The two-pillar solution to international tax: where we are now?

International Tax

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Work continues by the OECD/G20 Inclusive Framework on BEPS on the two-pillar solution agreed in October 2021 that is intended to address the challenges arising from the digitalisation of the global economy. The CIOT has recently considered a Progress Report from the OECD on Pillar One and draft legislation published by the UK government that will implement Pillar Two in the UK.

In October 2021, the OECD/G20 Inclusive Framework on BEPS (Inclusive Framework) reached an agreement on a two-pillar solution to reform the international tax framework in response to the challenges of digitalisation.

The CIOT welcomed this historic agreement which aims to bring the international corporate tax framework up to date with the challenges of the digitalising economy, as well as to introduce more transparency and fairness in the global tax environment. We have long advocated a multilateral solution to these issues. We have been increasingly facing an international tax landscape of unilateral measures (and retaliatory actions) being taken independently by countries. These measures lead to less alignment of tax bases globally, resulting in potential double taxation and a significant compliance burden for businesses, and consequently restrict economic growth and innovation. Thus, the two-pillar solution and its key objective of stabilising the international corporate tax framework is welcome.

‘Pillar One’ involves a partial reallocation of taxing rights over the profits of multinational enterprises (MNEs) to the jurisdictions where consumers are located. (This is intended, among other things, to address the issue that many of the tech giants, under existing rules, pay most of their tax in the US, despite making sales all across the globe.)

‘Pillar Two’ intends to ensure that MNEs pay a minimum rate of 15% corporation tax (or their version of it) in every country they operate in.

Pillar One

In July 2022, the OECD Secretariat published a ‘Progress Report on Amount A of Pillar One’ (www.tinyurl.com/2s3e295u) and the CIOT welcomed this as a significant step in delivering the two pillars. We recognised the significant progress on the work on Amount A of Pillar One reflected in this report, following the consultations on the building blocks relating to the new taxing right under Amount A that have taken place during Spring and Summer 2022.

The Progress Report gave a welcome opportunity to comment on the draft domestic model rules for the various building blocks for Amount A. In our response, we also noted the revised schedule for the ongoing work, with the intention now being that the Pillar One rules will come into force in 2024, provided that a critical mass of countries enter into a multilateral convention to implement it.

Whilst recognising the political drive behind the two pillars, we also said that we support the additional time being taken in the design of these innovative rules that are intended to last for decades.

Our response welcomed the draft model rules in the Progress Report that introduce mechanisms to simplify the position for MNEs, indicating that the Inclusive Framework has listened to stakeholder feedback on previous consultations. We suggested that the ongoing work should continue to focus on the practicalities of the model rules and continue to ensure that these are as practicable and straightforward as possible, while delivering the policy aims.

We also said that effective relief from double taxation is crucial in order to deliver the policy aim of Pillar One, being the allocation of profits of an MNE to jurisdictions in which goods or services are supplied or consumers are located (market jurisdictions).

We noted that Pillar One is not intended to give rise to an overall increase in taxation for the MNE. Rather the rules are intended to operate as a reallocation of profits from one jurisdiction to another. Therefore, alongside the new taxing right for market jurisdictions, it is important that the rules provide relief for the equivalent amount that, under the existing profit allocation rules, are taxed elsewhere in order

to prevent double taxation that would penalise and discourage cross-border activity. We noted the ongoing work in this area.

Our full response to the OECD can be found at: www.tax.org.uk/ref985

Pillar Two

Pillar Two intends to ensure that MNEs pay a minimum rate of 15% corporation tax (or their version of it) in every country they operate in. The Inclusive Framework has published model legislation (Model Rules) with the aim for countries to legislate these Pillar Two rules (also known as the Global Anti-Base Erosion (GloBE) Rules) in 2022, with effect from 2023.

In July 2022, the UK government published legislation, as part of the draft Finance Bill legislation package, for a new 'multinational top-up tax', which will implement Pillar Two in the UK. The CIOT welcome the publication of this draft legislation, notwithstanding the recognition that there are many areas that require further multilateral work through the Inclusive Framework. This affords an opportunity for early scrutiny. The legislation is long and complex and the new rules will pose big administrative and compliance challenges for tax authorities and affected businesses alike.

Over the summer, the CIOT has met with HMT/HMRC to discuss the draft legislation and the implementation of Pillar Two in the UK. CIOT representatives have also taken part in a series of technical meetings held by HMT/HMRC at which the legislation has been discussed clause by clause, page by page. These meetings have given a welcome and valuable opportunity for detailed and open discussion, but have also highlighted the many remaining open questions within the draft legislation that need to be resolved by the Inclusive Framework.

The CIOT has previously urged the government not to rush ahead with implementing Pillar Two rules before other competitor countries. To this end, we welcomed the government's decision to delay the proposed implementation date of the reform to the end of 2023 rather than, as previously suggested, next April.

However, at our recent meetings we have also discussed with HMT and HMRC the reporting obligations that will arise for MNEs ahead of actual implementation if the legislation is enacted in the UK on the currently proposed timetable of the next Finance Bill.

We have suggested that the legislation remains in draft while the unresolved points are worked through and that it is not enacted until it is in a more settled state and closer to the implementation date.

Our press releases on Pillar Two can be found at: www.tax.org.uk/multinational_tax_plan and www.tax.org.uk/global_minimum_tax

Sacha Dalton *sdalton@ciot.org.uk*