# Tax News & Views

## OECD Pillar Two: Side-by-side package released

On January 5, 2026, the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting ("Inclusive Framework") published details of a "side-by-side package" in relation to the Pillar Two global minimum tax rules ("Pillar Two"). The document includes agreed-upon administrative guidance on a side-by-side system, a permanent simplified effective tax rate (ETR) safe harbor, an extension of the transitional country-by-country (CbC) reporting safe harbor, and a substance-based tax incentive (SBTI) safe harbor.

### I. Components of the Pillar Two rules

The Pillar Two global minimum tax rules have been agreed to by more than 140 members of the Inclusive Framework. Jurisdictions are in the process of implementing rules in local legislation, which began to apply starting in January of 2024. The Pillar Two rules apply to large multinational groups with annual consolidated group revenue of at least €750 million, and result in "top-up" tax amounts to bring the overall tax on profits in each jurisdiction where a group operates up to a 15% minimum effective tax rate. The key components are: qualified domestic minimum top-up taxes (QDMTTs), which allow jurisdictions to charge any top-up taxes due with respect to local profits; the income inclusion rule (IIR) under which parent company jurisdictions apply the top-up tax rules on a top-down basis; and the undertaxed profits rule (UTPR), which will apply as a secondary (backstop) rule where the other rules have not been fully applied.

### II. Side-by-side system

The side-by-side (SbS) system consists of two new permanent safe harbors that are available to multinational groups headquartered in jurisdictions recognized by the Inclusive Framework as having an eligible tax regime.

### A. Side-by-side safe harbor

Under a new permanent side-by-side safe harbor ("SbS safe harbor"), no top-up tax will be payable ***under an IIR or a UTPR*** on any undertaxed profits of a member of the MNE Group if the ultimate parent entity (UPE) is located in a jurisdiction with a qualified SbS regime. A group with a UPE located in a jurisdiction that does not have a qualified SbS regime ***cannot apply the safe harbor***, even if the low-tax entity resides in a jurisdiction with a qualified SbS regime.

The SbS safe harbor ***does not apply to QDMTTs***, which will continue to be in effect, including to the overseas operations of groups headquartered in a jurisdiction with a qualified SbS regime.

The Inclusive Framework will maintain a central record of jurisdictions with a qualified SbS regime. ***As of January 5, 2026, the central record confirms that only the United States has a qualified SbS regime.***

It is intended that groups with a UPE located in a jurisdiction that has a qualified SbS regime may elect for the SbS safe harbor to apply for years beginning on or after January 1, 2026 (or a later year as listed in the central record). Jurisdictions that are constitutionally or legally restricted from adopting the safe harbor with retroactive effect must do so instead from the earliest practical date.

A jurisdiction has a qualified SbS regime if it:

- Has an ***eligible domestic tax system*** with:
  - A nominal statutory ***corporate income tax rate of at least 20%*** (taking into account any sub-national corporate income taxes and/or preferential adjustments, ***e.g.***, generally available tax credits, deductions, or exclusions equal to a percentage of the taxable income);
  - A ***QDMTT or corporate alternative minimum tax*** with a nominal rate of at least 15%. A corporate alternative minimum tax must be based on financial statement income. It may be subject to appropriate adjustments consistent with the policy objectives of minimum taxation, but must be applicable to a substantial portion of the profits of in-scope multinational groups' operations in the jurisdiction; and
  - ***No material risk*** that in-scope multinational groups headquartered in the jurisdiction will be subject to an effective rate of tax below 15% on their profits in the headquarter jurisdiction.
- Has an ***eligible worldwide tax system*** that:
  - Has ***a comprehensive tax regime*** applicable to all resident companies ***on overseas income***, including active and passive income of controlled foreign companies (CFCs) and foreign branches, regardless of whether that income is distributed. Limited exclusions consistent with the policy objectives of minimum taxation are permitted, ***e.g.***, exclusions for high-taxed income;
  - Incorporates substantial unilateral mechanisms to ***address base erosion and profit shifting (BEPS) risks***, ***e.g.***, considering inclusions from CFCs that are subject to low taxation separately from those subject to high taxation in the CFC jurisdiction. The regime must preclude foreign tax credits on high tax active income from being offset against a tax liability arising from low tax passive income; and
  - Has ***no material risk*** that in-scope multinational groups headquartered in the jurisdiction will be subject to an effective rate of tax below 15% on the overall profits of their overseas operations.
- Provides ***a foreign tax credit for QDMTTs*** on the same terms as other creditable covered taxes; and
- Enacted its eligible domestic/worldwide tax system prior to January 1, 2026—in which case the Inclusive Framework will assess whether the jurisdiction has a qualified SbS regime by June 30, 2026. The eligibility of tax systems enacted on or after January 1, 2026, will be assessed in a timely manner once the relevant jurisdiction initiates a request in 2027 or 2028, taking into account that the Inclusive Framework considers that the adoption of a coordinated global minimum tax (particularly through the implementation of QDMTTs) is "critically important and should be the primary system."

Further work will be done on revisions to the GloBE information return (GIR) with respect to the SbS safe harbor, including to identify data that may not be required. A group that makes the SbS safe harbor election in a jurisdiction with an IIR or a UTPR will provide the "MNE group information" (section 1 of the GIR) to that jurisdiction but will not be required to complete the high-level summary of GloBE information (***e.g.***, ETR ranges).

### B. UPE safe harbor

In addition to the SbS safe harbor, a new permanent UPE safe harbor applies for years beginning on or after January 1, 2026, and effectively replaces the transitional UTPR safe harbor, which expired at the end of 2025. If that jurisdiction has a qualified UPE regime, groups may elect to apply the UPE safe harbor such that no top-up tax will be payable under the UTPR on any undertaxed profits in the UPE jurisdiction. The UPE safe harbor does not affect the application of the IIR or UTPR with respect to any constituent entities located outside of the UPE jurisdiction and has no impact on the operation of QDMTTs.

A jurisdiction has a qualified UPE regime if it has an eligible domestic tax system enacted and in effect on January 1, 2026. In line with the approach for the SbS safe harbor, a qualified UPE regime must have a nominal statutory corporate income tax rate of at least 20%, a QDMTT or corporate alternative minimum tax with a nominal rate of at least 15%, and no material risk that in-scope multinational groups headquartered in the jurisdiction will be subject to an effective rate of tax below 15% on their profits in the headquarter jurisdiction.

The Inclusive Framework will publish a central record of jurisdictions with a qualified UPE regime. As of January 5, 2026, no jurisdictions are listed as having such a system.

### III. Simplified ETR safe harbor

The side-by-side package also provides a new permanent simplified ETR safe harbor that seeks to reduce the compliance burden associated with Pillar Two in a "meaningful share" of jurisdictions in which in-scope groups operate.

Under the permanent ETR safe harbor, where the calculation of a "simplified ETR" for a "tested jurisdiction" is at least the Pillar Two minimum rate (***i.e.***, 15%), or where it has an overall "simplified loss," the Pillar Two top-up tax for the entities in that jurisdiction will be zero. Note that a group may have multiple separate safe-harbor tested jurisdictions for a given country and therefore a requirement to calculate separate simplified ETRs for the safe harbor if, for example, there are entities such as joint ventures and minority-owned entities.

The simplified ETR is calculated as the "simplified taxes" amount divided by the "simplified income" amount. Both amounts are based on financial accounting data used to prepare the group's consolidated financial statements and therefore, unlike the existing transitional CbC reporting safe harbor, ***no data points will be taken from a group's CbC report***. The simplified ETR calculations of jurisdictions whose QDMTT rules require use of local financial accounting standards will also be based on the local standard, but jurisdictions are encouraged to allow groups to elect to use the financial accounting standards used for the consolidated financial statements. Groups may compute the simplified ETR using available jurisdictional-level data and do not need to determine all tax and income amounts on a separate-entity basis first.

Under this safe harbor, the calculation rules for simplified income and simplified taxes each include a small number of mandatory adjustments, alongside a variety of other adjustments, some of which are dependent on specific facts and circumstances, and others that are entirely optional at the election of the business. These adjustments are designed to allow as many groups as possible to meet the safe harbor requirement in as many jurisdictions as possible (in circumstances where there would be no top-up tax under the main rules).

Calculation of simplified income starts from aggregate jurisdictional profit before tax, defined by reference to main Pillar Two rules concepts such as the "financial accounting net income or loss" (FANIL). Three "basic" adjustments, based on equivalent main Pillar Two rules, are then required to remove "excluded dividends" and "excluded equity gains or losses," and add back policy disallowed expenses (such as fines and penalties of €250,000 or more). The Inclusive Framework expects that, in many cases, these will be the only adjustments required.

Additional adjustments or simplifications include industry adjustments for certain financial services and shipping entities, and conditional adjustments for "equity-reported items" and an "M&A simplification." Additional optional adjustments to better align simplified income with local tax bases are available, including several based on elections under the main Pillar Two rules.

Simplified taxes are the current and deferred taxes accrued in the FANIL of the constituent entities in the tested jurisdiction, subject to adjustments with respect to items such as non-covered tax amounts, taxes related to amounts excluded from the simplified income calculation, uncertain tax positions, and current tax not expected to be paid within three years. Deferred tax expense movements relating to deferred tax liabilities that would need to be tracked under the main Pillar Two "recapture rule" generally are excluded. Other deferred tax-specific safe harbor adjustments include a simplified methodology to recast deferred tax expenses at 15%, simplified adjustments for negative taxes in simplified loss years, and the disregarding of any accounting valuation allowances or recognition adjustments. A number of optional elections may also be made, including to obtain the benefit of qualified refundable tax credits (QRTCs) and marketable transferable tax credits (MTTCs), and the new substance-based tax incentive safe harbor (see below). Additional guidance is provided with respect to determining the Pillar Two transition year for a jurisdiction and the application of the main Pillar Two rules' transition provisions (Article 9.1) for purposes of the safe harbor, as well as the impact of tax adjustments after year end.

The simplified ETR safe harbor contains specific transfer pricing rules, including an election to enable the calculations to be based on the arm's length pricing used to compute taxable income in local tax returns, in line with transfer pricing policies. The safe harbor also includes a simplified approach for the cross-border allocation of income and taxes (***e.g.***, with respect to permanent establishment amounts), and additional specific rules for tax-neutral UPEs, tax transparent entities, stateless entities, and investment entities.

The safe harbor also includes integrity rules that may require additional adjustments to be made to produce outcomes consistent with four principles: matching intragroup income and expenses; fully allocating all income to a tested jurisdiction; deducting expenses and losses only once and in a single tested jurisdiction; and recording tax amounts only once and in a single tested jurisdiction.

The safe harbor will first be available to groups for years commencing on or after December 31, 2026 (i.e., for tax years beginning in 2027). The safe harbor may also be available one year earlier, for years commencing on or after December 31, 2025 (***i.e.***, for 2026), but only where all the jurisdictions with Pillar Two taxing rights over the tested jurisdiction have implemented early.

A group may elect for the simplified ETR safe harbor to apply for a tested jurisdiction for the first time only if there were no top-up tax liabilities for the tested jurisdiction for all years beginning in the preceding 24 months (***i.e.***, the previous two years). A tested jurisdiction may fall in and out of the scope of the safe harbor (***i.e.***, the rules ***do not follow the "once-out always-out" approach*** of the transitional CbC safe harbor). A similar 24-month condition applies where a business wishes to re-enter the safe harbor rules in subsequent years.

## IV. Extension of transitional CbC reporting safe harbor

The Inclusive Framework has agreed upon a 12-month extension of the existing transitional CbC reporting safe harbor. The CbC safe harbor originally applied for the first three years of Pillar Two only, ceasing to be available from 2027 onwards. The CbC safe harbor will now be available for years beginning on or before December 31, 2027. The 17% transitional rate applicable to the CbC safe harbor's "effective tax rate test" in 2026 will also apply to the test in 2027.

## V. SBTI safe harbor

The Inclusive Framework has adopted a new permanent SBTI safe harbor to allow groups to "benefit from certain tax incentives that are strongly connected to economic substance" in a jurisdiction.

The SBTI safe harbor will allow businesses to elect for a top-up tax amount, corresponding to "qualified tax incentives" (QTIs) used by constituent entities in a jurisdiction in a year, to be reduced to zero. The calculation of top-up tax amounts "corresponding to" a QTI is based on the reduction in total top-up tax payable that would arise for the jurisdiction if the QTIs used were treated as additional adjusted covered tax amounts paid. This calculation is subject to a "substance cap" rule, limiting the benefit where there are insufficient levels of payroll costs and tangible assets in the country.

### A. Qualified tax incentives

To be a qualified tax incentive, an incentive must be "generally available" to taxpayers (***e.g.***, excluding any incentives limited only to those businesses within the scope of Pillar Two and those arising from a discretionary arrangement between the group and a government).

A QTI must be either an expenditure-based or production-based tax incentive:

- An "expenditure-based tax incentive," ***e.g.***, in the form of a tax credit, an additional tax deduction, or an exemption, must be calculated directly by reference to the expenditure incurred (***i.e.***, based on a portion of qualifying expenditure). The value of the incentive must not exceed the amount of expenditure incurred (taking into account any other tax incentives provided with respect to the same item of expenditure). Allowances for capital expenditure that give rise to timing differences only are not QTIs. However, where an allowance provides tax relief in excess of the original capital investment (***e.g.***, a super deduction), the excess may be considered an expenditure-based tax incentive for QTI calculation purposes.

- A "production-based tax incentive" must be calculated ***based on volume (not value)*** of production of tangible property (including production of electricity and processing activities such as extraction and refining) in a jurisdiction. It must also be based on units produced in the jurisdiction providing the incentive.

Tax incentives that reduce the liability for a non-covered tax are excluded, as are tax incentives that apply only to expenditures incurred in producing income that is excluded from the scope of Pillar Two income, or incentives in the form of subsidies and grants. An election may be made to treat a QRTC or an MTTC, as defined in previous Pillar Two administrative guidance, as a QTI for Pillar Two purposes instead of a QRTC or MTTC (provided that the credit qualifies as an expenditure- or production-based tax incentive).

A QTI must be calculated based on expenditure that has been incurred (***i.e.***, accrued or paid), or output that has been produced, by the time that the amount of the incentive is determined. Incentives based on future expenditure or production or calculated with respect to expenditure or production before the incentive was in effect, are excluded.

### B. Substance cap

The substance cap limits the notional increase to adjusted covered taxes from the use of QTIs to an amount equal to the greater of 5.5% of eligible payroll costs of employees performing activities in the jurisdiction and 5.5% of the depreciation and depletion of eligible tangible assets located in the jurisdiction. An alternative cap, equal to 1% of the carrying value of eligible tangible assets in the jurisdiction (excluding land and other non-depreciable assets), is available via a five-year election.

Businesses can elect to apply the SBTI safe harbor in a jurisdiction for years beginning on or after January 1, 2026.

## VI. Next steps

### A. Work program for additional simplification

The Inclusive Framework has committed to a work program for further clarification and simplification of the Pillar Two rules, including:

- Completion of work on a permanent routine profits test and ***de minimis*** test (scheduled for completion in the first half of 2026);
- Further simplification of the main Pillar Two rules, focusing on continuity issues, to ensure businesses may benefit from the ETR safe harbor simplifications even where, in a subsequent year, they may not qualify;
- Further administrative guidance on technical issues; and
- Exploring integration of the simplified calculations in the simplified ETR safe harbor into the main rules.

Further work will also be undertaken on streamlining reporting obligations, including consideration of adaptations to the GIR, to be completed in the first half of 2026, to allow jurisdictions to adopt changes for years in which the safe harbors apply.

### B. Stocktake

Inclusive Framework members will agree on a process for an evidence-based "stocktake" of the side-by-side system (including the level of implementation of QDMTTs), to be concluded by 2029, to ensure that any substantial risks that might be identified with respect to the level playing field or BEPS are addressed to preserve the common policy objectives of Pillar Two and the side-by-side system. The Inclusive Framework commits to take action to address any such substantial risks identified, as well as to consider targeted solutions targeted at more concentrated risks. The Inclusive Framework will also look to identify opportunities for alignment and simplification, ***e.g.***, alignment of qualified UPE regimes with QDMTTs.

### C. Reinforcing effectiveness of QDMTTs

The Inclusive Framework will continue to work on reducing compliance burdens, including identifying possible opportunities for further coordination for businesses with operations in QDMTT jurisdictions.

The Inclusive Framework will work on ensuring that conditional or discriminatory taxes are not recognized as covered taxes, with the qualified status of domestic minimum top-up taxes remaining dependent on their "consistent and non-discriminatory application" to businesses, regardless of whether a business has elected to apply the SbS safe harbor.

## VII. Deloitte comments

The Inclusive Framework's long-awaited side-by-side-package introduces a number of welcome simplifications to the Pillar Two global minimum tax regime. These are set out as safe harbors from the Pillar Two rules, an option preferred by the European Commission and considered within the scope of the existing European Union directive implementing the global minimum tax.

The side-by-side safe harbor and the UPE safe harbor look at jurisdictions' existing tax regimes and seek to minimize duplication where these are sufficiently similar, in policy aims and outcomes, to the Pillar Two rules. The side-by-side safe harbor is particularly impactful to US multinationals and was the subject of a G7 agreement reached in June of 2025. It effectively alleviates US-headed groups from the "international" aspects of Pillar Two (the IIR and UTPR pieces) ***from 2026 onwards***, on the basis that US groups are subject to the net controlled foreign corporation tested income (formerly GILTI) and corporate alternative minimum tax regimes in the United States (***i.e.***, US MNE Groups are still subject to applicable IIR and/or UTPR obligations for tax years beginning before 2026). Notably, it appears that all US-located UPEs may qualify for the SbS safe harbor, even if those UPEs are not subject to one or more eligible tax rules (***e.g.***, US partnerships and S corporations).

It may be that other jurisdictions are able to take advantage of the side-by-side safe harbor (or UPE safe harbor) in the future, but currently only the United States is listed as qualifying. It is important to note that the SbS safe harbor is predicated on many jurisdictions having introduced the domestic Pillar Two rules via QDMTTs, and US groups will, as with all other groups within the scope of Pillar Two, continue to have to comply with QDMTT requirements in local jurisdictions for all years.

The additional safe harbors cover several key areas of broad application and apply to any group within the scope of Pillar Two. These safe harbors remain relevant for US MNEs who are subject to one or more QDMTTs, as well as US subsidiaries of foreign-parented groups.

At more than 50 pages in length, the simplified ETR safe harbor contains a number of provisions that are designed to help groups reach safe harbor status in as many jurisdictions as possible, negating the need for additional data and reporting for the "full" rules. The challenge will be that groups will have to consider jurisdictions, or groups of jurisdictions, differently, as some will require more adjustments than others to qualify. There is also an extension of the existing CbC reporting safe harbor for one year, to allow time for jurisdictions to legislate for the new simplified ETR safe harbor.

The substance-based incentives safe harbor, which applies beginning in 2026, looks to provide relief from Pillar Two top-up tax where there are tax credits that arise from incentives calculated by reference to either expenditure or production output (as opposed to those where the credit is calculated by reference to income that is then exempt). This new safe harbor also lessens the distinction between refundable and nonrefundable tax credits. In each case, the amount is capped (at the jurisdiction level) based on the amount of payroll costs or tangible assets in the jurisdiction.

The Inclusive Framework makes clear in the publication that further simplification work will be carried out on Pillar Two. This will include not only permanent safe harbors covering substance-based income and ***de minimis*** amounts, but also further work on simplifying and aligning compliance and reporting obligations. Further work will be undertaken with a view to publishing an updated GIR by June 30, 2026, to apply the new safe harbors and simplifications. This suggests there may be a GIR (1) that is used for compliance for 2024 and 2025 (taking into account that in accordance with the OECD timetable, the first December 31, 2024, returns are due by June 30, 2026), and a new GIR (2) that is used for 2026 onwards, but this is subject to confirmation.

The side-by-side package represents significant work by Inclusive Framework members to agree to political positions and to accept safe harbors where possible. Perhaps inevitably, this means that other areas of uncertainty have not yet had the airtime to reach agreement. This includes further work on technical areas of the Pillar Two regime, for example, possible adjustments arising from hyperinflationary environments and further work on a dispute resolution mechanism suitable for Pillar Two. It is expected that these will continue to be worked on and reports released by the OECD as soon as possible.

### Potential Financial Statement Impacts of side-by-side package

The side-by-side package constitutes new information that should be considered in the reporting period that includes the issuance date. In some instances, this may result in a change in tax law in the reporting period that includes the issuance date to the extent a jurisdiction automatically incorporates OECD guidance into enacted tax law. Conversely, many jurisdictions will have to formally adopt the side-by-side package through a change in tax law. US GAAP requires a change in tax law to be recognized in the reporting period that includes the date of enactment; therefore, monitoring enactment of these new safe harbors will be important. One issue of note is that there may, subject to jurisdictions' legislative processes and timetables, be a disconnect between the timing of the new safe harbors being enacted for financial statement purposes, and the years to which the safe harbors will ultimately apply. For example, the side-by-side safe harbor is intended to take effect on January 1, 2026, but may not be enacted in some, perhaps many, jurisdictions until 2027. Accordingly, this may mean that financial statements for periods ending prior to enactment require the accrual of Pillar Two top-up taxes even where these ultimately may be alleviated by subsequent enactment of legislation incorporating the new safe harbors.

Additionally, the enactment of the new safe harbors may impact the valuation allowance assessment for companies that elected to consider the impact of Pillar Two in the valuation allowance of regular tax DTAs. See Deloitte's Financial Reporting Alert 24-1 Frequently Asked Questions About "Pillar Two" for more information.

**Potential disclosures:** If enactment occurs after the balance sheet date, but before the issuance of the financial statements, entities should consider whether a subsequent event disclosure would be required to keep the financial statements from being misleading (see ASC 855-10-50-2).

In addition, SEC Regulation S-K, Item 303(a)[1], requires entities to provide certain forward-looking information related to "material events and uncertainties known to management that are reasonably likely to cause reported financial information not to be necessarily indicative of future operating results or of future financial condition." Accordingly, entities subject to these rules should consider disclosing, when material, the anticipated future impact of newly enacted laws, as well as those expected to be enacted, on their results of operations, financial position, liquidity, and capital resources.

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1 SEC Regulation S-K, Item 303(a), "Management's Discussion and Analysis of Financial Condition and Results of Operations: Objective."

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