



## Tax Newsflash

### OECD Inclusive Framework reaches political agreement on taxing the digitalised economy and a global minimum rate



On 1 July 2021, the G20/OECD Inclusive Framework on BEPS (‘the [Inclusive Framework](#)’) published a [Statement](#) on the key components of global tax reform, agreed by 130 of its members.

Since 2017, the 139 member countries of the Inclusive Framework have been jointly developing a ‘two-pillar’ approach to address the tax challenges arising from the digitalisation of the economy. This led to the publication of two detailed ‘Blueprints’ in October 2020 on potential rules for addressing nexus and profit allocation challenges (‘[Pillar One](#)’) and for global minimum tax rules (‘[Pillar Two](#)’). The proposals were updated and simplified by the US Biden Administration in April 2021, and formed the basis for the political agreement reached by the G7 countries in June 2021.

#### Deloitte Comments

Further to political agreement by the G7, 130 countries have now agreed the key components for changes to the international tax framework. These countries represent more than 90% of global GDP and this is another huge step for global tax reform on a coordinated basis.

The OECD estimates that under Pillar One, taxing rights on more than USD 100 billion of profit will be reallocated to market countries each year. The global minimum corporate income tax under Pillar Two - with a minimum rate of at least 15% - is estimated to generate around USD 150 billion in additional global tax revenues annually.

An ambitious and challenging timetable has been set with plans for both Pillar One and Pillar Two to apply from 2023, which if achieved would be considerably earlier than expected. There are technical (and some policy) areas that the OECD will continue to work through and US Congress will also need to pass the proposals.

The 'largest and most profitable' businesses that will need to reallocate a share of global residual profit to market countries under Pillar One have been confirmed as those with global turnover above €20 billion (until 2031, at least) and a profit margin above 10%. The Inclusive Framework has agreed that the share reallocated to market countries should be in the range of 20-30% (the G7 had previously agreed at least 20%). Extractives and regulated financial services have been confirmed as excluded from scope. Companies within the scope of Amount A will benefit from mandatory binding dispute resolution mechanisms, including transfer pricing and business profits disputes related to Amount A.

A key component of the agreement remains the commitment for the implementation of Pillar One to be coordinated with the removal of unilateral Digital Services Taxes and relevant similar measures.

The countries have also agreed with the G7 that a global minimum tax under Pillar Two should be at least 15%, calculated on a country by country basis. This is likely to co-exist with the US's GILTI regime, provided that this aligns with calculations on a country by country basis (as proposed by the Biden Administration).

The treaty-based subject to tax rule on interest, royalties and other payments is recognised as an integral part for developing countries, and has a rate of 7.5%-9% (on a gross payment rather than net profit basis). Similarly, the marketing and distribution function return (Amount B) will be simplified and streamlined, with a particular focus on the needs of developing countries.

The long list of countries in agreement with the proposals include China, India, Switzerland, Singapore, the United Arab Emirates, Bermuda, Jersey, Guernsey and the Isle of Man. Of the Inclusive Framework countries that have not yet agreed to the proposals, the most notable are EU members Ireland and Hungary.

## Nexus and profit allocation rules (Pillar One)

### Amount A

Pillar One's 'Amount A' proposal reallocates taxing rights in favour of market countries through the creation of a **new taxing right**. A share of a group's global residual profit will be **reallocated to market countries** using a **formulaic approach**. No physical presence is required in a market country to create an Amount A nexus/taxable presence.

Agreement has been reached that Amount A should apply to multinational businesses with **global annual turnover exceeding EUR 20 billion** and **profitability above a 10% margin**. Businesses in the **extractive** and **regulated financial services sectors are excluded** from Amount A.

The global annual turnover threshold will be reduced to EUR 10 billion in the future, depending on a successful implementation of Amount A, including in respect of tax certainty. A review to determine the success will be undertaken seven years after the rules enter into force (so expected to be in 2030).

Segmentation rules will apply only in exceptional circumstances where a segment disclosed in financial statements meets the scope of the rules.

A **market country** will be entitled to an allocation of Amount A if revenues of at least **EUR 1 million** are generated in that country. For countries with GDP lower than EUR 40 billion, this threshold will be EUR 250,000. Revenues will be sourced to the **end market country where goods or services are used or consumed**. Detailed sourcing rules will be developed for specific categories of transactions. Requirements to trace small amounts of sales will be kept to a minimum.

In-scope businesses will **reallocate 20%-30% of their residual profit above a 10% profit level to market countries** using a revenue-based allocation key. The 10% profit level will be calculated as the ratio of profit before tax to revenue. Profit amounts will be derived from financial accounts with a small number of adjustments.

A **marketing and distribution profits safe harbour** will limit the Amount A allocation to market countries where residual profits are already taxed.

To eliminate double taxation, any Amount A liability will be allocated to entities that earn residual profit and relieved via either exemption or credit.

The administration of the new rules will be streamlined and businesses will be able to manage their compliance through a single entity.

Implementation **will be coordinated with the removal of all digital services taxes (DSTs)** and other relevant similar measures on all companies.

## Amount B

Further work will be undertaken in respect of Amount B to **simplify and streamline** the pricing of **'baseline marketing and distribution activities'** undertaken by related party distributors.

## Tax certainty

Mandatory and binding dispute resolution mechanisms will be available in respect of all issues related to Amount A, including transfer pricing, business profits, and determination of whether an issue falls within the scope of the Amount A dispute resolution mechanism. Some small developing economies that have few or no mutual agreement procedure

cases may be considered for an elective (rather than mandatory) dispute resolution process.

## Global minimum tax (Pillar Two)

### Income inclusion rule and undertaxed payment rule

New rules will ensure that large multinational businesses pay a **minimum effective rate of tax of at least 15%** on profits in all countries. The **income inclusion rule** will result in additional 'top up' amounts of tax being payable by a parent entity of the group to its tax authority. The **undertaxed payment rule** will apply as a secondary (backstop) rule where the income inclusion rule has not been applied.

Multinational groups with consolidated revenues of at least **EUR 750 million** will be in scope, but countries will be free to apply lower thresholds to groups headquartered in their country. Ultimate parent entities that are government entities, international organisations, non-profit organisations, pension funds or investment funds, and any holding vehicles used by such entities, will not be subject to the rules.

The allocation method for top-up taxes under the undertaxed payment rule, including in respect of low taxed profits in the country of the ultimate parent, remains to be agreed.

The Pillar Two rules will have the status of a **common approach**: countries will not be required to adopt them, but if they choose to, implementation must be in a manner consistent with the model rules and Inclusive Framework guidance. Consideration will be given to the conditions under which the US GILTI regime will co-exist with the Pillar Two global minimum tax, including being applied on a country by country (jurisdictional) basis.

Effective tax rate calculations will use a **tax base determined by reference to financial accounts**, subject to agreed adjustments and mechanisms to address timing differences.

There will be a **formulaic substance carve-out** to exclude income that is at least a 5% return on tangible assets and payroll (7.5% during a five-year transition period). There will also be a de minimis exclusion, and an exclusion for international shipping income. The Inclusive Framework expressed an ambition for the global minimum tax to have a limited impact on businesses carrying out economic activities with substance and discussions will continue in respect of the design of the rules in this respect, with a final decision to be made by October 2021.

Implementation will also feature safe harbours and/or other **simplification mechanisms** to avoid disproportionate compliance costs.

### Subject to tax rule

The **subject to tax rule** will allow limited source taxation on related party **interest, royalties and a defined set of other payments**. The rule will be incorporated into bilateral tax treaties by countries that apply nominal rates of tax below a minimum rate to such receipts where requested by developing country members of the Inclusive Framework.

The taxing right will be limited to the difference between the subject to tax minimum rate (between 7.5%-9%) and the tax rate on the payment.

## Implementation

An implementation plan will be agreed including: model income inclusion and undertaxed payment rules with coordination mechanisms; a model Subject To Tax rule, together with a multilateral instrument to facilitate its adoption; and transitional rules, possibly deferring implementation of the undertaxed payment rule.

## Next steps

G20 Finance Ministers will discuss the two-pillar proposals on 9-10 July. Further technical work, including the implementation plan, will be finalised by October 2021, ahead of further Inclusive Framework and G20 Finance Minister meetings. Further technical work on the fixed marketing and distribution function return (Amount B) is scheduled to be completed by the end of 2022.

The new nexus and profit allocation rules (Amount A) will be implemented through a new multilateral instrument which will be available in 2022, and are scheduled to come into effect in 2023. Pillar Two is also scheduled to come into effect in 2023.

If you have any questions, please contact our professionals:

### International and M&A Tax

#### National Leader

**Vicky Wang**

Tax Partner

+86 21 6141 1035

[vicwang@deloitte.com.cn](mailto:vicwang@deloitte.com.cn)

#### Hong Kong

**Jonathan Culver**

Tax Partner

+852 2852 6683

[jculver@deloitte.com.hk](mailto:jculver@deloitte.com.hk)

Get in touch



Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited (“DTTL”), its global network of member firms, and their related entities (collectively, the “Deloitte organization”). DTTL (also referred to as “Deloitte Global”) and each of its member firms and related entities are legally separate and independent entities, which cannot obligate or bind each other in respect of third parties. DTTL and each DTTL member firm and related entity is liable only for its own acts and omissions, and not those of each other. DTTL does not provide services to clients. Please see [www.deloitte.com/about](http://www.deloitte.com/about) to learn more.

Deloitte is a leading global provider of audit and assurance, consulting, financial advisory, risk advisory, tax and related services. Our global network of member firms and related entities in more than 150 countries and territories (collectively, the “Deloitte organization”) serves four out of five Fortune Global 500® companies. Learn how Deloitte’s approximately 330,000 people make an impact that matters at [www.deloitte.com](http://www.deloitte.com).

Deloitte Asia Pacific Limited is a company limited by guarantee and a member firm of DTTL. Members of Deloitte Asia Pacific Limited and their related entities, each of which are separate and independent legal entities, provide services from more than 100 cities across the region, including Auckland, Bangkok, Beijing, Hanoi, Hong Kong, Jakarta, Kuala Lumpur, Manila, Melbourne, Osaka, Seoul, Shanghai, Singapore, Sydney, Taipei and Tokyo.

The Deloitte brand entered the China market in 1917 with the opening of an office in Shanghai. Today, Deloitte China delivers a comprehensive range of audit & assurance, consulting, financial advisory, risk advisory and tax services to local, multinational and growth enterprise clients in China. Deloitte China has also made—and continues to make—substantial contributions to the development of China's accounting standards, taxation system and professional expertise. Deloitte China is a locally incorporated professional services organization, owned by its partners in China. To learn more about how Deloitte makes an Impact that Matters in China, please connect with our social media platforms at [www2.deloitte.com/cn/en/social-media](http://www2.deloitte.com/cn/en/social-media).

This communication contains general information only, and none of Deloitte Touche Tohmatsu Limited (“DTTL”), its global network of member firms or their related entities (collectively, the “Deloitte organization”) is, by means of this communication, rendering professional advice or services. Before making any decision or taking any action that may affect your finances or your business, you should consult a qualified professional adviser.

No representations, warranties or undertakings (express or implied) are given as to the accuracy or completeness of the information in this communication, and none of DTTL, its member firms, related entities, employees or agents shall be liable or responsible for any loss or damage whatsoever arising directly or indirectly in connection with any person relying on this communication. DTTL and each of its member firms, and their related entities, are legally separate and independent entities.

© 2021 Deloitte Touche Tohmatsu in Hong Kong, Deloitte Touche Tohmatsu in Macau, and Deloitte Touche Tohmatsu Certified Public Accountants LLP in the Chinese Mainland. All rights reserved.

**To no longer receive emails about this topic please send a return email to the sender with the word “Unsubscribe” in the subject line.**