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# Global IFA Travelling Lectureship Programme 2025

## Topic: **Pillar Two and its ramifications**



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# **Pillar Two and its ramifications**

**Lecture  
Christian Kaeser**

# ***Structure of the presentation***

**1- Pillar Two: how it all started**

**2- Pillar Two: where we are right now (the “GlobE debacle”)**

**3- Pillar Two: How to get out of this mess**

**4- Selection of practical concerns currently raised by GloBE rules -  
Simplifications**

# ***1 – Pillar Two: how it all started***

## **1.1. The BEPS Project**

## **1.2. The OECD and the Inclusive Framework**

## **1.3. BEPS Action Item One**

## ***1.1 – The BEPS Project***

- **BEPS: Base Erosion and Profit Shifting**
- **Started in 2013 by the OECD tasked by the G20**
- **Target on aggressive tax planning and tax avoidance by MNEs**
- **Resulted in the 15 BEPS Action Items (AI), covering topics such as hybrid mismatches arrangements, treaty abuse or PE avoidance**

## ***1.2 – OECD & the IF***

- **To achieve a global consensus on the BEPS Action Plan, the OECD established the Inclusive Framework (IF) in 2016**
- **Allow interested jurisdictions (i.e. Non-OECD-Members) to work together on an equal footing**
- **OECD and IF cannot set rules, they can only develop models/frameworks**
- **The jurisdictions need to implement the proposed rules into domestic law**
- **E.g.: ATAD I & II in the EU, or BEAT and GILTI in the U.S.**

## ***1.3 – BEPS Action Item One***

- **BEPS Action Item One was to deal with the issues around the taxation of the digital economy.**
- **The OECD struggled to find a tailor-made solution after exploring various approaches.**
- **The exercise ended with the Two-Pillar-Solution:**
- **Pillar One: Profit Allocation – dead end with the U.S. not playing along**
- **Pillar Two: GloBE rules**

# ***2 – Pillar Two: Where we are right now***

## **2.1. The GloBE Rules**

## **2.2. Implementation Status: the EU and the rest of the world**

## **2.3. Interplay between GloBE Models rules (EU directive) and domestic legislation**

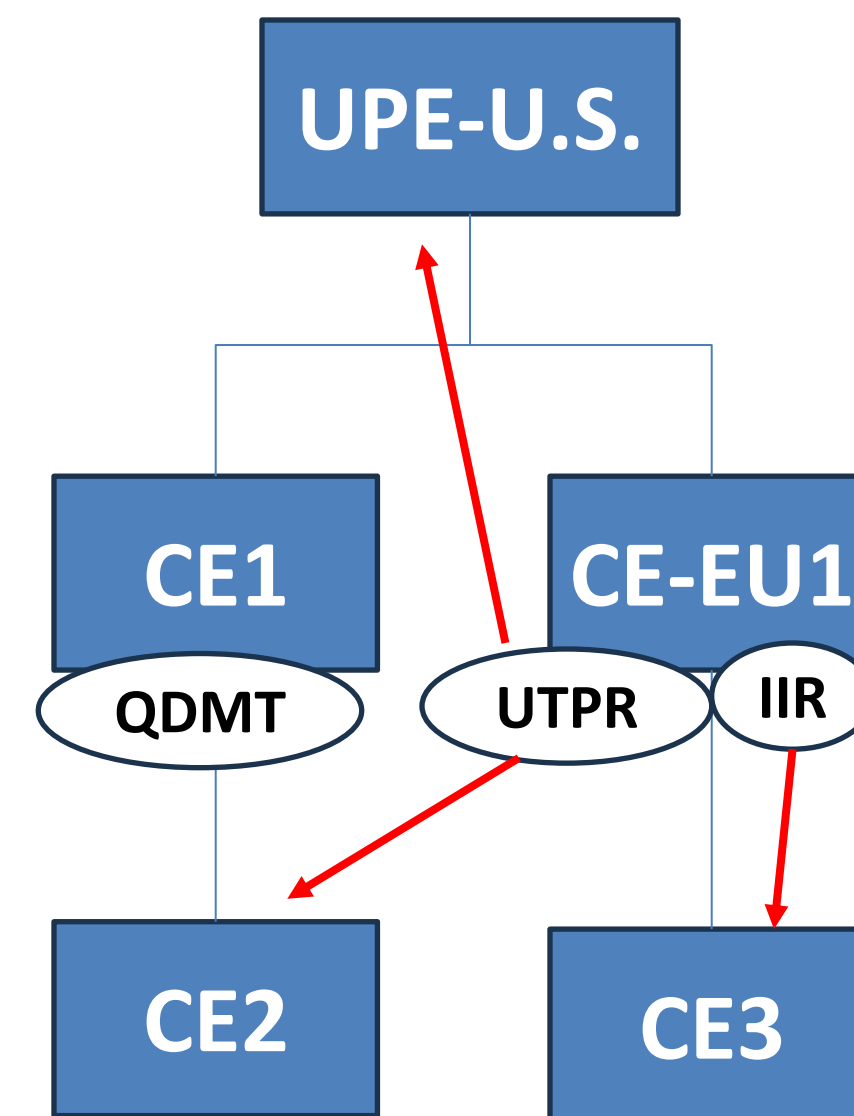
## **2.4. U.S. cancelation of “Global Tax Deal” and threat of retaliatory measures**





## 2.1 The GloBE Rules

- Tax imposed under GloBE is a “top-up tax” calculated and applied at a jurisdictional level.
- GloBE uses a uniform base and definition of covered taxes to identify those jurisdictions where an MNE is subject to an effective tax rate below 15%.
- It then imposes a coordinated tax charge that brings the MNE’s effective tax rate on that income up to the minimum rate,
- after taking into account a substance-based carve-out.
- Top Up Tax is collected under an Income Inclusion Rule (IIR), either at the level of the Ultimate Parent Entity (UPE) or under a Qualifying Domestic Minimum Top up Tax (QDMTT) at the level of a constituent entity
- As a backstop the Undertaxed Profits Rule (UTPR) applies. The UTPR imposes a Top Up Tax on constituent entities for low taxed income which is earned by other related parties of this entity.



## ***2.1 The GloBE Rules: the STTR***

- The STTR is a treaty-based rule that protects the right of developing Inclusive Framework members to tax certain intra-group payments, where these are subject to a nominal corporate income tax that is below 9%**
  - Exceptions apply, in particular to some items of covered income that result in a mark-up on costs of 8.5% or less in the hands of the person deriving that income**
- The STTR MLI is open for signature since 19 September 2024**
  - 9 Signatories**
  - 24 Jurisdictions signed a declaration of political support**
  - 57 Jurisdictions participated in the signing ceremony**

## ***2.2 Implementation Status: EU & RoW***

- Directive 2022/2523 of 15 December 2022 implemented in almost all EU Member States, with some late legislative actions (Cyprus, Poland, Portugal and Spain only implemented after having been referred to CJEU on 3 October 2024)**
- Deferred implementation of GloBE in Estonia, Latvia, Lithuania, Malta and Slovak Rep.**
- Mixed Picture outside the EU:**
  - « full package » : IIR + UTPR + DMTT (New Zealand, Liechtenstein, Turkey, South Korea, Japan (expected for end of March 2025))**
  - only IIR and DMTT, but not UTPR (Switzerland, Norway, Malaysia...)**
  - only DMTT, but not IIR and UTPR (Barbados, Brazil, Mauritius etc.)**



## ***2.3 Interplay GloBE – Domestic Legislation***

- **GloBE Rules are only “Model Rules”:**
  - **Countries are free to deviate, not implement;**
  - **dynamic development at the OECD creates legislative issues (“per se OECD legislation”) – see latest examples on next slide**
- **But GloBE Rules impact country behavior:**
  - **Some countries implemented a CIT (e.g. UAE)**
  - **Many went for a QDMTT (see previous slide)**
  - **Tax Incentives need to be carefully designed to work in a GloBE world**
- **EU Member States have locked themselves in: the EU Directive 2022/2523 obligates all EU MS to implement the GloBE Rules**



**25 April 2024**

Consolidated Commentary incorporates Agreed Administrative Guidance that has been released by the Inclusive Framework since March 2022 up until December 2023

**17 June 2024**

Guidance on application of the recapture rule applicable to deferred tax liabilities, cross-border allocation of current and deferred taxes, allocation of profits and taxes in certain structures involving Flow-through Entities, and the treatment of securitisation vehicles.

**15 January 2025**

Guidance on Central Record of Legislation with Transitional Qualified Status

Guidance on the basis that MNE Groups shall rely on to complete the GloBE Information Return

Guidance addresses the treatment of certain deferred tax assets that arose prior to the application of the global minimum tax as a result of certain governmental arrangements or following the introduction of a new corporate income tax.

***Illustration of ongoing dynamics at the OECD***

## ***2.4 The U.S. cancel “Global Tax Deal”***

### **-Executive Order Jan/20 on “The OECD Global Tax Deal”**

- All commitments in the IF cancelled**
- Investigation whether foreign countries don't comply with U.S. tax treaties, or impose extraterritorial or discriminatory taxes on American companies**
- Develop a list of options for protective measures or other actions to respond**

### **-Executive Order Jan/20 on “America First Trade Policy”:**

- Secretary of the Treasury tasked to analyze foreign countries applying discriminatory or extraterritorial taxes pursuant to sec. 891 IRC**
- This provision (from 1934), allows for a doubling of the tax rate on individuals/corporations of those foreign countries.**
- Applies to US source income; cannot exceed 80% of the taxpayer's income**

## ***2.4 The U.S. cancels “Global Tax Deal”***

**-Possible actions following Executive Order on “The OECD Global Tax Deal” :**

**“Defending American Jobs and Investment Act” reintroduced (first time 2023) by House Republicans on 22 January (Ways and Means Committee)**

- Tax rates on US income of wealthy investors and corporations in countries that apply discriminatory taxes such as the UTPR surtax would increase by 5% each year for four years, after which the tax rates remain elevated by 20% while the “unfair taxes” are in effect**
- Treaty override (lex posterior) – domestic withholding at 30%**

## ***3. Pillar Two: How to get out of this***

- **To avoid U.S. retaliatory measures on a country level:**
  - **If country has not implemented GloBE rules, only go for a QDMTT**
  - **If country implemented a UTPR, give the U.S. a permanent UTPR Safe Harbor,**
  - **and also accept the GILTI as a qualifying IIR.**
  - **Retaliate back.... Not a wise option for most countries**
  
- **At Inclusive Framework level:**
  - **Global consensus is apparently lost (China not implementing GloBE, neither)**
  - **Strive for overhauling the GloBE rules: more flexibility (GILTI), better, wider and permanent safe harbors, and especially simplification of the GloBE Rules**



# ***4. – Selected topics of practical interest for MNE groups - Simplifications***

**-Legal value of IF Guidance : a practical issue**

**-Transition into GloBE rules : deferred taxes, GIR (content, timing...), compliance burden, safe harbours**

**-“Mechanics” of GloBE rules : group scope, covered taxes, allocation of top-up taxes within the group...**

**-Mergers and acquisitions : group structures, GloBE impact of acquisitions...**

**-Legal certainty**

A photograph of modern glass skyscrapers under a clear blue sky, with a blue tint. The buildings are tall and slender, with many windows reflecting the sky.

# ***Pillar Two and its ramifications***

## ***Global Considerations***

***Dr. Giammarco Cottani, LL.M.***



**International Fiscal Association**

# ***Content Outline***

**1. Pillar Two: the US (S)aga...**

**2. Pillar Two Selected issues on Lack of Coordination**

- ***Scope, Mergers and Demergers between GloBE Model Rules and some EU countries***
- ***Permanent Establishment Definition under Globe Rules***
- ***Spotlight on Investment Entities***

**3. Some Final (rather critical...) Remarks**

# 1. Pillar Two: the US (S)aga...

## None of the GloBE rules are currently in place

### US domestic entity taxation – no QDMTT

- Taxation based on US tax principles, not financial accounting/GloBE
- 21% headline rate, but reduced by numerous tax incentives
- US corporate alternative minimum tax applies narrowly and does not align with GloBE rules

### US outbound taxation – no Qualified IIR (currently)

- GILTI applies at a 10.5-13.125% rate – below 15% minimum
- Allows for global blending
- Computed based on US tax principles rather than GloBE
- Blended CFC Regime allocation rules expire in 2027

### US will not adopt UTPR

- BEAT does not qualify
- UTPR safe harbor expires in 2026

## *1. Background on US Approach to P2*

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- P1 and P2 discussions began late in the first Trump Administration – mainly to address issues with DSTs
- Biden White House and Treasury Department proposed implementing some/all P2 rules
  - Implementation of a QDMTT
  - Modification of GILTI to increase rates and reduce global blending
  - Modification of BEAT to resemble original payment-based UTPR
- Certain proposals to further align US law with P2 passed US House of Representatives but failed in the Senate
- US did not further attempt to implement P2 – other than by issuing limited administrative guidance to reduce certain disagreements

# 1. Another Possible Retaliation coming from the US..

## ▶ H.R. 591, *Defending American Jobs and Investment Act* (Jan. '25)

- Would enact new section 899
- Identifies and addresses **extraterritorial taxes and discriminatory taxes** by foreign countries on U.S. businesses, like the UTPR and DSTs
- Gradual U.S. tax rate increases on certain income earned by entities and individuals in countries implementing such taxes:
  - 5% annual increase for four years
  - Remains at 20% while taxes are in effect
- Consideration of these taxes in U.S. negotiations – related to either tax or trade agreements
- Presidential authority to prohibit government contracting and procurement agreements with such foreign countries.



- HR 591 has overwhelming support by House Republicans



- Possible revenue offset in budget reconciliation
- Treasury, House W&M are coordinating efforts to prepare for a possible Byrd Rule challenge



- Broader than section 891
- Provides for more targeted response
- Includes a detailed definition of an “extraterritorial” or “discriminatory” foreign tax

## 2. Lack of coordination: Scope, Mergers and Demergers between GloBE Rules and the EU Directive

### Consolidated Revenue Threshold Definition:

- **OECD Model Rules** rely on a *multi-year* threshold concept (requiring €750 million consolidated revenue in at least 2 of the 4 preceding years) without separately defining an “annual” threshold.
- **Netherlands** explicitly defines the “consolidated revenue threshold” solely as an annual €750 million revenue, deviating from the OECD/EU’s hybrid approach and creating a narrow, monetary-only interpretation.
- **Germany** avoids ambiguity by using distinct terms for the one-year monetary threshold (***Schwellenwert***) and the overall multi-year threshold (***Umsatzgrenze***), thereby aligning with the meaning in the OECD model rules
- **Interpretation of Article 6.1.1**: Technical drafting of the merger/demerger scope rules in each country has led to different interpretations of subparagraphs (i) and (ii) of GloBE Article 6.1.1 (**governing first-year vs. multi-year revenue tests for new groups**). **Germany** heads to the substance of the model rules but drops certain phrases like “tested Fiscal Year,” enabling an “**extrapolation**” in the demerger test (i.e. treating first-year results as indicative for the four-year period).
- The **UK** explicitly inserted the word “**and**” between its equivalents of subparas., deviating from the OECD/EU text – this drafting choice makes the first-year and multi-year tests **cumulative** rather than alternative, imposing a stricter combined threshold condition. The **Netherlands** substantially restructured its demerger provision: it created a self-referential test for the first year (leading to a circular logic that had to be patched with an additional fiction), and it failed to extend that fiction to cover the multi-year test in subparagraph (ii).

## 2. Selected Issues: Permanent Establishment Definition

### - Overview of PE Definitions in GloBE Rules

- Four different permanent establishment (PE) definitions:
  - **Treaty PE:** Exists when there's an applicable tax treaty between the head office jurisdiction and PE jurisdiction, and the PE jurisdiction taxes income under a provision similar to Article 7 of the OECD Model
  - **Domestic CIT PE:** Applies when no applicable tax treaty exists, but the PE jurisdiction taxes income on a net basis similar to its own tax residents
  - **Deemed PE:** Applies when no applicable tax treaty exists and the PE jurisdiction has no CIT system, but would have taxing rights under OECD Model provisions
  - **Stateless PE:** Applies when none of the above definitions are met, there's a foreign place of business, and the head office jurisdiction exempts that income

### - Hierarchical Relationship Between PE Definitions

- The rules should be applied in a step analysis (hierarchical approach):
  - First determine if there's an applicable tax treaty in force
  - Then check if the PE jurisdiction has a CIT system
  - Then analyze if the PE would exist under OECD Model provisions
  - Finally, consider if the Stateless PE definition applies

### - Interpretation Issues with Treaty PE Definition

- Ambiguity in the term "taxes the income" - should this be interpreted as:
  - Actual taxation requirement, or
  - Merely having the right to tax under the treaty?
- It seems it should mean "may tax" (having the right to tax) based on:
  - Article 3.4.2(a) of GloBE Rules and related Commentary
  - Domestic exemptions shouldn't affect Treaty PE status, only its ETR

### - Challenges with Treaty Provisions and Exclusive Taxing Rights

- When a tax treaty gives exclusive taxing rights to the residence state (e.g., international traffic income):
  - The Commentary indicates no Treaty PE exists under GloBE Rules
  - This transfers potential top-up tax risk from the PE jurisdiction to the head office state - This may undermine domestic branch exemption systems



## 2. Selected Issues: Spotlight on Investment Entities

### ◆ **GloBE's Broad Scope vs. IFRS Limits: A Hidden Compliance Trap**

GloBE recognizes investment entities even when **IFRS 10 would not**—especially those measuring assets at cost. **Italy aligns with this broader scope**, forcing consolidation for entities otherwise exempt under accounting rules.

➤ *Result:* Unexpected GloBE exposure for Italian funds and holding vehicles.

### ◆ **Standalone ETR in Italy: Neutrality Principle Under Pressure**

OECD GloBE isolates investment entity ETRs to **shield minority investors** from group-level top-up taxes. **But Italy allows QDMTT collection at the fund level** if no local CE exists, risking a breach of neutrality.

➤ *Result:* Policy clash between administrative simplicity and global tax design principles.

### ◆ **Optional Regimes: Flexibility Meets Ambiguity in Cross-Border Chains**

GloBE elections (transparency / taxable distribution) shift tax to **investor-level jurisdictions**. Italy adopts both options but offers **little clarity on layered cross-border structures** (e.g., fund-of-funds).

➤ *Result:* Risk of mismatches in timing, location, and compliance obligations.

### ◆ **Example Deemed Consolidation in Italy: From Passive Vehicle to Group Entity**

GloBE applies a "**deemed**" group test even without actual consolidated accounts. Italy enforces this rigorously—**capturing PE platforms and "for-sale" holdings** long excluded under GAAP.

➤ *Result:* Substantial reporting and tax implications for funds never considered part of an MNE group.

### ***3. Some Final (rather Critical...) Remarks***

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- **Pillar Two is Not (Yet) a “Global” Minimum Tax**

Divergences in implementation (e.g., US non-adoption, EU inconsistencies, local QDMTTs) show this is **not one cohesive system**—but a patchwork of overlapping, sometimes conflicting, rules. Policymakers must stop pretending GloBE has achieved global consensus.

- **Complex Rules Create Asymmetric Burdens—Especially for Funds**

Investment entities and passive holding vehicles are **over-exposed** under current interpretations. The interplay between consolidation rules, standalone ETR, and optional regimes creates **uncertain outcomes for minority investors** and unaligned tax liabilities.

- **Neutrality is at Risk—More Than Policymakers Admit**

What was meant to be a minimum floor is now shaping into a **de facto global tax base definition**, often overriding domestic and treaty policies. The original neutrality principle—especially in investment contexts—is **increasingly compromised**.

- **Without Real Coordination, Pillar Two May Trigger Retaliation, Not Harmonization**

The threat of retaliatory moves like **US H.R. 591** highlights the geopolitical fragility of Pillar Two. Unless jurisdictions align technically and politically, the system risks becoming a **trigger for trade and tax wars**, not a platform for cooperation.

A photograph of modern glass skyscrapers under a clear blue sky, with a blue tint. The buildings are tall and slender, with many windows reflecting the sky.

# **Pillar Two and its ramifications**

## **PANEL DISCUSSION**



# IFA 2025 LISBON

5-9 OCTOBER 2025

## Highlights

### 2 Main Subjects

Subject 1. Residency of legal entities for corporate income taxation

Subject 2. Improper use of tax treaties and source taxation: policy, practice and beyond

### 8 Scientific Seminars

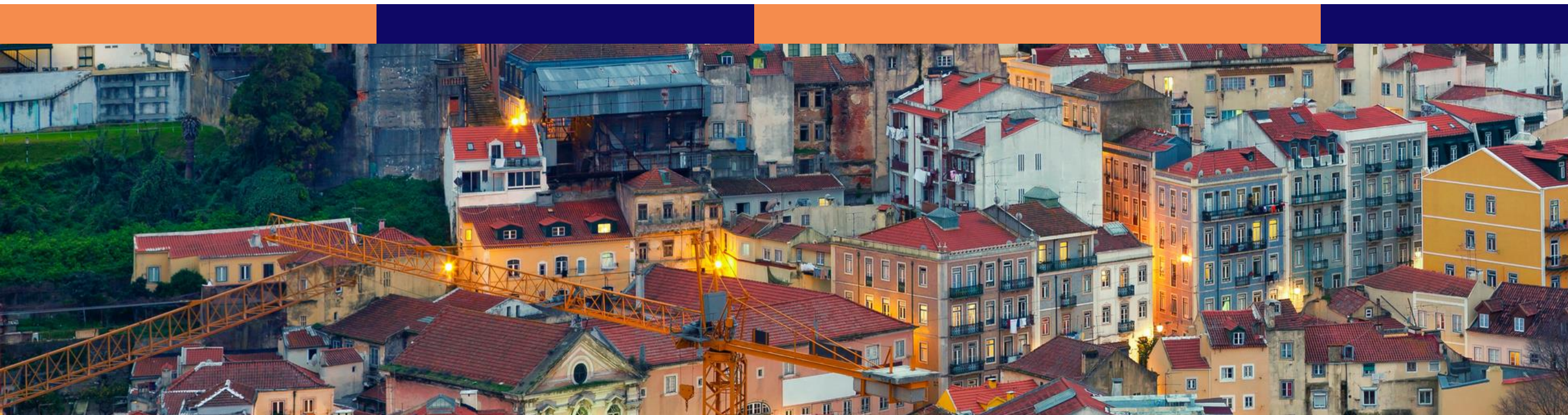
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