpayers. This may result in the more disconcerting outcome where some countries may cherry pick amongst the various global and supra-regional measures and combine them with unilateral domestic measures in a way that leads to incoherence and double taxation. The importance of quantifying the impact to individual countries is particularly necessary for EU member countries as any such tax measure will need unanimous consent. Therefore, more data and a fuller impact assessment will likely be requested by member states before they agree to adopt and implement Pillar 2.

### **A3 Lack of Clarity in Policy Objectives Can Lead to Unintended Consequences and Undermine Tax Certainty**

Pillars 1 and 2 in reallocating taxing rights between sovereign states have already departed from the BEPS project objective of preventing double non-taxation by updating and sharpening international tax rules but leaving sovereign taxing rights untouched. Pillar 1's proposals applicable to digital business models has similarly moved beyond the BEPS Action 1's position that the digital economy cannot be ring-fenced. Further, there is ongoing assessments of preferential tax regimes

conducted by the Forum on Harmful Tax Practices (FHTP), comprising of the same 130 member jurisdictions of the Inclusive Framework.

A key concern is the sweeping application of the four component parts of the GloBE – income inclusion rule, undertaxed payments rule, switch-over rule and subject to tax rule to all businesses beyond taxing digital businesses which was the original intent when the Task Force for Digital Economy was set up. This is regardless whether such taxpayers have engaged in abusive transactions or avoidance.

We submit that greater clarity and transparency as to the policy intent of Pillar 2 would benefit all stakeholders. It is unclear what precise "ongoing risks" or "structures" Pillar 2 seeks to cover in seeking the "development of a co-ordinated set of rules to address ongoing risks from structures that allow MNEs to shift profit to jurisdictions where they are subject to no or very low taxation"<sup>1</sup> that is not already addressed by the measures in BEPS, Pillar 1 and the FHTP, not to mention the other multilateral measures proposed by the EU and individual country general and specific anti-avoidance provisions. Perhaps it would be useful to share the varied points of views of different countries and stakeholders as this can help bring balance to the deliberations. We observe for instance, that the Programme of Work<sup>2</sup> mentioned that some members consider that the current BEPS measures do not yet provide a comprehensive solution for BEPS whilst the same document states in a footnote that other members are of the view that the rules explored in Pillar 2 may encroach upon the sovereignty of jurisdictions as states may have different reasons to subject certain income to lower tax rates<sup>3</sup>.

Even if such risks or structures can be accurately delineated, there is a trade-off between precision and administrability. Adopting the more precise jurisdictional or entity blending approach and crafting detailed guidance for the GloBE to target these identified abuses for instance, would come at a cost of the advantage of a simple and administrable worldwide blending regime that is uniformly applied.

1 See page 3 of the Public consultation document Global Anti-Base Erosion Proposal ("GloBE") (Pillar Two).

2 Programme of Work, 28 - 29 May 2019 at Point 53 on page 25.

3 Programme of Work, footnote 2 at page 33.



This lack of coherence and coordination in the policy objectives amongst the various international tax reform measures can lead to significant unintended consequences and significantly undermine tax uncertainty. For example, countries have environmental "green" tax measures to encourage the development, manufacture and deployment of low emission vehicles, clean energy and even energy efficient datacenters for the digital companies. A GloBE minimum tax can undermine the policy objectives of these measures if the post-incentivised low effective tax rates, that is needed to spur green investments, fall under the agreed threshold.

As another illustration, a country may have been applying certain tax measures in good faith on the basis that such measures have been given a clean bill of health by the FHTP in its peer review process. Similarly, taxpayers have restructured their business affairs in reliance on such tax measures having been acceptable to the FHTP under international standards. A GloBE minimum tax may overturn all of this, including the findings of the FHTP merely because the effective tax rate mechanically falls under the threshold.

From a macro-economic perspective, Pillar 2 may be perceived as an attack on Capital Import Neutral (CIN) tax systems, as opposed to Capital Export Neutral (CEN) tax systems. The discussion between CIN and CEN has always been around in international taxation. Pillar 2 goes to the heart of that discussion thus it is surprising to find scant reference to this aspect in the Programme of Work and the Consultation Document. Further, certain regulated industries such as financial services and insurance have had long-standing structures operating in certain offshore jurisdictions. The global economy depends on the efficient deployment of capital to where is it most productively used and the business arrangements of the financial services industry is driven largely by prudential and regulatory requirements. Similarly, global supply chains follow shipping routes and commercial trading practices that have been facilitated by customs rates that have been regulated by the WTO and GATT regimes. The GloBE being a blunt policy instrument risks disrupting such long established arrangements and throwing sand onto the wheels of efficient capital and trade flows.

## B Practical Implementation

### B1 Increased Compliance Burden

The foremost question is whether the heavy compliance burden that a GloBE will impose on all stakeholders is necessary, commensurate with the "harm" and effective given the nature and extent of the avoidance.

Before meaningfully answering the question, the policy intent of GloBE needs first to be clearly defined, followed by an assessment of how effective the other measures - BEPS, Pillar 1, ATAD, etc have been in addressing the problem, what elements of abusive behaviour remains and whether GloBE remains the most appropriate tool to target it.

### B2 Transmission Mechanism

Next, the appropriate transmission mechanism for implementation, in case should GloBE be adopted, needs to be considered. Apart from unilateral adoption, bilateral agreements (which will e.g. need to be amended due to the likely conflict between the GloBE under-taxed payment rule and the cost-deduction non discrimination rule of Article 24, Para. 4, of the OECD Model Tax Convention), the main multilateral "transmission" mechanisms to effect any global measure such as BEPS comprises mainly of the tax treaties and commonly accepted soft law guidance from the OECD such as the model convention, the transfer pricing guidelines and BEPS type recommendations that are not commonly endorsed minimum standards. The limitations of OECD soft-law guidance as a transmission mechanism is apparent from past experience where for instance, the adoption of the Authorised OECD Approach in the attribution of profits to permanent establishment, now a decade old, remains uneven.

### B3 Emerging Economies

Having member firms around the world, we are more acutely aware of the capacity constraints faced by emerging economies. According to a McKinsey study<sup>4</sup> for instance, the share of large companies with turnover of more than one billion US dollars that are family owned

<sup>4</sup> Åsa Björnberg, Heinz-Peter Elstrodt, and Vivek Pandit, "The family-business factor in emerging markets", McKinsey Quarterly, Dec 2014 available at <http://www.mckinsey.com/global-themes/winning-in-emerging-markets/the-family-business-factor-in-emerging-markets>

can be as high as 70 – 80 percent in Latin America and 80 – 90 percent in South East Asia. These family owned multinational conglomerates, particularly if they are not listed and not obliged to follow IFRS will face significant challenges in complying with the proposals. Similarly, challenges exist for the advisors and tax administrators of emerging economies with limited capacities to properly advise on and administer complex rules. An undesirable consequence may be that valuable resources are diverted from other measures such as digitalization of VAT receipts and bringing the domestic shadow economy into the tax base that may be more efficacious in raising revenue.

In relation to the point above about the efficacy of OECD transmission mechanisms, it is worth noting that in emerging Asia for instance, there are only 4 OECD member countries out of 48 countries recognized by the United Nations with the latter exhibiting varying degrees of acceptance of OECD guidances. So even if the global consensus holds amongst the members of the Inclusive Framework, timing differences in adoption counted in years due to varying pace of adoption can lead to unintended arbitrage opportunities or double taxation prior to the changes being uniformly adopted.

#### **B4 Future Ongoing Maintenance**

Thinking through the ongoing modalities of implementation is non-trivial because of the lack of a supranational world body to maintain a GloBE system once it is implemented. Apart from the lack of effective dispute resolution mechanism, there is also a lack of a global enforcement mechanism should jurisdictions not implement, vary the implementation from what was intended or cherry pick certain parts of the proposals to be implemented.

For example, what if certain countries fail to introduce or inappropriately implement the GloBE or after several years, the threshold of 15% or the carveouts are deemed to be inappropriate? Will there be a need for the world to continually reconvene future Task Forces to deliberate and come to consensus? The lack of a supranational body with enforcement rights against non-compliance by state actors adds another dimension to the lack of effective dispute resolution mechanism to address double taxation.

#### **B5 Allowing More Time – Staggering the Change in Phases and Transitional Provisions**

It is submitted for the reasons explained above that implementation of any Pillar 2 consensus be spaced out over two or more phases, permitting both tax administrators, advisors and taxpayers to settle into the new BEPS regimes before embarking on further changes in Pillars 1 and 2. The experience of implementing the Country-by-country report shows that even years after the regime is rolled out, there are clarifications that are needed. Pillars 1 and 2 will be even more far-ranging and serious in its implications than the reporting requirement that is the Country-by-country report in the way it seeks to reorder the international tax framework for allocating taxing rights.

There should also be appropriate transitional provisions to address the need for tax certainty. A more deliberate pace of implementation will give time for the principles to be more fully developed and translated into legislation, regulations and implementation guidance. All stakeholders will have more time to adapt and adjust, resulting in increased levels of buy-in to these changes.

### **C Technical Comments**

#### **C1 Maintaining and Reconciling Different Tax Accounting Computations**

The proposed Pillar 2 approach seems to be based on the assumption that the financial accounts of an entity do not adequately reflect its effective tax burden. This then necessitates the introduction of a new set of computational rules which overlap with those provided by national tax and accounting rules. If each country continues to have its own rules for determining the corporate income tax base, the tax accounting compliance burden for taxpayers would be greatly increased. Each taxpayer entity may be compelled to maintain three or more different sets of tax accounting computations - one based on their national tax law and accounting rules, a second based on the revised segmentation and attribution rules of Pillar 1 and a third based on the envisaged GloBE blending and other convention. Even if Pillar 2 accepts the use of consolidated financial accounts as the basis for computation and the adjustments for temporary and permanent differences explained, experience in audits have shown that individual tax authorities will

still prefer to make their assessments based on local GAAP and tax computation rules. In this regard, the accounting convention of GloBE should take into consideration and accept the accounting basis upon which taxpayers have relied on in preparing their Country-by-country reports. This is not least to avoid auditor confusion over different views of a multinational enterprise's (MNE) worldwide tax profile presented under different accounting conventions. Following the Country-by-country reporting rules, a pragmatic way to address concerns about taxpayer arbitraging between different accounting conventions can be addressed by requiring consistency across time once the taxpayer elects a certain set of accounts e.g. using local statutory accounts to compute effective tax rates.

### C2 Headquarters or Ultimate Parent Jurisdiction

In line with the Country-by-country reporting regime, it should be clarified that the accounting convention, the computation and administration of the GloBE should be the sole responsibility of the ultimate parent entity under the rules of the jurisdiction where the ultimate parent entity is tax resident. The potential issue of the jurisdiction of the ultimate parent entity not enacting or enforcing GloBE will have to be dealt with when considering the implementation modalities as unlike reporting obligations, additional income inclusion or denying deduction cannot be done by a surrogate entity.

### C3 Increased Book-Tax Difference

To the extent these proposals impact the IFRS or GAAP accounting in way as to broaden book-tax differences, it would be prudent that the financial accounting community at the national level and relevant international accounting bodies be engaged. This is not least so the Pillar 1 and 2 measures take into account and keep up with the broader global efforts in regard IFRS and GAAP convergence.

After providing the overarching policy, implementation and technical comments above, we will address the specific questions raised in the Consultation document hereafter in Section II. Our comments are therefore inherently limited to the GloBE proposal as referred to in the Consultation Document.

## II Our Specific Responses to the Questions raised in the Consultation Document

### BOX 1

- a Do you agree that the use of financial accounts as a starting point can provide an appropriate income base (for the computation of an effective tax rate) and would simplify and reduce the compliance costs of the GloBE proposal?
- b What would be the consequences of using the accounting standards applicable to the ultimate parent entity of the MNE? Would you suggest a different approach?
- c How would you recommend determining whether a financial accounting standard is an appropriate standard for determining the tax base under the GloBE proposal?
- d Do you have concerns that allowing more than one financial accounting standard to serve as the starting point for determining the tax base under the GloBE proposal will place some MNEs at a competitive advantage due to variations in financial accounting standards among jurisdictions?
- e There may be some instances where MNEs, particularly smaller MNEs, do not prepare consolidated financial statements for any purpose. How much of an issue do you think this is and for what types of MNEs? Where this is the case, how would you suggest the issue should be addressed?
- f Are there additional or different considerations that apply to the tax base determination for purposes of an undertaxed payments rule?

**1a** We believe financial accounting standards would be a good starting point. IFRS is a good basis as it is commonly accepted in many countries but this preference is not universal and may vary by the size of companies and the industry they are in. Small and privately held companies often prefer not to use IFRS. To the point made in C1 above, taxpayers should be permitted to elect on an irrevocable basis, to use local statutory financial standards.

To provide certainty, the GloBE proposals could consider specifying a certain number of acceptable accounting standards as a starting point and include guidance for

local authorities and taxpayers where there is a desire to transition from other GAAPs to IFRS.

**1b** The option could be given to using the accounting standards actually applicable to any individual entity or consolidated group (where consolidation entails the exoneration from separate entity financial reporting). The parent company, when collecting (and adjusting) the financial statement of all its subsidiaries for the preparation of the consolidated financial statement, could require the computation of the effective tax rate of all its subsidiaries.

However, as explained in C.2 above where the ultimate parent entity is frequently best placed to implement the various elements of GloBE, use of the accounting standards applicable to the ultimate parent entity of the MNE would be advisable and possibly necessary in such cases to ensure a standardized and coherent approach to GloBE implementation. It is worthwhile considering a simplified approach where the effective tax rate could be calculated by the parent company simply by leveraging on the data available on Table 1 of the Country-by-country report.

**1c** In general, financial accounting standards widely applied and recognized by professional accounting organisations either at a national or supranational level should be considered as adequate. As mentioned above, for clarity, the GloBE implementation guidance could specifically state a non-exhaustive list of accepted accounting standards.

**1d** No, we are not concerned in regard to this point. As mentioned above, the risks of abuse or systematic advantage can be mitigated by requiring irrevocable election and thereafter, consistent use of the chosen standard going forward.

**1e** Assuming the safe-harbours and carve-outs are set at an appropriate level, this should exclude most small MNEs and leave only the larger MNEs in scope of the GloBE. In such cases, it may be possible to require such MNEs to prepare consolidated financial statements using one of the commonly accepted GAAP standards. However, to do so could be tantamount to artificially conjuring a parallel tax computation that departs from the ordinary way the MNE manages its financial and tax computation. A set of tax computation that is artificially imposed

beyond the ordinary course of business is unlikely to have the effect of shaping behavior. Therefore, the better view is to permit the use of local GAAP by such MNEs.

#### BOX 2

- a** What are the material permanent differences between financial accounting income and taxable income that are common across jurisdictions and that you think should be removed from the tax base without undermining the policy intent of the GloBE proposal?
- b** Do you have views on the methods that could be used for dealing with permanent differences?
- c** Do you have any comments on the practicality of making adjustments for permanent differences?
- d** Do you think any other adjustments to the financial accounts require attention?

**2a** The material differences pertain to dividends, capital gains and interest costs. In addition, all kinds of participation exemptions should be considered for removal from the tax base.

**2b** A detailed list of exclusions or adjustments should be clearly stated to ensure a standardized approach complemented by guidelines where necessary to limit possible difference of interpretation. At the same time each taxpayer should be allowed to make additional adjustments, provided that these additional adjustments are described and adequately justified.

**2c** In some jurisdictions such as Italy, an adjustment might potentially be of temporary nature in a given fiscal year, but may eventually become that of a permanent nature. For example, an accrual for bad debt provision or for a possible legal controversy may entail an increasing adjustment in the financial year of the accrual and in the subsequent financial year(s), making a decreasing adjustment if the risks actually materialize and only up to the amount of the costs/loss borne by the taxpayer. The same applies to interest deduction. In a given financial year interests may not be deductible. However, they can be carried forward and become deductible if the company generates in future financial years sufficient EBITDA margins. The above examples illustrate that computation



of the effective tax rate may not be appropriate if it is calculated on an ex-ante approach.

**2d** Yes, as mentioned above, each subsidiary should be allowed to make additional adjustments, provided that these additional adjustments are disclosed and adequately justified.

**BOX 3**

- a** Do you have any comments on the use of carry-forward of losses and excess tax as a mechanism for addressing temporary differences under the GloBE proposal?
- b** Do you have any comments on the use of deferred tax accounting as a mechanism for addressing temporary differences under the GloBE proposal?
- c** Do you have any comments on the use of a multi-year approach to measure the average effective tax rate as a mechanism for addressing temporary differences under the GloBE proposal?
- d** Do you have any comments on what limitations (if any) should be imposed on the normal financial accounting rules for deferred tax assets and liabilities and the practicalities of imposing those limitations?
- e** Do you see opportunities for potential abuse in any of the approaches for addressing temporary differences described above? Do you have suggestions for designs to prevent those abuses?
- f** Do you have any suggestions for alternative mechanisms for dealing with temporary differences?
- g** Do you have any additional comments on Section 2, including comments based on experiences with existing regimes that you suggest should be adopted or avoided?

**3a** There may be different kinds of tax attributes in different jurisdictions, not only losses (e.g. non-deductible interest carry-forward) and sometimes the national tax law grants a carry-forward for an unlimited period. Thus, this approach could be challenging for the taxpayers. Nevertheless, it seems inherently fair that if the national tax law permits carry-forward, that the GloBE proposals do not override such legislation without a good reason.

We submit that it would be advisable that for tax purposes the same adjustments made under the applicable GAAP be accepted. Example 5 in the Annex to the Public Consultation Paper indicates that GAAP accounting of deferred taxes is (setting aside the subjective evaluation of deferred assets and liabilities) sufficient to provide a measure of the effective tax on profits in the years where the tax on profits is lower than the nominal rate due to the offset of losses (Year 2 of the Example).

**3b** We refer to examples 3 to 5 in the Annex to the Public Consultation Paper which indicate that there is no need to introduce specific rules or methodologies on the top of the generally accepted accounting principles of deferred taxes for the purpose of measuring the effective tax rate.

**3c** A multi-year approach would be complex and the effectiveness would depend on the number of years taken into account. Nevertheless, we propose that the option of using a three year multi-year approach be permitted on an irrevocable election basis so long as such an approach is used consistently by the taxpayer.

**3d** We do not believe that there is a need for general limitations to be imposed. Certain possible inconsistencies between the GAAP accounting and the tax rules could be aligned. For example, under most GAAPs, deferred tax assets may be created only if the taxpayer expects to generate taxable profits in the future sufficient to absorb the underlying losses.

**3e** We do not foresee significant opportunities for abuse that will not become apparent and potentially dealt with by general anti-avoidance legislation.

**BOX 4**

- a** How would you assess the general compliance costs and economic effects of a GloBE proposal that is based on either an entity, jurisdictional or worldwide blending approach?

Most of the industry and professionals we have spoken to favor the worldwide blending approach, as they believe this to be the simplest approach to apply. A worldwide blending approach also appears to be the most likely approach that minimises compliance costs for MNEs and improves the speed and efficiency in tax collection.

Regarding addressing temporary differences, they think worldwide blending should be combined with deferred tax accounting, as the application of carry-forward of losses and excess tax in combination with worldwide blending appear too complex. On the other hand, there are MNEs and industry professionals who think that a jurisdictional approach could be easiest to manage in practice.

If the worldwide blending approach is applied at the level of the ultimate parent and the top-up is calculated based on the nominal tax rate of the country of residence of the ultimate parent, the GloBE approach might have an unintended consequence of triggering a "race to the bottom" of tax rates or foregoing of taxing rights by jurisdictions keen to attract ultimate parent companies to base there. MNEs could decide to relocate their ultimate parent companies to such jurisdictions with low or minimal top up tax or who are more generous in their interpretation of deduction denials required under GloBE.

In case of local tax grouping or consolidated regimes, the entity approach could be considered to be replaced by a tax group approach for consistency. In such cases, the jurisdictional approach would be a workable solution, ensuring the reach of the expected economic effects but without imposing excessive general compliance costs.

Regardless of the approach adopted, we submit that the minimum tax rate considered for the test should take into account the fact that MNEs will have to bear significantly higher administrative costs. In order not to stifle innovation and healthy competition given the speed at which MNEs can enter into new businesses and new jurisdictions, the final GloBE regime should seek to ensure fair competition among companies operating in diverse distant markets.

#### BOX 5

- a In the absence of any of the approaches for addressing temporary differences discussed in Section 2, do you consider that a worldwide approach would be effective at managing the volatility issues discussed above?

A worldwide approach may reduce but may not be sufficient to wholly neutralise the volatility issues.

#### BOX 6

- a Assuming that the MNE's income for purposes of the GloBE proposal would be determined by reference to financial statements (adjusted as necessary) and assuming further that an MNE already prepares consolidated financial accounts, what are likely to be the compliance implications for MNEs in (i) separating the income and taxes of their domestic and foreign operations under a worldwide blending approach, (ii) separating the income and taxes to a jurisdictional level, or (iii) breaking down income and taxes to an entity level?
- b How would these compliance implications change if the income for purposes of the GloBE proposal was determined by reference to the rules used for calculating the tax base in the shareholder jurisdiction?

**6a** In order to avoid excessive compliance cost and at the same time achieve reliable results by avoiding discretionary allocation of the income, we submit that it is advisable not to require an MNE Group to separate figures which would have been included a single company financial report (e.g., separating the profits of a foreign branch and those of the State of residence of the enterprise) or the breaking down of a consolidated financial report into constituent separate company financial reports where it would not have been otherwise required of the MNE.

**6b** We submit that it is not wise to offer a number of permutations such that countries in implementing GloBE can pick and choose or in the worst case, require the tax base to be computed in two or more alternative jurisdictions.

**BOX 7**

- a** How would you suggest to apportion the income of an entity between the branch and the head office and do you think it should follow what is done for tax purposes?
- b** What are the compliance implications of such an allocation under a worldwide, jurisdictional and entity blending approach?
- c** Is the compliance impact smaller for those MNEs that are subject to CbC reporting requirements and that are already required to report the income of a branch and head-office separately even where no such requirement exists under financial accounting rules?

**7a** If there is worldwide blending, there should not be a need for apportionment. In the event that such apportionment is unavoidable, we would suggest applying principles consistent with the attribution of profits to permanent establishments.

**7b** As mentioned above the compliance burden will be much more onerous under the jurisdictional and entity blending approach.

**7c** We do not believe the compliance impact to be significantly lower for entities that already prepare Country-by-country reports as these computations will be used for the purpose of levying top up taxes or denying deductions, thus will have to be more robust and comprehensive taking into account the overall tax regime of the jurisdiction collecting the GloBE taxes. Country-by-country reports are intended by the OECD only for high level risk assessments, not the basis upon which tax adjustments are raised.

**BOX 8**

- a** How would you suggest to apportion the income of a transparent entity and do you think it should follow what is done for tax purposes?
- b** What are the compliance implications of such an allocation under a worldwide, jurisdictional and entity blending approach?
- c** Is the compliance impact smaller for those MNEs that are subject to CbC reporting requirements and that are already required to report the income of a transparent entities separately even where no such requirement exists under financial accounting rules?

**8a** To avoid complications, the apportion of income of a transparent entity should follow the tax rules of the jurisdiction that is administering the GloBE taxes.

**8b** Similar to 7b) above.

**8c** Similar to 7c) above.

**BOX 9**

- a** How would you suggest dealing with attributing taxes that arise in another jurisdiction or entity under a jurisdictional or entity blending approach?
- a** What comments, if any, do you have on the practicality of crediting taxes paid in an intermediate jurisdiction or entity, such as under a CFC rule, against income of the subsidiary or branch?

**9a** Attributing taxes that arise in another jurisdiction or entity should be considered to appropriately reflect the real effective tax rate. This should be done in a manner having regard to tax credits and timing when such taxes arise.

#### BOX 10

- a Assuming that the starting point for calculating the income of the MNE under the GloBE proposal is based on the financial accounts do you have any comments on the practicality of dealing with taxation of dividends under worldwide, jurisdictional and entity blending approaches?
- b Do you have any comments on how the taxation of dividends should be dealt with under the GloBE proposal?
- c Are there any other issues that you wish to highlight regarding worldwide, jurisdictional or entity blending?

The taxation of dividends should have regard to the treatment of dividends under the Country-by-country regime to minimise differences and confusion such differences may cause – refer for example to “Treatment of dividends for purposes of “profit (loss) before income tax”, “income tax accrued (current year)” and “income tax paid (on cash basis)” in Table 1 (September 2018, updated November 2019)” under Section 7 of the OECD’s Guidance on the Implementation of Country-by-Country Reporting BEPS ACTION 13.<sup>5</sup>

#### BOX 11

- a Do you have any comments, based on your own experience, as to the preferred design of a carve-out taking into account factors such as simplicity, compliance costs, certainty, incentives and behavioural impacts?
- b Are there any technical or compliance considerations that would make you concerned about a particular type of carve-out (i.e. based on facts and circumstances or on a formulaic approach), or suggest that there should be no carve-outs at all? If so, please explain based on your own experience.
- c Would you favour thresholds based on the size of the taxpayer? If so, please give your reasons and suggest a metric that you think should be used.
- d Would you favour any de minimis carve-outs? If so, what type of carve-out do you consider would result in the right balance between compliance costs and benefits?
- e Would you favour a carve-out for specific sectors or industries? If so, please state the sector or industry, explain your reasons and share thoughts on how such a carve-out could be operated with as little compliance cost and uncertainty as possible.
- f Do you have any additional comments on carve-outs, including comments based on experiences with existing regimes that you suggest should be adopted or avoided?

The ultimate question of whether ‘enough tax has been paid’ is unavoidably a subjective one but it needs to be weighed against the very real costs of increased compliance burden and double taxation. Perhaps before layering another set of complex tax rules onto international commerce, it is worth considering an a priori safe-harbour threshold along the lines of the following

Total taxes paid in fiscal year per submitted tax returns / Global revenue (using the single common most accounting standards available)

This threshold should be set high enough so that the majority of compliant taxpayers would have the certainty that they do not need to deal with GloBE and those that find that they do, have to achieve tax certainty by making adjustments to meet the threshold.

<sup>5</sup> Available at <https://www.oecd.org/ctp/guidance-on-the-implementation-of-country-by-country-reporting-beps-action-13.pdf>

To this quantitative bright line test can be added qualitative requirements with the caveat that the guiding principle for designing any safe-harbours or carve-outs should be simplicity and administrability. Certain indicia of abusive avoidance behaviour can be specified using well established principles for example, the principles in the Cadbury Schweppes case<sup>6</sup> or the principal or business purpose test so that the burden of GloBE compliance is limited to situations where the minority of arrangements that are artificial and the small group of taxpayers whose behaviour is unacceptable by international standards. The corollary to this is to have substance based carved outs in order to limit the impact of Pillar 2 to targeting artificial profit shifting instead of structures or arrangements that reflect genuine economy reality or activity. This will better align with EU law, which respects the fiscal autonomy of the EU member states and therefore only allows anti-abuse measures which specifically target artificial arrangements.

### Small & Medium Sized Enterprises

Small and Medium sized companies, particularly those with limited cross-border presence or those with limited related party dealings (e.g. less than 20% of turnover) should be carved out from the GloBE proposal as there is little incentive to engage in sophisticated avoidance and consequently does not justify the cost of complying nor the authorities' resources devoted to policing GloBE. A threshold based on global consolidated turnover such as that in the Country-by-country reporting regime could be applied. However, as opposed to a reporting requirement that is the country-by-country regime, the consequences to a level playing field of such a threshold effectively bifurcating the taxation regimes between GloBE and non-GloBE needs to be carefully modelled and examined.

### III Closing remarks

WTS Global is grateful for this opportunity to comment and contribute to the Inclusive Framework and the OECD work to combat tax avoidance and evasion. The efforts of the OECD and the Inclusive Framework in spending resources to engage as broadly as possible, not just the 130 or so members of the Inclusive Framework but also industry and tax professionals is laudable and well appreciated. Nevertheless, we are hopeful that the considerations and issues articulated out above will be

factored into the further work on the Pillar II proposals in order to ensure that proposals are coherent, administrable and avoids double taxation.

### Speed is often the enemy of the Good.

As more elegantly put by Daniel Bunn, 'Addressing tax avoidance is a key political issue for many countries, but these policies should not be discussed without accounting for the size of the current problem, how recent policy changes have addressed it, and what potential impacts might come from this new approach.' To this, we urge that the Inclusive Framework permit more time to assess the impact of BEPS and Pillars 1 and 2 (including fundamentally whether Pillar 2 is even necessary if the other measures prove to be effective), to thorough debate, quantify and understand the impact and deliberate these changes, including considering lengthening the time-frame for implementation so that the key concerns can be addressed and implementation proceed in an orderly and coordinated manner. The short time period for comments poses a challenge to all stakeholders involved and limits much needed in-depth analysis that will be needed if the complex issues raised in Pillar 2 are to be addressed in a coherent and comprehensive manner. In this regard, upon global consensus being reached by the Inclusive Framework on Pillar 2, the experts of WTS Global would welcome future opportunities to contribute to the specific design of each of the four component parts of the GloBE – income inclusion rule, undertaxed payments rule, switch-over rule and subject to tax rule, so that they may be technically robust yet practicable.

We live in momentous times when the international order, not just in taxation but also in trade and other areas is increasing under strain. This transition to what is in essence a new international architecture on income taxation should be deliberate and calibrated, with the norms carefully crafted so that they are coherent, administrable and avoids double taxation. Global consensus is already hard enough to achieve, moving too quickly may ironically undermine this very consensus as difference in extent and timing of implementation opens up opportunities for arbitrage or lead to unintended double taxation.

We thank you again for the opportunity to provide our comments and look forward to engaging with the OECD in its work finding a long-term, sustainable solution.

<sup>6</sup> Cadbury Schweppes plc, Cadbury Schweppes Overseas Ltd v Commissioners of Inland Revenue, Case C-196/04, 12 Sept 2006.



## WTS Global contributors – key contacts

(alphabetical on surname)

### Matthias Mitterlehner

Head of International Tax, ICON (Austria)

Member of WTS Global

matthias.mitterlehner@icon.at

T +43 (0) 732 69412-6990

### Koen Morbée

Partner, International Tax at Tiberghien (Belgium)

Member of WTS Global

koen.morbee@tiberghien.com

T +32 (0)2 773 40 80

### Giovanni Rolle

Partner, WTS R&A Studio Tributario Associato (Italy)

Member of WTS Global

giovanni.rolle@taxworks.it

T +39 (0)11 433 83 51

### Sam Sim

Co-founder and Senior Of Counsel, Taxise Asia LLC  
(Singapore)

Member of WTS Global

sam.sim@taxiseAsia.com

T +65 (0) 64 38 16 96

### Ruth Steedman

Senior Managing Director, FTI Consulting (United Kingdom)

Member of WTS Global

ruth.steedman@fticonsulting.com

T +44 (0) 20 37 27 17 11 / +44 (0)7583 096126

### Wim Wuyts

CEO at WTS Global (Belgium)

wim.wuyts@wts.com

T +32 (0) 2 801 30 33

[wts.com/global](https://wts.com/global)

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## Imprint

WTS Global

P.O. Box 19201 | 3001 BE Rotterdam

Netherlands

T +31 (10) 217 91 71 | F +31 (10) 217 91 70

[wts.com](https://wts.com) | [info@wts.de](mailto:info@wts.de)

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