Consistency versus “Gold Plating”: The EU Approach to Implementing the OECD Pillar Two

This article considers the proposed EU Directive to transpose the OECD Global Anti-Base Erosion (GloBE) Model Rules into EU secondary law. It describes the key aspects of the rules, notes the differences between the EU proposal and the OECD Model Rules, and demonstrates how the new charging provisions will operate.

1. Introduction

On 22 December 2021, the European Commission (the “Commission”) published a proposal to transpose the OECD’s Global Anti-Base Erosion (GloBE) Model Rules (the “Model Rules”) into EU secondary law (the “Directive”). The Model Rules were released two days before, on 20 December 2021, and form part of the OECD’s Two Pillar solution to address the tax challenges arising from the digitalization of the economy. The Model Rules were agreed by 136 members of the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS) on 8 October 2021.

Pillar Two of the OECD solution seeks to introduce a global minimum effective rate of corporate taxation at an agreed minimum rate of 15%. The Model Rules to give effect to the global minimum tax regime introduce the following two new charging provisions:

1. the Income Inclusion Rule (IIR): the IIR imposes top-up tax on a parent entity in respect of income taxed below the 15% minimum agreed effective tax rate (ETR); and
2. the Undertaxed Payment Rule (UTPR): the UTPR is a supporting rule that denies tax deductions or requires an equivalent adjustment to the extent the low tax income of a Constituent Entity is not subject to tax under an IIR.

The Model Rules are, according to the Inclusive Framework statement, to be brought into law in 2022, with the IIR becoming effective in 2023 and the UTPR having effect from 2024 onwards. The EU proposal follows suit – the proposed Directive requires the Member States to bring into force the laws, regulations and administrative provisions necessary to comply with the Directive by 31 December 2022. The Member States are required to apply the GloBE Model Rules from 1 January 2023 with the exception of the UTPR, which is to be applied from 1 January 2024.

It is expected that the OECD publishes further Commentary on the Model Rules shortly, which provides additional clarity on how the Model Rules should be interpreted and applied. The OECD has also announced plans to continue progress early in 2022 by launching public consultations on the implementation aspects of Pillar Two and addressing the coexistence of the rules with the US Global Intangible Low-Taxed Income (GILTI) rules.

At an EU level, the implementation of the proposed Directive is considered a key priority item setting a goal of reaching unanimity agreement among Member States on the implementation of the rules by spring 2022. Before then, stakeholders are invited to share their views on the EU implementation until 6 April 2022 in the form of a public consultation.

The aim of this article is first to describe the content and structure of the Model Rules and to point out apparent

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The differences between these rules and the Directive (see section 2). The technical content of this article is primarily based on the text of the Model Rules. Minor wording differences between the Model Rules and the Directive are not highlighted in the text below. However, where a more material difference between the drafting of the OECD Model Rules and the Directive has been identified, this is highlighted. By way of case studies (see section 3), the authors next demonstrate that the charging provisions as drafted in the Directive (as published by the Commission in December 2021) could deviate from the Model Rules, which, in certain scenarios, could give rise to a risk of double taxation. The conclusions of the article are presented in section 4.

The article is not intended to provide a comprehensive overview of the OECD Model Rules or the Directive. Given this context, there are certain aspects of the rules (for example, the treatment of mergers, joint ventures and eligible distribution tax systems) that are not covered within the scope of this article.

2. Overview of the Model Rules and the Proposed Directive

2.1. Introductory remarks

The Model Rules are designed as a “common approach,” meaning that Inclusive Framework member jurisdictions are not required to adopt the rules, but they must accept their application by other Inclusive Framework members. Also, where the members of the Inclusive Framework adopt the Model Rules, they must implement and administer the rules consistently. Accordingly, in order to ensure a consistent and harmonized implementation across the European Union, the Commission has proposed that the agreement reached at OECD level would be implemented by way of a Directive that closely follows the content and structure of the Model Rules. However, the Commission has included some additional provisions that are aimed at aligning the rules with primary EU law, i.e. eliminating the risk of discrimination between cross-border and domestic situations.

The Model Rules effectively provide for a five-step workflow to apply top-up tax in respect of low-taxed Constituent Entities in a multinational enterprise (MNE) group. The five-step workflow is outlined in Figure 1.

2.2. Identification of in-scope entities

The Model Rules apply to entities and permanent establishments (PEs), being Constituent Entities, that are part of an MNE group with a consolidated group revenue that exceeds EUR 750 million in at least two of the last four consecutive fiscal years. In an attempt to eliminate any risk of discrimination between cross-border and domestic situations, the proposed Directive has a wider scope and also applies to large-scale domestic groups (i.e. groups in which all the group entities are located in a single Member State) that meet the scoping thresholds. Certain types of entities are excluded from the scope of the Model Rules. These entities include government entities that do not carry on a trade, international organizations and non-profit organizations and pension funds. The list of excluded entities also encompasses investment funds and real estate investment vehicles provided they are the Ultimate Parent Entity (the UPE) of an MNE group. Entities owned by these excluded entities can be considered to be excluded entities in certain circumstances. However,

12. Inclusive Framework Statement, supra n. 4, at p. 3.
15. Art. 2, para. 1 and art. 3, para. 5 Directive, supra n. 1.
the Model Rules also provide jurisdictions with the option to apply the GloBE rules to these excluded entities.16

2.3. The ETR calculation

2.3.1. Opening comments

Once it has been determined that an MNE group falls within scope of the GloBE rules, the next step is to determine whether the ETR for each jurisdiction in which the group operates is less than the agreed minimum tax rate of 15%. If this is the case, top-up tax is calculated for that jurisdiction and allocated to the appropriate group entities as per the IIR and the UTPR. If the ETR – as determined under the GloBE rules – is equal to or higher than 15%, no top-up tax is required for that jurisdiction for the given fiscal year.

The ETR for a jurisdiction is equal to the sum of the adjusted covered taxes (the numerator) divided by the GloBE income or loss of Constituent Entities located in the jurisdiction (the denominator),17 both of which are discussed in detail in sections 2.3.2. and 2.3.3.

2.3.2. Calculation of the GloBE income or loss

The starting point for determining GloBE income or loss (the qualifying income or loss under the Directive) is the net income (or the loss) of a Constituent Entity. This is determined based on the consolidated financial statements of the UPE before any consolidation adjustments (i.e. the stand-alone accounts including the effect of intra-group transactions). In certain conditions, the financial accounting net income or loss of a Constituent Entity can also be determined based on an acceptable accounting standard that is different to the one applied by the UPE.18

The financial accounting net income or loss is then subject to a series of adjustments. It is understood that these adjustments are intended to account for categories of income and expenses that Inclusive Framework jurisdictions commonly treat differently for tax purposes. The adjustments include additions to GloBE income for net tax expenses, disallowed expenses (for example, bribes and certain fines and penalties) and reductions in respect of dividends and capital gains in connection to non-portfolio shareholdings with regard to participation exemption regimes.19 The financial accounting net income or loss is also subject to industry-specific adjustments, which include the exclusion of international shipping income and partly ancillary international shipping income20 as well as adjustments in relation to insurance companies.21

Furthermore, the Model Rules provide for a safeguard provision in respect of tax credits to reduce the risk of them being used to distort the ETR calculation.22 Tax credits that are deemed refundable in accordance with the definition of the Model Rules are treated as income for GloBE purposes. However, other tax credits reduce the amount of adjusted covered taxes and, therefore, also the overall ETR. In addition, an anti-avoidance rule is included in respect of intra-group financing arrangements used to reduce top-up tax liability in a low-tax jurisdiction (by artificially increasing the ETR) without increasing the tax liability in a high-tax jurisdiction at the same time.23

The calculation of GloBE income or loss allows for optional adjustments (following an election) to account for tax rules that deviate from accounting standards with regard to stock-based compensation schemes,24 or the consolidation of group entities that are located in the same jurisdiction.25 However, where the Model Rules provide for an option to offset income and losses arising from the disposal of tangible assets located in the Constituent Entity’s jurisdiction to third parties within a five-year period, the Directive only provides that option for immovable assets.26

The financial accounting net income or loss may further be re-allocated to account for the tax treatment of flow-through entities, hybrid entities and PEs.27 In addition, adjustments may be required to ensure that intragroup transactions are recognized in accordance with the arm’s length principle.28

2.3.3. Computation of adjusted covered taxes

The starting point for the calculation of the ETR numerator is the amount of covered taxes that is included in the financial net income calculation in the financial statements. Covered taxes include taxes recorded in respect of a Constituent Entity’s net income (potentially including withholding taxes on interest and royalties), taxes imposed in lieu of a corporate income tax, taxes imposed under eligible distribution tax systems and taxes on retained earnings and corporate equity.29 It is anticipated that taxes accrued under Pillar One of the OECD BEPS 2.0 proposals and taxes arising from the Pillar Two Subject to Tax Rule (STTR) – which is still being developed by the OECD – would both be considered to meet the definition of covered taxes. In contrast, it is understood that con-
sumption taxes (for example, sales taxes and value-added taxes), excise taxes, digital services taxes and ad valorem taxes (for example, stamp duties) would fall outside the scope of the covered taxes definition.

As with the calculation of GloBE income in section 2.3.2., the amount of covered taxes is subject to a number of adjustments including reductions for tax expenses relating to excluded income (for example, non-portfolio dividends) and uncertain tax positions, as well as reductions for certain tax credits and accrued taxes that are not paid within three years. The Model Rules also require adjustments to covered taxes where it is necessary to allocate covered taxes from one Constituent Entity to another either because of the nature of the taxpayer (for example, flow-through entities, hybrid entities or PEs) or because of the cross-border character of the tax (for example, controlled foreign company (CFC) rules and withholding taxes).

Covered taxes may also be subject to adjustments where a Constituent Entity records an adjustment to its covered taxes in its financial accounts for a previous fiscal year. The adjustment is either to be made in the current fiscal year (an increase in covered taxes) or in the form of a recalculation of the previous fiscal year’s ETR, which gives rise to an additional top-up tax in the current fiscal year (a material reduction in covered taxes).

In order to account for temporary accounting (book) to tax differences, a Constituent Entity’s adjusted covered taxes includes an allowance for deferred tax expenses, as encompassed in the financial statements. However, a full allowance for deferred taxes is not provided for in all cases, as the Model Rules contain a requirement to recast the deferred tax expense down to the minimum 15% rate where the deferred tax expense is included in the financial statements at a higher rate. Adjustments are also required where certain deferred tax liabilities are not unwound within five years (i.e. the tax is not paid by that time). However, this five-year recapture of unpaid deferred tax liabilities does not apply to an agreed list of "recapture exception accruals" under the Model Rules. It is understood that this list should include, for example, tax systems that provide for accelerated tax depreciation of certain tangible capital assets.

A simplification measure is also included in the Model Rules that allows an MNE group, by way of an election and in lieu of the previously noted deferred tax accounting rules, to establish a deemed deferred tax asset for a jurisdiction at the minimum rate where a net qualifying loss is incurred. The GloBE loss deferred tax asset is to be carried forward to subsequent fiscal years, and offset against future net GloBE income.

2.3.4. The simplification measure

The Model Rules provide for an optional safe harbour provision that applies on a jurisdictional basis, thereby reducing the top-up tax for the relevant jurisdiction to zero. No detail is provided on how the safe harbour should be calculated, but reference is made to the GloBE implementation framework, which is being currently developed at OECD level. However, under consideration in respect of the UK consultation document, the safe harbour could be applied by way of a simplified jurisdictional ETR calculation. Another option, as proposed by German academics, is a two-level simplification approach consisting of a country-level test and – when necessary – an MNE-level test.

Contrary to the Model Rules, the proposed Directive does not currently contain a safe harbour election, which has also been highlighted as an issue in responses to the public consultation. The proposed Directive also does not provide the Commission with the power to adopt delegated acts with regard to the GloBE implementation framework. It, therefore, seems likely that the Directive would have to be amended, subject to the unanimous agreement by Member States, to take account of any safe harbour measure that is agreed at OECD level in due course.

2.4. Calculation of the top-up tax

Figure 2 sets out the method for the calculation of the top-up tax.

The top-up tax for a low-taxed jurisdiction is calculated by multiplying the top-up tax percentage (i.e. difference between the minimum rate of 15% and the ETR of the jurisdiction) by the excess profit for a jurisdiction. The excess profit is the positive amount, if any, between the GloBE income and the losses of all of the Constituent Entities in the jurisdiction, after taking account of a substance-based income carve-out. The latter is determined as a markup on the carrying value of eligible tangible assets and eligible payroll costs. The markups are

30. Art. 4.1.3 Model Rules, supra n. 2 and art. 20, para. 3 Directive, supra n. 1.
31. Art. 4.3 Model Rules, supra n. 2 and art. 23 Directive, supra n. 1.
32. Art. 4.6 Model Rules, supra n. 2 and art. 24 Directive, supra n. 1.
33. Arts. 4.1.1 (b) and 4.4 Model Rules, supra n. 2 and arts. 20, para. 1 (b) and 21 Directive, supra n. 1.
34. Art. 4.4.3 Model Rules, supra n. 2 and art. 21, para. 2 Directive, supra n. 1.
35. Art. 4.4.4 Model Rules, supra n. 2 and art. 21, para. 7 Directive, supra n. 1.
36. Art. 4.4.5 Model Rules, supra n. 2; art. 21, para. 8 Directive, supra n. 1.
37. Art. 4.5 Model Rules, supra n. 2 and art. 22 Directive, supra n. 1.
38. Art. 8.2 Model Rules, supra n. 2.
42. Art. 5.2 Model Rules, supra n. 2 and art. 26 Directive, supra n. 1.
initially 8% for tangible assets and 10% for payroll – both metrics reduce over a ten-year period to 5%.\textsuperscript{43}

The top-up tax for a low-taxed jurisdiction is further increased by an additional top-up tax as a result of an adjustment made to covered taxes or GloBE income (or loss) to a prior fiscal year, or as a result of negative covered taxes that are lower than the expected adjusted covered taxes.\textsuperscript{44} The Model Rules also provide for an option for jurisdictions to impose a domestic top-up tax to Constituent Entities located in that low-taxed jurisdiction. Where a “qualified” domestic minimum top-up tax (QDMTT) is put in place, the parent entity applying the IIR is required to give credit for this “qualified” domestic minimum top-up tax when calculating the top-up tax payable for that jurisdiction, i.e. a domestic top-up tax reduces the general top-up tax liability of the parent.\textsuperscript{45}

On request and subject to conditions, a \textit{de minimis} exclusion can also apply which serves to reduce the top-up tax for the Constituent Entities located in a jurisdiction to zero in respect of a fiscal year where the average GloBE revenue of such jurisdiction is less than EUR 10 million, and the average GloBE income or loss of such jurisdiction is a loss or is less than EUR 1 million.\textsuperscript{46}

In a final step, the jurisdictional top-up tax is allocated among the Constituent Entities in a jurisdiction with reference to the proportion of the Constituent Entity’s GloBE income to the aggregated GloBE income of all Constituent Entities in that jurisdiction.\textsuperscript{47} According to the UK consultation document, allocating the top-up tax to individual Constituent Entities ensures that top-up tax collection by multiple entities or under different charging rules is coordinated, and that only the appropriate top-up tax for the jurisdiction is collected (i.e. eliminating over or under taxation).\textsuperscript{48}

2.5. Imposition and allocation of top-up tax

2.5.1. The QDMTT

Based on article 5.2.3, it is understood that the Model Rules provide Inclusive Framework members with an option to apply a QDMTT to Constituent Entities located in their territory. It is expected that the Commentary and the GloBE implementation framework will develop processes and provide guidance for tax administrations in implementing a QDMTT and determining whether a foreign minimum tax is considered to be a QDMTT.

The Directive makes use of that option and allows a Member State to collect top-up taxes in respect of the excess profits of low-taxed Constituent Entities located in its jurisdiction in priority to the IIR top-up tax collection mechanism (as outlined in section 2.5.2.).\textsuperscript{49} However, responses to the public consultation highlight that the proposed Directive does not clarify whether the QDMTT should follow the mechanics of the IIR, i.e. top-up tax to be collected by a parent entity in that Member State, or whether the QDMTT should be imposed on each low-taxed Constituent Entity individually. It is also noted that the proposed Directive does not clarify whether the calculation of the excess profits of Constituent Entities is to be based on the financial accounting standard used in the consolidated financial statements of the UPE or whether the calculation can be based on a domestic financial accounting standard (i.e. the generally accepted accounting principles of that Member State), which might provide for a higher or lower amount of top-up tax charged compared to the IIR mechanism.\textsuperscript{50}
2.5.2. The IIR

Following the application of a QDMTT, the IIR is the primary charging rule under the Model Rules to collect top-up tax in respect of jurisdictions with a jurisdictional ETR below the minimum agreed rate. The IIR charging provisions contain rules covering which MNE group entity should apply the IIR. Priority is generally given to the parent entity at the highest point in the ownership chain, which is charged the top-up tax in proportion to its allocable share in the low-taxed Constituent Entity’s income (i.e. a top-down approach is generally applied).

For instance, in a multi-tiered structure, where the UPE of the MNE group is subject to an IIR that is consistent with the GloBE rules (a qualified IIR), the UPE pays the IIR top-up tax in respect of a low-taxed Constituent Entity in priority to any Intermediate Parent Entity (IPE) in the structure.51 Where the UPE is not subject to a qualified IIR, the IIR taxing rights “drop” down to the jurisdiction of the IPE underneath it if it applies a qualified IIR and so on down the chain of ownership.52

In order to realize consistency with EU law, the proposed Directive is not limited to cross-border situations, but also applies to large-scale domestic groups.53 In addition, the Directive requires the application of the IIR in situations in which a low-taxed Constituent Entity is located in the same jurisdiction as the taxable parent entity (the UPE or the IPE). As a result, the IIR as proposed by the Directive also applies to the parent entity itself, where it is located in a low-taxed Member State.54 However, the Directive does not entirely clarify what amount of top-up tax is allocated to the parent entity in that scenario. In particular, where an IPE is required to collect top-up tax in respect of itself, it is not clear whether this relates to 100% of the top-up tax computed or whether it should be limited to the UPE’s allocable share of the top-up tax for that entity.55

Moreover, the proposed Directive empowers the Commission to add, in an Annex to the Directive, a list of third country jurisdictions to that have implemented a legal framework in their domestic law, which is considered by the European Union to be a qualified IIR. In this way, MNE Groups that are headquartered outside of the European Union should be in a position to assess whether the IIR applied by the UPE resident in a non-Member State is acceptable in the European Union or – in the case of IIRs that do not qualify – whether the IIR needs to be applied by EU-based IPEs.56

As an exception to the top-down approach, where a low-taxed Constituent Entity is held indirectly by a significant

(i.e., by more than 20%) minority interest holder outside the MNE group, the rules permit the Partially Owned Parent Entity (POPE) of this low-taxed Constituent Entity to apply the IIR in priority to any other parent entities located higher up the ownership chain, including the UPE (referred to as a bottom-up approach). In such situations, the POPE is required to apply the IIR in respect of its ownership percentage of the low-taxed Constituent Entities.57

As the Model Rules also require the UPE or the IPE to apply the IIR, the split-ownership rule provides for an IIR offset mechanism, which clarifies that the parent higher up the ownership chain reduces the amount of top-up tax by the amount already collected by a POPE under a qualified IIR.58 This situation is a similar outcome to scenarios in which the top-up tax liability of a taxable parent is reduced, as a domestic top-up tax is in place.

2.5.3. The UTPR

Under the Model Rules, the UTPR serves as a backstop to the IIR by imposing any remaining top-up tax relating to low-taxed Constituent Entities, where either:

- no top-up tax is collected under a qualified IIR, as:
  - none of the parent entities (the UPE and the IPEs) are subject to a qualified IIR; or
  - the low-taxed Constituent Entity is located in the jurisdiction of the taxable parent entity; or
  - not all of the top-up tax that is allocable to the UPE is collected under the IIR, as: (i) the UPE is not subject to a qualified IIR and (ii) the UPE holds more interest in a low-taxed Constituent Entity than any other IPEs that are subject to a qualified IIR.59

As noted in section 2.5.2., the Directive provides for an expanded scope of the IIR to comply with EU law, i.e. an EU parent collects top-up tax for itself and for Constituent Entities in its own low-taxed jurisdiction. This should, in theory, reduce the number of instances in which the UTPR can apply to cases in which the UPE is located outside the European Union and:

- the UPE, together with its subsidiaries located in that same jurisdiction, are low-taxed (i.e. no top-up tax collection under the IIR);60 or
- the UPE’s jurisdiction of residence has not implemented a qualified IIR and not all of the top-up tax that is allocable to the UPE is collected under the IIR, as the UPE holds more interest in the low-taxed Constituent Entity than any other IPEs that are subject to a qualified IIR.61

The total UTPR top-up tax is allocated to jurisdictions where the MNE group has Constituent Entities, and which have adopted the UTPR into law (the UTPR jurisdictions).62 How to impose the UTPR top-up tax that is allocated to the jurisdiction is up to the UTPR jurisdiction tax authorities. It could be by way of denial of a tax

51. Art. 2.1.1 and 2.1.3(a) Model Rules, supra n. 2 and arts. 5 and 6, para. 3(a) Directive, supra n. 1.
52. Art. 2.1.2 and 2.1.3(b) Model Rules, supra n. 2 and art. 6, para. 3(b) Directive, supra n. 1.
54. Id., at arts. 5, paras. 2 and 6, para. 2.
55. KPMG Public Consultation Response, supra n. 41. See also J. Rueck & D. Fehling, Effektive Mindestbesteuerung in der EU – der Richtlinienentwurf zur Umsetzung der GloBE-Regelungen [Effective minimum taxation in the EU – the proposed Directive to implement the GloBE rules], IStR, Volume 31, Issue 2, p. 53 (2022)).
57. Art. 2.1.4 and 2.1.5 Model Rules, supra n. 2 and art. 7 Directive, supra n. 1.
58. Art. 2.1 Model Rules, supra n. 2 and art. 9 para. 2 Directive, supra n. 1.
59. Art. 2.5 Model Rules, supra n. 2.
61. Id., at art. 11.
62. Art. 2.5.1 Model Rules, supra n. 2 and art. 13 para. 2 Directive, supra n. 1.
deduction (of any type) or an equivalent adjustment such as an additional top-up tax.\textsuperscript{63} Alternatively, it is expected that a jurisdiction could include an additional amount of deemed income, or it could choose to reduce an allowance or deemed deduction to reflect an allocation of top-up tax.

To the extent that top-up tax allocations cannot be imposed immediately, such taxes can be carried forward for imposition in a later year in the same jurisdiction under the Model Rules.\textsuperscript{64} While it is expected that a carry-forward mechanism would also be applied at an EU level, this is not explicitly referenced in the current text of the Directive.

The allocation mechanism for the total UTPR top-up tax takes into account the relative “substance” of Constituent Entities in the UTPR jurisdictions. A jurisdiction’s UTPR percentage (i.e. the share they are allocated of the total UTPR top-up tax) is determined by calculating:\textsuperscript{65}

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\text{Number of employees in the jurisdiction} \times 50\% + \frac{\text{Total value of tangible assets in the jurisdiction}}{\text{Number of employees in all the UTPR jurisdictions}} \times 50\%
\]

If a UTPR jurisdiction does not fully impose top-up tax in accordance with the amount that it has been allocated for a given fiscal year, its UTPR percentage is reduced to zero for subsequent periods until the amount from the previous years has been collected.\textsuperscript{66} This serves as an incentive for jurisdictions to implement the UTPR in a way that ensures that any UTPR top-up tax allocable to that jurisdiction is collected efficiently (which may in turn result in jurisdictions favouring additional top-up taxes over denials of deductions).\textsuperscript{67}

The Model Rules also provide for transition rules that reduce the UTPR top-up tax to zero for MNE groups in the initial phase of their international activity. This exclusion applies for a transitional period of five years, provided that the MNE group: (i) does not have Constituent Entities in more than six other jurisdictions; and (ii) the sum of the net book value of the tangible assets in the MNE group does not exceed a given threshold.\textsuperscript{68} In order to ensure equal treatment between MNE groups and large-scale domestic groups, the proposed Directive also excludes income from the activities of large-scale domestic groups for a transitional period of five years.\textsuperscript{69} In addition, the proposed Directive applies this transitional rule not only for the purposes of the UTPR, but also the IIR.\textsuperscript{70}

### 2.6. Filing obligations

The Model Rules require each Constituent Entity of an MNE group located in a jurisdiction to file a top-up tax information return, unless the return is filed by the UPE located in another jurisdiction, with which an exchange of information agreement exists. There is also scope for a Constituent Entity to designate another entity located in its jurisdiction to file on its behalf.\textsuperscript{71} The Model Rules require the filing entity to report certain data points, including: the location of Constituent Entities, the corporate structure of the group and information necessary to compute the ETR for the jurisdiction and the top-up tax for each Constituent Entity in the MNE group. The Model Rules also provide for additional information to be agreed as part of the forthcoming GloBE implementation framework to become reportable information.\textsuperscript{72}

The Directive does not refer to additional information being reportable following agreement through the GloBE implementation framework. It seems likely that the Directive would need to be amended in this respect as well, to take account of any additional reporting information that is agreed at OECD level in due course. Where an EU-based Constituent Entity is also required to file, the Directive reduces the scope of reportable information if the EU-based Constituent Entity has a non-EU-based UPE that is subject to rules considered equivalent to the Directive.\textsuperscript{73}

The returns must be filed within 15 months after the end of the fiscal year to which they relate.\textsuperscript{74} An extended 18-month filing deadline applies for MNE groups that are in the initial phase of their international activity.\textsuperscript{75} The proposed Directive does not clarify the reporting requirements for large-scale domestic groups.

In terms of penalties, the Model Rules do not contain any specific recommendations. However, the proposed Directive requires Member States to introduce penalties for making false declarations and for failures to file the information return within the prescribed deadline. In this regard, the Directive states that an administrative pecuniary penalty of at least 5% of the Constituent Entity’s turnover should be introduced by the Member State where a Constituent Entity has not provided the top-up tax information return. The penalty would be applied by a Member State if, following any reminder issued, the Constituent Entity has not made the filing within a period of six months.\textsuperscript{76}

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\textsuperscript{63} Art. 2.4.1 Model Rules, supra n. 2.

\textsuperscript{64} Art. 2.4.2 Model Rules, supra n. 2.

\textsuperscript{65} Art. 2.6.1 Model Rules, supra n. 2 and art. 13, para. 5 Directive, supra n. 1.

\textsuperscript{66} Art. 2.6.3 Model Rules, supra n. 2 and art. 13, para. 8 Directive, supra n. 1.

\textsuperscript{67} For instance, this appears to be the current position of the UK government. See UK Consultation, supra n. 39, at No. 7.47 et seq.

\textsuperscript{68} Art. 9.3 Model Rules, supra n. 2 and art. 47 Directive, supra n. 1.

\textsuperscript{69} Art. 50 Directive, supra n. 1.

\textsuperscript{70} Id., at art. 47.

\textsuperscript{71} Art. 8.1.1 and 8.1.2 Model Rules, supra n. 2 and art. 42, paras. 2 and 3 Directive, supra n. 1.

\textsuperscript{72} Art. 8.1.4. Model Rules, supra n. 2 and art. 42, para. 5 Directive, supra n. 1.

\textsuperscript{73} Art. 42, para. 6 Directive, supra n. 1.

\textsuperscript{74} Art. 8.1.6 Model Rules, supra n. 2 and art. 42, para. 7 Directive, supra n. 1.

\textsuperscript{75} Id., supra n. 2.

\textsuperscript{76} Art. 44 Directive, supra n. 1.
3. Case Study Examples and the Charging Provisions

3.1. The examples: Assumptions

The following examples seek to illustrate the differences between the Model Rules and the proposed Directive, while also highlighting some outcomes where the IIR and the UTPR are both applicable that seem to be somewhat counter-intuitive. In the following examples, it is assumed that:

- Substance-based carve-out and domestic top-up taxation should be disregarded.
- The full amount of top-up tax was collected in previous fiscal years, and all Constituent Entities have sufficient deductible expenses.
- No Constituent Entity has a preferential entitlement to GloBE income (for example, there are no special classes of shares with preferential dividend rights). As such, each Constituent Entity’s ownership interest of an entity is aligned with its ordinary share capital holding in that entity.

3.2. A low-taxed EU UPE applies GloBE rules (Example 1)

3.2.1. The facts

Hold Co is the UPE of an MNE group and is tax resident in jurisdiction A. Hold Co owns 100% of B Co (tax resident in jurisdiction B). C Co owns 100% of C Co (tax resident in jurisdiction C). Jurisdictions A, B and C (all Member States) have adopted a qualified IIR and UTPR (in the form of a denial of deduction). The key facts in respect of Example 1 are set out in Figure 3.

3.2.2. Assessment (the Model Rules)

3.2.2.1. The IIR

Hold Co qualifies as the UPE of the MNE group, and, therefore, is subject generally to top-up tax under the IIR equal to its allocable share in respect of those low-taxed Constituent Entities in which it has a direct or indirect equity interest. In this case, Hold Co is not required to collect top-up tax under the Model Rules as jurisdictions B and C are both high-taxed jurisdictions (both jurisdictions have ETRs of 20%). Accordingly, no top-up tax should be due under the IIR for B Co and C Co. While the ETR of jurisdiction A is 10%, which is less than the minimum, the Model Rules do not provide for the possibility to apply the IIR where the jurisdiction of the taxable parent is low-taxed.77

3.2.2.2. The UTPR

Under the IIR as set out in section 3.2.2.1., no top-up tax is collected with regard to jurisdiction A. Accordingly, the total top-up tax of 10 is to be collected under the UTPR by all jurisdictions that are subject to a qualified UTPR, and where Constituent Entities are located, namely jurisdictions A, B and C.78 The UTPR top-up tax is to be allocated between those jurisdictions, as follows:

- Jurisdiction A is allocated top-up tax of in total 2. Accordingly, Hold Co is denied a deduction of 10 to ensure that 2 is collected by way of additional tax (i.e. the denial of 10 deduction at a nominal tax rate of 20%).79
- Jurisdiction B is allocated top-up tax of in total 3. Accordingly, B Co is denied a deduction of 15 to ensure that 3 is collected by way of additional tax.
- Jurisdiction C is allocated top-up tax of 5 in total. Accordingly, C Co is denied a deduction of 25.80

The top-up tax allocated to jurisdiction A does not affect the calculation of its ETR as the UTPR top-up tax is excluded from the calculation of adjusted covered taxes.81

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77. Art. 2.1 Model Rules, supra n. 2.
78. Id., at art. 2.5.1.
79. Id., at art. 2.4.1.
80. Id., at arts. 2.4.1 and 2.6.1. That is, 10 x (50% x 600/1000 + 50% x 800/2000).
81. Id., at art. 4.2.2.
3.2.3. **Assessment (the Directive)**

In contrast to the Model Rules, the Directive permits the IIR to be applied at the level of the UPE. In this case, therefore, the UPE is liable for top-up tax where it is located in a Member State with a jurisdictional ETR of less than the agreed minimum rate.\(^{82}\) Accordingly, the fact that the ETR of jurisdiction A is low-taxed, gives rise to top-up tax of 15 under the IIR at the level of Hold Co.

As the UPE is not located in a third country jurisdiction that does not apply a qualified IIR\(^ {83}\) or located in a low-tax third country jurisdiction,\(^ {84}\) the UTPR does not apply in this scenario. No additional UTPR top-up tax should be payable under the Directive as a result.

3.2.4. **Comment**

Example 1 demonstrates the different scope in respect of the IIR between the Model Rules and the Directive. While the Model Rules apply the IIR only with regard to low-taxed Constituent Entities that are located in a different jurisdiction to the taxable parent, the Directive is not only limited to cross-border situations, but also requires the application of the IIR in situations in which a low-taxed Constituent Entity is located in the same Member State as the taxable parent entity (the UPE or the IPE), to achieve consistency with EU law.

3.3. **A non-EU UPE does not apply GloBE Rules and an EU IPE is low-taxed (Example 2)**

### 3.3.1. **The facts**

Hold Co is the UPE of an MNE Group and is tax resident in jurisdiction A that has not adopted GloBE rules. Hold Co owns 100% of B Co 1 and 40% of B Co 2 (both tax resident in jurisdiction B). The remaining 60% of B Co 2 is owned by B Co 1 which is deemed a controlling interest. B Co 2 owns 100% of C Co (tax resident in jurisdiction C). Jurisdictions B and C (Member States) have adopted a qualified IIR and UTPR (in the form of a denial of deduction). The key facts in respect of Example 2 are set out in Figure 4.
3.3.2. Assessment (the Model Rules)

3.3.2.1. The IIR

Hold Co (the UPE) is not subject to top-up tax, as jurisdiction A does not apply the IIR. Following the top-down approach, B Co 1 is subject to top-up tax under the IIR because it is the next parent down the ownership chain (the IPE). B Co 1 is subject to the IIR based on its allocable share in respect of those low-taxed Constituent Entities in which it has a direct or indirect equity interest. B Co 2 cannot apply the IIR, as a controlling interest in B Co 2 is held by an IPE subject to the IIR (B Co 1). The ETR of jurisdiction B is 10%, which is less than the minimum rate. However, the Model Rules do not provide for the possibility to apply the IIR where the jurisdiction of the taxable parent is low-taxed. The ETR of jurisdiction C is 10%, which is less than the minimum rate. Consequently, the top-up tax is 5 in total. B Co 1 is subject to top-up tax of 3 in respect of C Co, as it has an allocable share of 60% of C Co (because it indirectly owns 60% of the interest in C Co).

3.3.2.2. The UTPR

Under the IIR as set out in section 3.3.2.1, no top-up tax is collected with regard to jurisdiction B. Accordingly, the total top-up tax of 15 for this jurisdiction is to be collected under the UTPR by all of the jurisdictions that are subject to a qualified UTPR and where Constituent Entities are located, namely jurisdictions B and C. The UTPR top-up tax of 15 for jurisdiction B is allocated under the UTPR using the allocation mechanism (as described in Example 1, see section 3.2.2.2.) with jurisdiction B receiving 7.5 of the UTPR top-up tax and jurisdiction C receiving 7.5 of the UTPR top-up tax. With regard to jurisdiction B, the Model Rules do not define how the UTPR allocation should be allocated between Constituent Entities in that jurisdiction or if any split is required at all.

The total UTPR top-up tax for Jurisdiction C is 5. However, as top-up tax of 3 is being collected under the IIR, the total UTPR top-up tax is reduced to 2. This balance is to be collected by jurisdictions B and C under the UTPR using the UTPR allocation mechanism (as described in Example 1, see section 3.2.2.2.) with jurisdiction B receiving 1 of the UTPR top-up tax and jurisdiction C receiving 1 of the UTPR top-up tax.

3.3.3. Assessment (the Directive)

3.3.3.1. The IIR

In contrast to the Model Rules, the Directive allows for the IIR to be applied where the parent jurisdiction (in this case, jurisdiction B) is low-taxed. The IIR, therefore, applies at the level of B Co 1, which is located in a Member State. The jurisdictional top-up tax of jurisdiction B (15) is allocated among B Co 1 (5) and B Co 2 (10) in proportion to their respective GloBE income to their aggregated GloBE income. B Co 1 collects the full top-up tax computed for itself (5). With regard to B Co 2, B Co 1 collects top-up tax of 6, as it owns 60% of the interest in B Co 2.

In relation to the top-up tax payable for jurisdiction C, the result is the same as under the Model Rules, i.e. B Co 1 collects top-up tax of 3 as it owns 60% of the interest in C Co. B Co 2 does not apply the IIR, as B Co 1 is an IPE located in a Member State that holds a controlling interest in B Co 2. B Co 2 is also not a POPE.

3.3.3.2. The UTPR

The UTPR applies in this scenario as the UPE is located in a third country jurisdiction that does not apply a qualified IIR. The total UTPR top-up tax for jurisdictions B and C is equal to the sum of all top-up tax allocated to low-taxed Constituent Entities in jurisdictions B(15) and C (5), respectively. Then, it is also necessary to assess whether the UTPR amount for both jurisdictions can be fully or partly reduced.

Jurisdiction B

Despite the fact that top-up tax of in total 11 has already been collected under the IIR (B Co 1 collects 5 for itself and 6 in relation to B Co 2), the full amount of 15 for jurisdiction B also must be collected under the UTPR, due to the fact that the UTPR top-up tax cannot be reduced under article 13, paragraphs 3 and 4 of the Directive.

No reduction under article 13, paragraph 3 of the Directive is available, as B Co 2 is not wholly held by a UPE that applies the IIR or via an IPE that applies the IIR (by virtue of being located in a Member State or a third country jurisdiction that applies the IIR). In this case, B Co 2 is partially held by a UPE that does not apply the IIR, and B Co 1 is wholly held by a UPE that does not apply the IIR.

B Co 1 is itself a parent entity that applies the IIR to its own top-up tax. However, it does not appear, based on the wording of the proposed Directive, that B Co 1 could reduce its UTPR amount to zero, as it is not held by a parent entity that applies the IIR. As such, it does not appear that relief is available under article 13, para-

85. Art. 2.1.2 Model Rules, supra n. 2.
86. Id., at art. 2.1.3.
87. Id., at art. 2.1.6.
88. Id., at art. 2.5.1.
89. Id., at art. 2.4.1.
90. Id., at art. 2.5.3.
91. Art. 6, para. 2 Directive, supra n. 1.
92. Id., at art. 8, para. 3. An alternative interpretation of article 8, paragraph 3 of the Directive, supra n. 1 stating that B Co 1 is subject to the full amount of top-up tax (100%) not only in respect of itself, but also in respect of B Co 2 (see J. Reck & D. Feihling, Effektive Mindestbesteuerung in der EU – der Richtlinienentwurf zur Umsetzung der GloBE-Regelungen [Effective minimum taxation in the EU – the proposed Directive to implement the GloBE rules], ISB, Volume 31, Issue 2, p. 53 (2022)) is to be rejected as article 8, paragraph 3 of the Directive, supra n. 1 only relates to the full amount of top-up tax computed for the taxable parent entity.
93. Id., at art. 8, para. 2.
94. Id., at art. 6, para. 1.
95. Id., at art. 6, para. 3(b).
96. Id., at art. 7.
97. Id., at art. 11.
98. Id., at art. 13, para. 2.
A reduction in the UTPR top-up tax is also not available under article 13, paragraph 4 of the Directive, as this provision is limited to amounts collected under the IIR in a third country jurisdiction. A reduction in respect of the IIR collected by B Co 1 (for itself and B Co 2) in a Member State does not appear to be available based on the wording of the Directive.

The UTPR top-up tax of 15 is collected by all of the jurisdictions that are subject to a qualified UTPR, and where Constituent Entities are located, namely jurisdictions B and C. The allocation is made using the UTPR allocation mechanism (as described in Example 1, see section 3.2.2.2.) with jurisdiction B receiving 7.5 of the UTPR top-up tax and jurisdiction C receiving 7.5 of the UTPR top-up tax. With regard to jurisdiction B, the Directive does not define how the UTPR allocation should be split between Constituent Entities in that jurisdiction or if any split is required at all.

Jurisdiction C

With regard to jurisdiction C, a full reduction in the UTPR top-up tax is available, as C Co is wholly held by the UPE indirectly through a parent entity (B Co 2), which is located in a Member State. Based on a strict reading of the Directive, article 13, paragraph 3 appears to apply relief, despite the fact that B Co 2 is not required to apply the IIR in respect of C Co (as noted in section 3.3.3.1.). As a result, the UTPR top-up tax in respect of jurisdiction C is reduced to zero, despite the fact that only 60% of the total top-up tax is collected with regard to jurisdiction C (under the IIR).

3.3.4. Comment

Example 2 demonstrates that the provisions of article 13 of the Directive do not follow the UTPR mechanism as formulated under the Model Rules. Accordingly, article 13 of the Directive does not appear to function in the way the EU legislators most likely intended.
In general, the intention of article 13, paragraphs 3 and 4 of the Directive is to reduce the UTPR top-up tax in respect of cases in which the relevant top-up tax is fully (article 13, paragraph 3) or partly (article 13, paragraph 4) collected under the IIR elsewhere in the group (as is the case with article 2.5.2 and 2.5.3 of the Model Rules). However, with regard to jurisdiction C in Example 2, only 60% of the top-up tax has been collected by B Co 1 under the IIR. Nevertheless, no additional UTPR top-up tax is required to be collected based on the current drafting of article 13 of the Directive.

Moreover, when jurisdiction B in Example 2 is examined, full relief from the UTPR seems to be available only where the low-taxed Constituent Entities are wholly held by a UPE that applies the IIR or via an IPE that applies the IIR (by virtue of being located in a Member State or a third country jurisdiction that applies the IIR). Partial relief is only available where the top-up tax has been collected in a third country that applies a qualified IIR. This situation appears to ignore cases in which top-up tax is collected by an EU-based IPE, and full relief is not available and results in top-up tax seemingly being collected twice under the IIR and the UTPR, thereby leading to double taxation.

Example 2, therefore, demonstrates that subtle differences in how the Model Rules are introduced in jurisdictions can have a significant effect on the potential outcome of how top-up tax is collected. The Model Rules are intended to be applied on a consistent basis. Where this is not the case, such a situation raises the question of how the EU rules would interact with the GloBE rules introduced in a non-EU jurisdiction. In Example 2, it is unclear to the authors whether a UTPR in jurisdiction C (assuming jurisdiction C is a non-Member State) would apply in a scenario where the EU version of the UTPR did not pick up an equivalent amount of tax as was expected under the UTPR provisions in jurisdiction C. If this analysis were to be expanded across an MNE group, it could result in multiple different assessments being required if there are deviations in the manner that jurisdictions implement the GloBE Model Rules.

3.4. Minority shareholder: A non-EU UPE does not apply GloBE Rules (Example 3)

3.4.1. The facts

Hold Co is the UPE of an MNE Group, and is tax resident in jurisdiction A, a jurisdiction that has not adopted GloBE rules. Hold Co owns 100% of B Co, which is tax resident in jurisdiction B. B Co holds 90% of C Co (tax resident in jurisdiction C), with the remaining 10% of C Co being held by third parties. C Co holds 100% of D Co (tax resident in jurisdiction D). Jurisdictions B, C and D have adopted a qualified IIR and UTPR (in the form of a denial of deduction), and are Member States. The key facts in respect of Example 3 are set out in Figure 5.

3.4.2. Assessment (the Model Rules)

3.4.2.1. The IIR

Hold Co (the UPE) is not subject to top-up tax, as jurisdiction A does not apply the IIR. Following the top-down approach, B Co is subject to top-up tax under the IIR equal to its allocable share in respect of Constituent Entities that are taxed below the minimum agreed ETR, and in which B Co has a direct or indirect equity interest.99

The ETR for jurisdictions A and B is the same as the minimum rate (15%). Accordingly, no top-up tax is due for these jurisdictions. The ETR of jurisdiction C is 5%, which is less than the minimum rate. B Co, therefore, is subject to a top-up tax which is charged under the IIR. The jurisdictional top-up tax for jurisdiction C is 20. The inclusion ratio of B Co is 90% (as it directly owns 90% of the interest in C Co). Accordingly, B Co is subject to top-up tax of 18 in respect of C Co. The ETR of jurisdiction D is 10%, which is less than the minimum rate. B Co, therefore, is subject to a top-up tax, which is charged under the IIR. The jurisdictional top-up tax for jurisdiction D is 5. The inclusion ratio of B Co is 90% (as it indirectly owns 90% of the interest in D Co). Accordingly, B Co is subject to top-up tax of 4.5 in respect of D Co.

C Co is not required to apply the IIR, as less than 20% of its equity interests are held directly by minority shareholders that are not a Constituent Entity (i.e. C Co does not qualify as POPE).100 B Co also holds a controlling interest in C Co, and applies a qualified IIR.101

3.4.2.2. The UTPR

Under the IIR as set out in section 3.4.2.1., 90% of the jurisdictional top-up tax is collected by Hold Co. The remaining 10% of the top-up tax for jurisdictions C and D is not due under the UTPR. The total UTPR top-up tax in respect of both jurisdictions is reduced to zero, as all of the UPE’s ownership interests in the low-taxed Constituent Entity are held directly or indirectly by one or more parent entities that are required to apply a qualified IIR.102 In Example 3, Hold Co has an indirect ownership of 90% in C Co and D Co. B Co is a parent entity (as the definition includes IPEs), and it applies a qualified IIR to its 90% ownership interest in C Co and D Co. Accordingly, B Co applies the IIR, which captures all of the UPE’s ownership interest. The third-party minority shareholders are not subject to top-up tax, as they are not Constituent Entities within the MNE group for the purposes of the Model Rules.

However, if Hold Co held a direct ownership interest in C Co (for example, Hold Co owns 5% of C Co directly such that B Co only holds 85%), the assessment would differ. Under the IIR, 85% of the jurisdictional top-up tax would be collected by B Co. The remaining 15% of the top-up tax for jurisdictions C and D would be due under the UTPR.

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99. Id., at art. 2.1.4.
100. Id., at art. 2.1.3(b).
101. Id., at art. 2.1.4.
102. Id., at art. 2.5.2.
The total UTPR top-up tax would be equal to the top-up tax calculated for each low-taxed Constituent Entity (i.e. 20 for C Co and 5 for D Co). The total UTPR top-up tax is not reduced to zero, as all of the UPE’s ownership interest in the low-taxed Constituent Entity is not held directly or indirectly by one or more parent entities that are required to apply a qualified IIR. Hold Co does not apply an IIR, and has an indirect ownership of 90% in both C Co and D Co, whereas B Co (which does apply the IIR) only has a direct and/or indirect ownership of 85% in C Co and D Co. Consequently, the top-up tax calculated for the low-taxed Constituent Entity is subject only to a partial reduction for amounts brought into the charge of a qualified IIR. As B Co is subject to an IIR of 17 for C Co and 4.25 for D Co, the total UTPR top-up tax in respect of C Co is reduced to 3 and 0.75 for D Co, respectively. These amounts are allocated among qualifying UTPR jurisdictions using the standard UTPR allocation mechanism (as in Examples 1 and 2, see sections 3.2.2.2. and 3.3.2.2.).

3.4.3. Assessment (the Directive)

3.4.3.1. The IIR

In line with the outcome of the Model Rules, B Co (resident in a Member State) would be subject to the IIR and would collect top-up tax of 18 with regard to C Co and 4.5 for D Co, respectively. C Co would also not be required to apply the IIR, as 20% of its equity interests are held directly by minority shareholders that are not a Constituent Entity (i.e. C Co does not qualify as POPE). 3.4.3.2. The UTPR

As in Example 2 (see section 3.3.3.2.), the UTPR applies, as the UPE is located in a third country jurisdiction, and does not apply a qualified IIR. It, therefore, is necessary to calculate the UTPR amount chargeable in respect of low-taxed Constituent Entities (C Co and D Co) in accordance with article 13 of the Directive.

In this case, article 13, paragraph 3 of the Directive does not apply as C Co and D Co are not wholly owned directly or indirectly by Hold Co, as there is a third-party shareholder with a minority interest. The total UTPR top-up tax is also not reduced based on article 13, paragraph 4 of the Directive, as no amounts are allocated to a parent entity located in a third country jurisdiction that applies the IIR (the IIR is only applied by B Co, which is resident in a Member State), and the Directive does not provide for relief under article 13, paragraph 4 of the Directive in respect of the IIR applied within the European Union.

As such, and despite the fact that top-up tax has already been collected under the IIR by B Co, the total UTPR top-up tax in respect of C Co (20) and D Co (5) applies without reduction, is collectible under the UTPR and allocated between all of the UTPR jurisdictions (jurisdictions B, C and D) using the UTPR allocation mechanism. This result would not change if Hold Co were to hold a 5% ownership interest in C Co directly (i.e. B Co only holds 85%), as C Co and D Co would still not be wholly owned, directly or indirectly, by Hold Co due to the involvement of the third-party minority shareholder. Consequently, no reduction of the UTPR top-up tax would apply.

3.4.4. Comment

Example 3 demonstrates that, under the Model Rules, the UTPR relief can differ depending on whether a UPE (not subject to a qualified IIR) holds ownership interests in a low-taxed Constituent Entity directly or indirectly. Where the UPE ownership interest (of less than 100%) in a low-taxed Constituent Entity is held completely by way of IPEs, no UTPR top-up tax is payable. However, where a percentage of the UPE’s ownership interest is held directly by the UPE, the UTPR top-up tax is payable on the full amount of the top-up tax that is not collected by an IPE by way of an IIR (i.e. the top-up tax allocable to the UPE’s direct shareholding and the shareholdings of third parties). It is understood that this approach should simplify the application of the UTPR in the majority of cases, and allow for a greater level of top-up tax to be collected when compared against scenarios where the UPE applied the IIR to its full ownership interest. Where taxpayers have complex corporate ownership structures, the application of the UTPR relief mechanism, therefore, may act as an incentive for groups to restructure their corporate ownership structures to ensure that the amount of top-up tax payable is limited to the UPE’s ownership interest.

With regard to the Directive, Example 3 demonstrates the same outcome as before in Example 2. The top-up tax in respect of C Co and D Co seem to be collected twice under the IIR and the UTPR leading to double taxation. Accordingly, the authors’ comments under Example 2 are also valid here (see section 3.3.4.).

4. Conclusions

Based on the authors’ understanding of the proposed Directive, it seems that, while EU legislators moved ahead quickly with the EU implementation of the GloBE Model Rules using the momentum of the historic agreement of 8 October 2021 of the OECD/G20 Inclusive Framework, the adjustments made to reflect EU primary law requirements have given rise to certain deviations and adverse consequences. As Examples 1, 2 and 3 (see sections 3.2., 3.3. and 3.4., respectively) demonstrate, the fact that the EU broadens the scope of the IIR, while seeking to reduce the scope of the UTPR, results in inconsistencies in how both rules interact. In certain cases, this situation could give rise to risks of both double taxation and non-taxation.

The authors hope that those issues will be taken up by the Commission in the course of the public consultation process, and that amendments to the proposed Directive

103. Id., at art. 2.5.1.
104. Id., at art. 2.5.2.
105. Id., at art. 2.5.3.
106. Art. 6, para. 1 Directive, supra n. 1.
107. Id., at art. 7.
108. Id., at art. 11.
109. Id., at art. 13, para. 5.
will be made to rectify these inconsistencies. However, this may prove challenging, given the tight timeline for implementation if the rules are to become effective in 2023. In this regard, French President Emmanuel Macron announced that the implementation of the Model Rules on Pillar Two would be a key priority item as part of its Presidency of the Council of the European Union, setting a goal of reaching agreement on the implementation of the rules in the European Union by Spring 2022.

More generally, the timeline for approving the proposed Directive may prove challenging when viewed in the context of the reservations of some Member States that were raised during the public meeting of the European Parliament’s subcommittee on tax matters (FISC) on 18 January 2022. Several Member States (for example, Estonia, Finland, Hungary, Luxembourg, the Slovak Republic and Sweden) expressed concerns regarding the tight implementation timeline, and how this would fit within their domestic national law-making processes. Estonia also raised earlier concerns to the effect that the expansion of the Directive to cover domestic groups was not part of the OECD agreement, and Malta expressed strong reservations on certain issues about which they have not received any feedback or answer.

The approval and implementation process in the United States is also likely to have a significant effect on the EU approval process. As progress has stalled in the United States, this may create challenges at an EU level given that the GloBE Model Rules are seen as a “common approach”. While the member jurisdictions of the Inclusive Framework are not required to adopt the GloBE Model Rules, they are required to accept their application by other Inclusive Framework members. Where progress stalls globally, pressure might build for certain amendments to be made to the Model Rules, which, in turn, could require amendments to the EU proposals. This concern was most recently raised during the FISC meeting on 18 January 2022, where several Member States (notably, Estonia, Hungary and Poland) cautioned against an expedited approval process for the Directive, as they deem the OECD Pillar One and Pillar Two proposals as a package deal that was agreed on together by the Inclusive Framework. In this regard, Poland argued that it would not support the Directive without the United States implementing Pillar One, citing concerns regarding a potential effect on EU competitiveness if a minimum tax was introduced in the European Union without corresponding implementation of both of the OECD Pillars in the United States.

In contrast, the Commission and other Member States have expressed their strong willingness to implement an EU-wide minimum tax regime, and have argued that Pillar One and Pillar Two are separate acts from a legal perspective and follow a different implementation method (Pillar One – the Multilateral Convention and Pillar Two – the Directive). If this argument succeeds, Pillar Two should still be able to stand on its own without the support of Pillar One.

In conclusion, it remains to be seen if and when Member States can agree on the proposed EU Pillar Two Directive. In any event, it is to be hoped that, by the time approval takes place, the inconsistencies documented in this article will have been clarified, and that the mechanics of the EU charging provisions will have been aligned with the GloBE Model Rules.

110. See French Presidency/Macron Speech, supra n. 10.