

Frequently Asked Questions on Pillar 2 Directive

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General Questions Pillar 2 Directive

- **Question 1**

Will an implementation regulation be issued which would help MSs in administrative proceedings. Can additional information (timeframe, type of provision) be provided regarding the announced list of third country jurisdictions with qualified regimes?

- **Response**

It is currently not intended to issue some form of implementation regulation for purposes of the Directive.

For the necessary tax certainty for MNEs being in the scope of the Directive and preparing for the application of the minimum effective taxation rules for the fiscal year beginning on 31.12.2023 or later, the OECD is intending to issue a list which includes the jurisdictions with a “Qualified” IIR, UTPR and DMTT and jurisdictions that qualify for the QDMTT safe harbour (based on a transitional legal review).

- **Question 2**

Can a General Government that is a legal person be an UPE for purposes of the Directive?

- **Response**

It is our understanding that even when a central state is a legal person, it cannot be considered an UPE for the purposes of the Directive.

- **Question 3**

Can a Member State where only one constituent entity of a foreign ultimate parent entity is located implement the Directive in a way so that a qualified domestic top-up tax is computed based on an entity-by-entity level in its territory and skip the jurisdictional blending?

- **Response**

When there is a single constituent entity located in the jurisdiction, the jurisdictional blending approach is equivalent to an entity-by-entity approach.

When there are several constituent entities, the jurisdictional blending should in principle apply by aggregating the income and taxes of those entities.

- **Question 4**

For purposes of a qualified domestic top-up tax, can Member States apply a full jurisdictional blending which would include joint-ventures and joint-venture with the “standard” constituent entities?

- **Response**

A jurisdictional blending whereby joint-ventures and joint-venture subsidiaries would be blended with other constituent entities that are located in the same jurisdiction would be problematic as it could result in a different overall qualified domestic top-up tax amount than in case of two separate calculations. In this respect, reference is made to Article 36(3) of the Directive.

In accordance with Recital 24 of the Preamble to the Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Directive to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

The Administrative Guidance issued in February 2023 on QDMTT clarifies in paragraph 118.7 and 118.33 that the ETR and top-up tax of joint-ventures and joint-venture subsidiaries has to be computed separate from other constituent entities in the same jurisdiction.

- **Question 5**

If the Euro-denominated thresholds included in the Directive are denominated in a different currency in the implementation law of a Member State, should such Member State rebase those non-Euro denominated thresholds annually and if yes, how should it do so?

- **Response**

In accordance with Recital 24 of the Preamble to the Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

In the Directive, all thresholds are denominated in Euro's. However, a non-Euro denominated threshold should be possible if those thresholds are rebased annually. This view also forms part of the OECD Commentary to the Model Rules. Rebasing the non-euro denominated thresholds in the way proposed in the Administrative Guidance [AG22.04T18] is considered to be in line with the Directive.

- **Question 6**

How should qualified domestic top-up tax and UTPR be allocated among the constituent entities that are located in a jurisdiction?

- **Response**

The allocation of qualified domestic top-up tax and UTPR is left to the discretion of the Member States. Implementing an allocation approach that is in line with the allocation approach already included in the Directive should in any event be acceptable.

Chapter 1: General Provisions

ARTICLE 2

- **Question 1**

What does “value of the entity” used in Article 2(3)(b) and (c) of the Directive mean?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

It appears that the Commentary to the OECD Model Rules (Ch. 1, par. 47-51), could be used for the interpretation of the notion of ‘value of the entity’ used in Article 2(3)(b) and (c) of the Directive.

- **Question 2**

On the basis of Article 2 of the Directive where one or more of the four fiscal years is longer or shorter than 12 months, the revenue threshold shall be adjusted proportionally. Should the proportion be calculated on a monthly or a daily basis?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

It appears that the Commentary to the OECD Model Rules (Ch. 1, par. 15), could be used as a guidance on how the recalculation could be made.

- **Question 3**

Does holding assets or buying funds by an excluded entity within the meaning of Article 2(3)(b)(i) of the Directive include borrowing funds from third parties and making acquisitions of assets?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

The Administrative Guidance on ‘Clarifying the definition of Excluded Entity’ clarifies that borrowing funds and making direct acquisitions of assets falls within the meaning of “holding of assets or investment of funds”.

- **Question 4**

What does the term “almost exclusively” in the definition of an excluded entity in Article 2(3)(b) mean?

Are Member States entitled to specify the term “almost exclusively” in their national legislation (in particular with respect to QDTT), by reference to e.g. at least 90%-95% of revenue obtained from such operations or at least 90%-95% of assets connected to such operations?

What does the term “substantially all of its income” Article 2(3)(c) mean?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

Paragraphs 1.1.3, 1.5.1, 1.5.2 of the OECD Commentary and the corresponding paragraphs of the AG offer flexibility on the definition of an excluded entity:

“The provisions, when interpreted strictly, may prevent an entity from falling within the definition of Excluded Entity, where it only undertakes activities that consist of the holding of assets or investment of funds for the benefit of an Excluded Entity and carries out activities that are ancillary to those carried out by the relevant Excluded Entity.”

- **Question 5**

Does the central state or state treasury qualify as a legal person (“an ultimate parent entity”) for the purpose of the Directive?

- **Response**

When a central state or the State Treasury is a legal person, it cannot be considered as an ultimate parent entity for the purposes of the Pillar 2 Directive.

ARTICLE 3

- **Question 1**

Does the term “entity” mean any legal arrangement that prepares separate financial accounts or any legal person?

- **Response**

A legal person is indeed considered as an entity even if it does not prepare financial accounts.

The precondition to apply the Pillar 2 Directive rules is the existence of financial accounts. The definition of a legal person in the Pillar 2 Directive does not refer explicitly to financial accounts for legal persons since there is a presumption that they prepare such financial accounts (or that consolidating entities will do so).

- **Question 2**

Are “excluded entities” considered as constituent entities?

- **Response**

The “excluded entities” are not subject to the Pillar 2 Directive rules, except for the purposes of calculating the revenue threshold, to see whether a group falls within the scope. The excluded entities have to first be brought under the scope of the Pillar 2 Directive via Article 2(1). Subsequently, in Article 2(3), it is determined that the Directive does not apply to Excluded Entities.

- **Question 3**

What is the meaning of “deemed consolidation test” under Article 3(6)(d) of the Directive?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

Further clarification on the deemed consolidation test is provided in the Administrative Guidance [AG2022.04.T3].

- **Question 4**

If a sovereign wealth fund meets the definition of a governmental entity in Article 3(9) of the Directive, is it correct understanding that it should not be considered an UPE and should not be considered part of a MNE group?

- **Response**

In accordance with Recital 24 of the Preamble to the Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

The Administrative Guidance on ‘1.4 Sovereign wealth funds and the definition of Ultimate Parent Entity’ clarifies that a sovereign wealth fund that meets the definition of a governmental entity will not be considered to be an UPE and will not be considered part of a MNE Group.

- **Question 5**

Does “the private person” in the definitions of Article 3(9-11) include only private individuals or does it include not only private individuals but also in general non-governmental entities as well?

- **Response**

The reference to ‘private person’ in the definitions ‘governmental entity’ (Article 3(9)), ‘international organisation’ (Article 3(10)) and ‘non-profit organisation’ (Article 3(11)) covers both natural persons and legal persons.

- **Question 6**

What does taxing income on a net basis within the definition of permanent establishment mean?

- **Response**

Taxation on a net basis involves deductibility of expenses. With this condition, source-based taxation on a gross basis (e.g. withholding taxes) is excluded from the application of Article 3(13)-(b).

- **Question 7**

Can an insurance investment entity be an IPE within the meaning of Article 3 (20) or a POPE within the meaning of Article 3 (22) of the Directive?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

Considering the recent Administrative Guidance *“3.2. Exclusion of Insurance Investment Entities from the definition of Intermediate Parent Entity and Partially-Owned Parent Entity”* and in order to preserve the tax neutrality vis-à-vis minority interest-holders, it appears that the definitions of IPE and POPE should not include insurance investment entities.

- **Question 8**

‘Partially-owned parent entity’ means a constituent entity that owns, directly or indirectly, an ownership interest in another constituent entity of the same MNE group or large-scale domestic group, and for which more than 20 % **of the ownership interest in its profits** is held, directly or indirectly, by one or several persons that are not constituent entities of that MNE group or large-scale domestic group and that does not qualify as an ultimate parent entity, a permanent establishment or an investment entity;

Does this mean that the non-group owners are entitled to more than 20% of the profits (irrespective, if they have a lower share in the capital)?

- **Response**

Ownership interest means any equity interest that carries rights to the profits, capital or reserves of an entity, including the profits, capital or reserves of a main entity’s permanent establishment(s). The definition of ‘partially-owned parent entity’ is triggered if persons or entities outside of the group are entitled to more than 20% of the profits of an entity that meets the other requirements of the POPE definition (irrespective, of whether those persons or entities have a lower share in the capital of that entity).

- **Question 9**

How should preference shares that are accounted for as debt in the constituent entity’s financial accounts be considered for the purpose of ‘ownership interest’ under Article 3(23)?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across

Member States to the extent that those sources are consistent with this Directive and Union law.

In the Commentary to the OECD Model Rules (Ch. 10, par. 85), further explanation is provided on the term equity interest. It is stated that an equity interest is an interest that is accounted for as equity under the financial accounting standard used in the preparation of the Consolidated Financial Statements. This would mean that for the treatment of preference shares the treatment under the financial accounting standard used in the preparation of the Consolidated Financial Statements is decisive.

- **Question 10**

Assume that the following two different types of accounting regulations exist in a Member State:

1. accounting regulations which transpose the provisions of the Directive 2013/34/EU of the European Parliament and of the Council on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings; and
2. accounting regulations complying with IFRS, as adopted by the Union pursuant to Regulation (EC) No 1606/2002.

Are these standards acceptable financial accounting standards or authorized financial accounting standards?

- **Response**

Both sets of standards fit with the definition of acceptable financial accounting standard.

- **Question 11**

Does the condition of Article 3 (31) (b) defining ‘an investment fund’ require the investment policy to be fixed? Does the duration of the investment policy and the life of the fund need to be finite?

- **Response**

The content of the investment policy is not regulated by the Pillar 2 Directive.

- **Question 12**

Do unregulated funds which may still be considered as Alternative Investment Funds, to the extent that they are subject to Anti-Money Laundering and investor protection rules (though limited when compared to regulated funds) fall under the definition of ‘investment fund’ (in light of Article 3(31)-(f))? Does the reference to the “regulatory regime” refer to the need to obtain approval/authorization from the competent authorities/regulators? What would be the treatment of Registered funds (e.g. RAIFs) whose fund managers are regulated per se and the funds are subject to a lighter oversight regime?

- **Response**

The treatment of unregulated funds must be analysed and treated by the Member State depending on their own regulatory requirements.

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

In addition, in the Commentary to the OECD Model Rules (Ch. 10, par. 44), further explanation is provided on the requirement of being subject to the regulatory regime.

- **Question 13**

Do funds managed by their own government body, consisting of fit and proper directors meet the requirement of Article 3(31)-(g).

- **Response**

In general, investors and fund managers should not be the same person, only in exceptional cases and then it is up to the Member State to evaluate.

- **Question 14**

What is the meaning of the terms “widely held entity” or “holds predominantly immovable property” in the definition of ‘Real estate investment vehicle’?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

The terms “widely held entity” or “holds predominantly immovable property” are partially defined in the Commentary (Chapter 10, paragraph 145 and 148).

A widely held entity is one that has many owners that are not connected persons. A real estate investment vehicle that is owned directly by a small number of other widely held investment entities or pension funds that have numerous beneficiaries is considered to be widely held. An entity that holds predominantly immovable property, either directly or indirectly via securities (or a combination of the two) will meet the condition of the definition.

Member States implementing these definitions may specify more concretely the meaning of “a widely held entity” or “holds predominantly immovable property” depending on the national regulations.

- **Question 15**

Are the conditions set out in (b), (c) and (d) of Article 3(37) alternative to each other but cumulative with that set out in (a)?

- **Response**

The conditions of Article 3(37) are not cumulative (i.e. it is sufficient if one of the conditions is fulfilled).

- **Question 16**

The essential part of the “qualified refundable tax credit” definition is that it becomes refundable within four years, as a cash payment or cash equivalent. A “non-qualified refundable tax credit” means a tax credit that is not a qualified refundable tax credit but is refundable in whole or in part. Do “qualified refundable tax credit” and “non-qualified refundable tax credit” cover only tax preferences that constitute a direct decrease of tax or refund of tax due? In other words, do they cover tax preferences that allow for an additional deduction from the tax base?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

In the Commentary to the Model Rules (Chapter 3, paragraph 110), it is explained that refundable tax credits are *‘incentives to engage in certain activities, such as research and development, whereby the government allows the company to offset its taxes dollar-for-dollar for engaging in specified activities or incurring specified expenditures or the government will refund the amount of the unused credit if the company doesn't have any tax liability. In this way, the government effectively pays for the activity or expenditure in a similar manner to a grant.’*

It seems that tax preferences that allow for an additional deduction from the tax base and could not lead to a refund of tax due are not a tax credit and therefore cannot be considered as a refundable or a non-refundable tax credit.

ARTICLE 4

- **Question 1**

Article 4(7) concerns the change of the location of a constituent entity in the course of a fiscal year. Should the “change of the location” be understood narrowly (as a rule possible only for a European Company / SE or possible under the Directive 2019/2121), or it also encompasses the change of the location involving the procedure of liquidation? The domestic law may in practice require liquidation of the company planning to change the seat - should such potential cases be covered?

- **Response**

Article 4(7) of the Directive refers to cases where a constituent entity changes its location during a fiscal year. In that case, the constituent entity is deemed to be located in the jurisdiction where it was located at the beginning of that fiscal year. This could for example be the case when an entity that is not a flow-through entity moves its place of management to another jurisdiction during a fiscal year. A liquidation of an entity doesn't result in a change of location. Also, the liquidated entity would no longer be included in the consolidated financial statements of the group.

- **Question 2**

What is the meaning of “*the amount of tax paid in accordance with a controlled foreign company tax regime*” under Article 4(5) of the Directive.

- **Response**

Article 4(5) of the Directive applies where a constituent entity is located in two jurisdictions, which have no tax treaty in place. In order to determine the location of this constituent entity for Pillar 2 purposes, the jurisdiction that charged the higher amount of covered taxes for the fiscal year is considered to be the jurisdiction where the constituent entity is located.

If this constituent entity paid any tax in accordance with a controlled foreign company tax regime, this tax is to be excluded from the covered taxes for this purpose. As CFC tax is, in general, not levied on entities that are located in the same jurisdiction, the CFC-owner should therefore not be paying tax on an entity located in the same jurisdiction.

Chapter 2: IIR and UTPR

ARTICLE 9

- **Question 1**

What is the meaning of “acceptable financial accounting standard” under Article 9(2) of the Directive?

In particular, what if either (a) the ultimate parent entity did not prepare consolidated financial statements or (b) the ultimate parent entity’s consolidated financial statements were prepared using an authorised accounting standard which is not an acceptable financial accounting standard?

Should Article 9(2) be interpreted as referring to the consolidated financial statements prepared using the authorised financial accounting standard as adjusted to prevent any material competitive distortion?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

It appears that Paragraph 32 of the OECD Commentary to Article 2.2.3 could be relevant, so that where the ultimate parent entity does not prepare consolidated financial statements, the deemed consolidated financial statements are relevant.

Article 9(2) could be interpreted as referring to the consolidated financial statements prepared using the authorised financial accounting standard as adjusted to prevent any material competitive distortion.

ARTICLE 11

- **Question 1**

How should a QDTT take into account ownership level within a group where:

- i. a CE may not be 100% owned within the group,
- ii. there are minority owned CEs,
- iii. there are Joint Ventures?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

It seems that paragraphs 118.6 -118.8 and 118.10 of OECD (2023), *Tax Challenges Arising from the Digitalisation of the Economy – Administrative Guidance on the Global Anti-Base Erosion Model Rules (Pillar Two)*, OECD/G20 Inclusive Framework on BEPS, OECD, Paris dated 1 February 2023 could be considered here.

ARTICLE 14

• Question 1

After the meeting, we still don't have clarity on the actual application of the various paragraphs of art. 14. If possible, a practical example would be very helpful at a further stage.

○ Response

Article 14 Pillar 2 Directive consists of the following paragraphs:

Par 1: $UTPR\ Top-up\ Tax\ Amount = Total\ UTPR\ Top-up\ Tax \times UTPR\ \%$ (2.5.1 OECD MR)

Par 2: Total UTPR Top-up Tax is the top-up tax computed for each low-taxed CE in accordance with article 27, subject to par. 3 and 4 (2.5.1 OECD MR)

Par 3: The UTPR Top-up Tax is zero, if all UPE's ownership interest are held by parents applying a qualified IIR (2.5.2 OECD MR)

Par 4: The UTPR Top-up Tax shall be reduced by share of top-up tax that is already brought into charge under a qualified IIR (2.5.3 OECD MR)

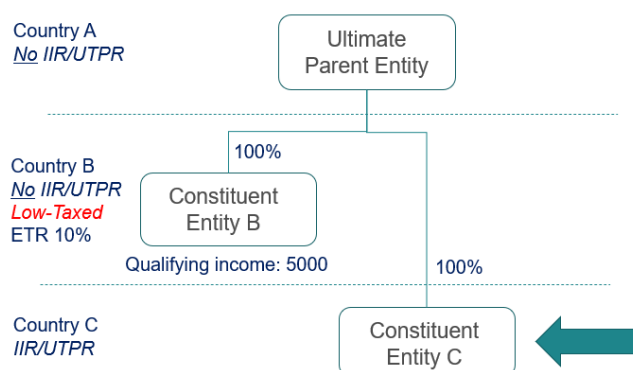
Par 5: Formula to determine the UTPR % (2.6.1 OECD MR)

Par 6&7: Explanation on the definitions used in the formula (2.6.2 OECD MR)

Par. 8: UTPR % shall be deemed to be zero, if UTPR Top-up Tax Amount allocated to a jurisdiction in a prior year has not yet resulted in an equivalent additional cash tax expense in that jurisdiction. Exclude elements from the formula. (2.6.3 OECD MR)

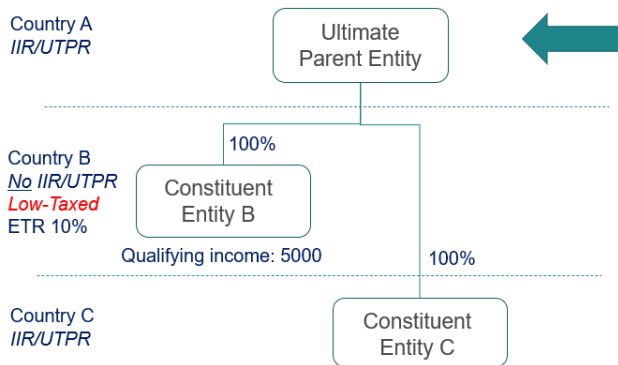
Par. 9: Irrespective of par. 8, UTPR % shall not be deemed to be zero, if this would mean that all jurisdictions would have a zero %. (2.6.4 OECD MR)

Example UTPR – art. 14(1) and 14(2):



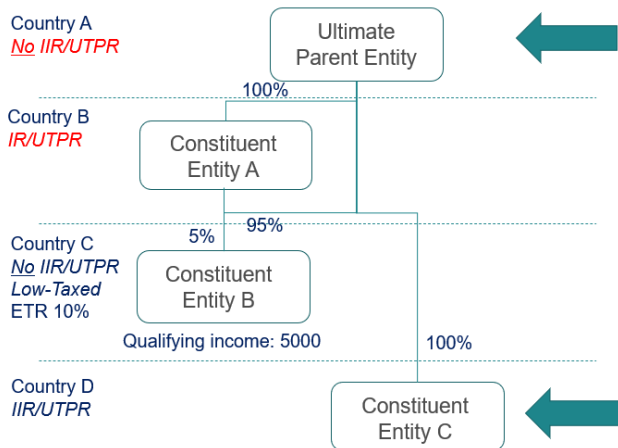
- The UPE is located in a jurisdiction that **does not** apply the IIR
- **Effective Tax Rate** Country B: 10%
- **UTPR Top-up Tax:** 250
[5000 * (15% - 10%)]
- CE C is subject to UTPR top-up tax of 250 in relation to CE B

Example UTPR – art. 14(3):



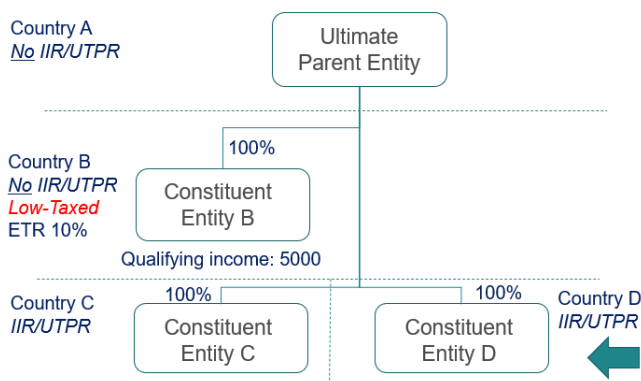
- The UPE is located in a jurisdiction that **does** apply the IIR
- **Effective Tax Rate** Country B: 10%
- **IIR Top-up Tax:** 250
[5000 * (15% - 10%)]
- **UTPR Top-up Tax:** 0
- Based on par. 3, the UTPR Top-up Tax is **zero**, as UPE applies a qualified IIR

Example UTPR – art. 14(4):



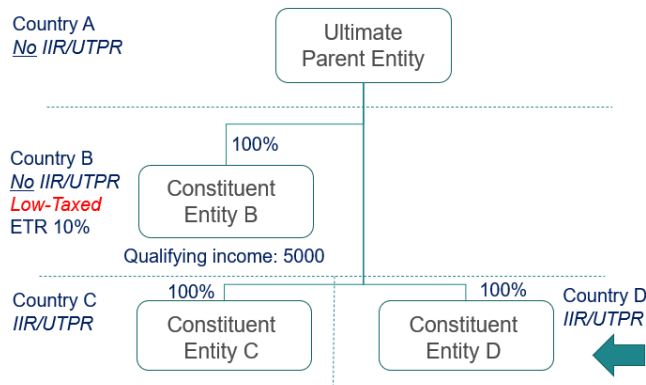
- The UPE is located in a jurisdiction that **does not** apply the IIR
- **Effective Tax Rate** Country C: 10%
- **IIR Top-up Tax:** 12.5
[5000 * (15% - 10%) * 5%]
- **UTPR Top-up Tax:** 237.5
[5000 * (15% - 10%) - 12.5]
- Based on par. 4, the UTPR Top-up Tax shall be **reduced** by share of top-up tax that is **already brought into charge under a qualified IIR**

Example UTPR – art. 14(5):



- The UPE is located in a jurisdiction that **does not** apply the IIR
- **Effective Tax Rate** Country B: 10%
- **UTPR Top-up Tax:** 250
[5000 * (15% - 10%)]
- Based on par. 5, the UTPR top-up tax of 250 shall be **allocated** among CE C and CE D based on number of employees and tangible assets

Example UTPR – art. 14(9):



- The UPE is located in a jurisdiction that **does not** apply the IIR
- **UTPR Top-up Tax: 250**
[5000 * (15% - 10%)]
- UTPR top-up tax amount allocated to **Country C and D** in a prior fiscal year has not resulted in an additional cash tax expense. As such, **UTPR % is zero for Country C and D.**
- Based on par. 9, the UTPR top-up tax of 250 shall be **allocated** among CE C and CE D based on number of employees and tangible assets

Chapter 3: Computation of the qualifying income or loss

ARTICLE 15

- **Question 1**

Does the adjustment to prevent “any material competitive distortion” under Article 15(5) of the Directive apply to both acceptable and authorized financial accounting standards or only to authorized financial accounting standards?

- **Response**

The reference to the adjustment to prevent material competitive distortions relates only to the use of an authorised accounting standard.

- **Question 2**

What is the relationship between Article 11(1) and Article 15(5) of the Directive?

- **Response**

Both provisions refer to the situation of a QD(M)TT being imposed. Article 11(1) of the Directive sets the general rules and conditions for a Member State that has elected to apply, within the EU, a QDTT. It clarifies that the “domestic excess profit” can be computed based on an accounting standard different from the one used for the consolidation, under certain conditions. Article 15(5), mirroring what is stated under Article 11(1), third subparagraph of the Directive, generally opens up the possibility for a constituent entity that is subject to a QD(M)TT either in a MS or in a third country to use accounting standards (both accepted or authorized) which are different from the ones used by the UPE when determining its financial accounting net income or loss (‘FANIL’) for purposes of Pillar 2.

ARTICLE 16

- **Question 1**

Are the rules included in the OECD administrative guidance on excluded equity gains or loss & hedges in line with Article 16 of the Directive?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

The Administrative Guidance on ‘Excluded Equity Gains or Loss and hedges of investments in foreign operations’ [AG22.04.T8] determines the extent to which gains and losses on hedging instruments may be treated as excluded equity gains or losses. It provides for a five-year election to treat foreign exchange gains or losses reflected in a constituent entity’s financial accounting net income or loss as an excluded equity gain or loss if certain conditions are met.

- **Question 2**

Should a withholding tax be part of “Net taxes expense” for the constituent entity making the payment, or for the constituent entity receiving the payment, or for neither of them?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

Paragraph 29 on the OECD Model Rules refers to a situation where the withholding tax is paid by the constituent entity on behalf of the recipient. As shown in the example, the interest withholding tax (covered tax) should be reported in the financial accounts of the interest recipient (i.e., creditor).

In the payer accounts:	Amount in EUR	In the recipient state:	Amount in EUR
Interest charge debit	1.000.000	Bank debit	900.000
Payment to creditor credit	900.000	WHT charge debit	100.000
Payment to tax authorities credit	100.000	Interest income gross credit	1.000.000

With respect to dividend WHT on intra-group profit distributions it should be noted that the covered tax is attributed to the distributing constituent entity.

- **Question 3**

Are dividends only excluded pursuant to Article 16(1)(b) of the Directive if they are classified as such by both the issuer and the holder of the relevant financial instrument?

- **Response**

Dividend is an undefined term in the Directive.

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

Although undefined common accounting terms should be interpreted consistent with their meaning in the financial accounting standard, the commentary defining Ownership Interest in Art. 10.1 (as modified by the Administrative Guidance Par. 2.3.3) provides additional input in order to address a specific case where, within the same MNE group, a financial instrument is issued by a constituent entity and held by another constituent entity. In such case, it shall be classified as debt or equity consistently by both and accounted for accordingly in the computation of the qualifying income or loss. In case of discrepancy, the classification adopted by the issuer should be applied by the issuer and holder.

- **Question 4**

Are movements in insurance reserves related to excluded dividends as in Article 16 (1)(b) of the Directive or an excluded equity gain or loss as in Article 16 (1)(c) from securities held on behalf of policyholders allowed as a deduction in the computation of qualifying income or loss?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

It appears that the Commentary to the corresponding Article 3.2.1(b) and 3.2.1(c) of the OECD Model Rules (as modified by the Administrative Guidance Par. 3.4.1.3) with respect to the treatment of excluded dividends and excluded equity gain or loss in the context of insurance could be of use here.

In order to avoid a distortive mismatch between excluded income and insurance liability expense, where a movement in an insurance company's reserves economically matches an excluded dividend from a security held on behalf of a policyholder, the correlative movement in the insurance reserves is not allowed as an expense in the computation of qualifying income or loss. Expenses related to excluded equity gains or losses from unit linked insurance must be excluded in the same way.

- **Question 5**

Do accrued pension expenses within in the meaning of Article 16(1)-(h) of the Directive also include direct pension payments i.e. that are not contributed to a fund? Should the accrued pension expenses be adjusted to ensure that the amount taken into account to determine the qualifying income or loss are the amounts contributed to the pension scheme.

- **Response**

Article 16(1)-(h) of the Directive defines accrued pension expense for the purpose of adjustments to the financial accounting net income or loss of a constituent entity and refers explicitly to the amount contributed to a pension fund.

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

A further guidance may be found in the Commentary to the Article 3.2.1(i) of the OECD Model Rules (as modified by the Administrative Guidance Par. 2.5) with respect to the treatment of accrued pension expenses.

The adjustment with respect to accrued pension expenses only applies in the case of pension expenses that are provided through a pension fund. Whenever pension expenses are accrued

for direct pension payments to former employees, no adjustment has to be made to the financial accounting net income or loss. These should be taken into account at the same time and in the same amount as they are accrued and expensed in the computation of financial accounting net income or loss.

The Administrative Guidance also clarifies that the adjustment relating to accrued pension expenses also applies where there is a pension surplus or pension income recognised in the financial accounting net income or loss.

- **Question 6**

When implementing the Directive, can Member States reflect the rule included in paragraph 3 of the OECD Commentary on the computation of GloBE Income or Loss (Chapter 3, article 3.1.2.) which states that income or expenses attributable to purchase accounting for an acquired business are not taken into account in the computation of the constituent entity financial accounting net income or loss?

- **Response**

In accordance with Recital 24 of the Preamble to the Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

As Article 16(2) of the Directive includes the same list of adjusted items as Article 3.1.2. of the OECD Model Rules, the reference to purchase accounting is a clarification and explanation on the approach for the calculation of the constituent entities adjusted financial accounting net income or loss. When the Commentary to the OECD Model Rules provides such additional information the Member State can take the details into consideration when implementing the Directive.

- **Question 7**

Could a constituent entity elect (for five years) to include in its qualifying income or loss dividends from all (both long-term and short-term) portfolio shareholdings (i.e. will these dividends not be excluded on the basis of Article 16(2)(b) of the Directive)?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

The Administrative Guidance on ‘Simplification for Short-term Portfolio Shareholdings’ [AG22.04.T11] allows a filing constituent entity to make a 5-year election for each constituent entity to include all dividends received with respect to portfolio shareholdings in the computation of the qualifying income or loss.

- **Question 8**

The Commentary to the Model Rules refers to stock-based compensation to employees and non-employees. Could you please confirm this is also the case under the Pillar 2 Directive?

- **Response**

Article 16(3) of the Directive doesn't make a distinction between stock-based compensation to employees and non-employees.

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

The Commentary to the OECD Model Rules (Chapter 3, paragraph 90), clarifies that, in principle, the election applies to stock-based compensation for employees and non-employees. However, if the local tax base applies different rules for employees and non-employees, the election will apply differently to stock-based compensation of employees and non-employees, in conformity with those local tax rules.

- **Question 9**

Article 16(4) provides for the following principles: *Any transaction between constituent entities located in different jurisdictions that is not recorded in the same amount in the financial accounts of both constituent entities or that is not consistent with the arm's length principle shall be adjusted so as to be in the same amount and consistent with the arm's length principle.*

Does Article 16(4) of the Directive require adjustments to the transaction between constituent entities located in different jurisdictions even where the same amount is reflected in financial statements – but this amount is not in accordance with the arm's length principle?

- **Response**

The adjustment should be made if the amount is not at arm's length, even if the same amount is reflected in the financial statements of both related parties.

- **Question 10**

Does an instrument issued by a constituent entity pursuant to prudential regulatory requirements (as in Article 16 (11) of the Directive) also include Restricted Tier One Capital issued by insurers?

- **Response**

Article 16 (11) of the Directive provides a set of rules that treats additional tier one capital in the same manner as a debt instrument. Distributions on additional tier one capital are treated as expenses of the issuer and income of the holder in the computation of qualifying income or loss.

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for

implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

The Model Rules definition in Article 10.1 of additional tier one capital made a direct reference to the prudential regulatory requirements of the banking sector. The administrative guidance agreed on 1 February 2023 (Section 3.3) further explains that the insurance sector is required to issue similar instruments and extends, through a modification to the Commentary to Chapter 3, paragraph 142, the definition of Article 10.1 to also include restricted tier one capital issued by insurers.

- **Question 11**

The Bank Recovery and Resolution Directive requires certain entities to meet a Minimum Requirement for own funds and Eligible Liabilities, known as MREL. Could a MREL be qualified as “an instrument issued... pursuant to prudential regulatory requirements” in accordance with Article 16(11) of the Directive so that it would meet the definition of “additional tier one capital”.

- **Response**

The MREL qualifies as additional tier one capital, because it is an instrument based on prudential regulatory requirements.

ARTICLE 17

- **Question 1**

Is the list in Article 17 (1)(a-b) of the Directive exhaustive? If not, can we assume that whatever is qualified under a special tonnage tax which is an EU approved regime is considered to be shipping and ancillary shipping income for the purposes of this Directive?

Does Article 17(1)(b)(iv) of the Directive aim to cover technical and crew ship management?

Do the words "held for use" in Article 17(1)(a)(vi) aim to cover both legal and economic owners?

- **Response**

Article 17 of the Directive defines international shipping income and qualified ancillary international shipping income. Only the income obtained from the activities listed in paragraph 1 (a) and (b) is considered as shipping and ancillary shipping income that is excluded from the computation of qualifying income or loss of a constituent entity. This list is exhaustive. Whenever an EU state-aid approved regime does not coincide with the list of Article 17 of the Directive, the relevant income will not benefit from the exclusion from the computation of qualifying income or loss.

Article 17(1)(a)(vi) of the Directive means that the income (capital gain or loss) obtained by a constituent entity from the sale of a ship used for the transportation of passengers or cargo in international traffic is excluded from the computation of its qualifying income or loss, provided that the ship has been held for use by the constituent entity for a minimum of one year. The aim of this 1-year condition is clarified in the Commentary to Chapter 3 (paragraph 159) to prevent ship trading activities from qualifying for the exclusion. It is further explained

that the ships that have been purchased for resale are usually recorded as inventory in the financial accounts (IAS 2) and capital gains or losses resulting from the sale of such ships do not qualify for the exclusion. On the other hand, legally owned ships used for international shipping operations are recognised as property, plant & equipment in the financial accounts (IAS 16) if they are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes, and are expected to be used during more than one period. If those have been recorded as being held for use in the financial accounts of the CE for more than 1 year, they will qualify for the exclusion.

Finally, with respect to the question regarding technical and crew ship management: whether these activities can be considered covered by Article 17, paragraph 1(b)(iv) depends on the exact facts and circumstances of the case.

Chapter 4: Computation of adjusted covered taxes

ARTICLE 20

- **Question 1**

Will a list be developed by name of covered taxes by jurisdiction (which is updated accordingly)?

- **Response**

As stipulated during the Council discussions on the Pillar 2 Directive, the Commission is not planning to develop a list of covered taxes for purposes of the Pillar 2 Directive. Whether such a list is established by the OECD for the Inclusive Framework would be for the OECD and Inclusive Framework members to decide.

- **Question 2**

Are domestic windfall taxes on surplus profits covered taxes?

- **Response**

Yes, there are no indications under the Directive that would exclude windfall tax on surplus profits from the category of covered taxes. Depending on the relevant national measure, they could be considered under any of the four categories listed under Article 20(1) of the Directive.

- **Question 3**

What is the treatment under the Directive of the corporate income tax retained by an entity (i.e. tax which is not payable but should be invested by the entity as per the conditions of the scheme) under state aid schemes for regional development, which are approved by the European Commission? Could this tax be considered a qualified refundable tax credit and consequently treated as provided for in Article 16(5), Article 21(2)(d) or Article 21(3)(c) of the Directive?

- **Response**

The fact that a tax scheme has been approved under State Aid does not imply a more favourable treatment under the Directive, as the measure has to be assessed under two separate and independent legal instruments. It seems that the measure (retained taxes to be used for regional development activities) would not qualify as a qualified refundable tax credit (e.g., it is not a tax credit, it is not refundable, it is not paid as a cash payment or a cash equivalent).

- **Question 4**

Are the following taxes covered taxes for purposes of the Directive?

1. taxes that are only due once;
2. windfall profit taxes;
3. sector specific taxes (e.g., telecommunication taxes); and
4. taxes which are charged only if certain conditions (i.e., size of the premises) are met (e.g., retail taxes in certain Member States).

- **Response**

Covered taxes are not required to be recurring taxes, nor is it intended to exclude taxes that apply on a non-recurring basis.

More broadly, the definition of covered taxes in Article 20 of the Directive could also apply to taxes that are imposed only on specific sectors or under certain conditions, provided they meet the elements of the definition of a covered tax and do not fall under the categories of taxes that are excluded based on Article 20(2) of the Directive.

ARTICLE 21

- **Question 1**

How should the amount of current tax expense with respect to income excluded from the computation of qualifying income or loss under Chapter III be calculated? Should the calculation be made on an apportionment basis?

- **Response**

Article 21(3)(a) of the Directive requires to exclude from adjusted covered taxes the amount of current tax expense with respect to income excluded from the computation of qualifying income or loss under Chapter III.

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

It seems that the Commentary to article 4.1.3 of the Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive.

For example, where the entire amount of the income item is excluded, the excluded taxes must be determined on the same basis. This means that in the case of a withholding tax on an excluded dividend, the entire withholding tax is excluded. However, in the case of a CFC charge on a minority interest, that portion of the shareholder's income tax attributable to the CFC must be excluded from the constituent entity's adjusted covered taxes when calculating the effective tax rate. If an item of income is partially excluded from the qualifying income or loss, Article 21(3)(a) shall apply only to the extent of the excluded portion.

- **Question 2**

As part of adjusted covered taxes computation, the reductions of the covered taxes shall include the amount of current tax expense with respect to income excluded from the computation of qualifying income or loss under Chapter III of the Directive.

An example of excluded income are dividends (save for short term portfolio shareholdings). However, withholding tax collected by the distributing constituent entity is allocated to this constituent entity, per Chapter IV of the Directive. Does Article 21(3)(a) apply effectively to withholding tax collected by a distributing entity if a dividend is excluded income?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

Based on the explanation provided in the Commentary to the OECD Model Rules (Chapter 4, paragraph 11), and Article 24(5) of the Directive, covered taxes imposed on intra-group dividends are included in the distributing constituent entity's adjusted covered taxes and, ultimately, in the numerator of the effective tax rate computation.

- **Question 3**

As part of the adjusted covered taxes computation, the reductions of the covered taxes shall include "the amount of current tax expense that relates to an uncertain tax position".

An uncertain tax position involves, typically, the generation of a deferred tax liability, which is then released when the given item is paid (or given proceedings resolved to the benefit of the entity). The payment is covered by Art. 21 (2) point c. Therefore, what should be understood by "current tax expense" in Article 21(3)(d) of the Directive?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

As explained in the Commentary to the OECD Model Rules (Chapter 4, paragraph 16), uncertain tax positions generally result when a Constituent Entity takes a filing position that is not more likely than not to be sustained upon examination. In such cases, a reserve has to be established based on financial accounting standards. When the reserve is released, expenses are reversed and a corresponding amount of income is reflected in the financial accounts. The movement in these amounts may not be included in Adjusted Covered Taxes unless and until the amount is actually paid.

The two provisions of the Directive address different situations: of Article 21(3)(d) of the Directive) addresses situations where uncertain tax positions are booked in the financial accounts, while Article 21(2)(c) of the Directive addresses situations where an amount of tax that is connected to an uncertain tax position is paid in the fiscal year and was previously treated as a reduction to Covered Taxes under paragraph (d).

ARTICLE 22

- **Question 1**

The total deferred tax adjustment amount shall be increased by, i.e., any amount of recaptured deferred tax liability determined in a preceding fiscal year that has been paid during the fiscal year.

Does „preceding fiscal year" mean the directly preceding fiscal year (e.g. in 2025, the preceding year would be 2024) or does it mean one of the previous fiscal years?

- **Response**

Based on the wording of Article 22(3) which refers to ‘a preceding fiscal year’ it is confirmed that this means “any preceding fiscal year”.

- **Question 2**

What is the meaning of the term “paid” with respect to a deferred tax liability and a recapture exception accrual? Could it cover also “reversed” or “paid”?

- **Response**

In principle, the term “paid” should be broadly interpreted.

- **Question 3**

Does the term ‘deferred tax expense’ include deferred tax net income/credit?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

Article 22(2) of the Directive refers to ‘deferred tax expense’. In the Commentary to the OECD Model Rules (Chapter 4, paragraph 70), further explanation is provided on the term ‘deferred tax expense’. The Commentary notes that deferred tax expense is comprised of the net movement in deferred tax assets and liabilities between the beginning and end of the fiscal year. When established, deferred tax assets are recorded as a negative tax expense (i.e., income tax benefit), whereas deferred tax liabilities are recorded as a tax expense.

- **Question 4**

The deferred tax may be different in the constituent entity's financial accounts vs the consolidated financial statements because e.g., an asset was previously transferred intragroup and is held at market value at transfer (less depreciation) in the financial accounts of the constituent entity but may be held at historical cost to the group (less depreciation) resulting in different deferred tax amounts. Which deferred tax amounts are relevant in such a case?

- **Response**

In general, the constituent entity’s financial statements are used as a starting point for the determination of the covered taxes, subject to the required adjustments (Article 22), and special rules such as in Article 35 (transfer of assets and liabilities) or Article 47 (Tax treatment of deferred tax assets, deferred tax liabilities and transferred assets upon transition).

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

It seems that the AG, section “1.3. Consolidated deferred tax amounts”, could be used for additional clarifications in respect of deferred tax amounts.

- **Question 5**

How are reversals of accruals to be treated since Article 22 of the Directive refers to amounts "paid"?

- **Response**

As far as Article 22 is concerned, in relation to reversals of accruals being "paid" it should be understood that it is the tax liability that gave rise to the accrual that is discharged/"paid".

Therefore, the reversal of accruals that are not a correction of a prior mistake shall be understood as being "paid".

ARTICLE 23

- **Question 1**

Article 23 (1) 2nd subparagraph states that "A qualifying loss election shall not be made for a jurisdiction with an eligible distribution tax system under Article 40."

Is the condition of Article 23(1) 2nd subparagraph fulfilled:

- By the mere existence of an eligible distribution tax system in the jurisdiction, or
- Only when the option prescribed for in Article 40 is exercised; or
- Only when all the constituent entities located in the jurisdiction are subject to that distribution tax system?

- **Response**

If a jurisdiction has an eligible distribution tax system under Article 40 of the Directive, it is not possible to make a qualifying loss election with respect to that jurisdiction even if the option under Article 40 of the Directive is not exercised.

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

It seems that further explanations may be found in the Commentary on article 4.5.5. OECD Model Rules (paragraph 116).

ARTICLE 24

- **Question 1**

Article 24(3) and Article 24(6) of the Directive set out rules regarding CFC push-down. More specifically, Article 24(6) of the Directive provides a limit to the above-mentioned push-down: "*A constituent entity that was allocated covered taxes pursuant to paragraphs 3 and 4 in respect of passive income shall include such covered taxes in its adjusted covered taxes in an amount equal to the covered taxes allocated in respect of such passive income*". How should the distinction between active and passive income be drawn?

- **Response**

Article 24(6) of the Directive includes a definition of passive income: "*For the purposes of this paragraph, 'passive income' means the following items of income*

included in qualifying income to the extent a constituent entity-owner has been subject to tax under a controlled foreign company tax regime or as a result of an ownership interest in a hybrid entity: (a) a dividend or dividend equivalents; (b) interest or interest equivalents; (c) rent; (d) royalty; (e) annuity; or (f) net gains from property of a type that produces income described in points (a) to (e).”

- **Question 2**

Regarding the push-down of covered taxes to controlled foreign entities (hereinafter, CFC push down), how should the amount of allocable CFC tax be determined, where the jurisdiction of the parent entity taxes under its CFC tax regime both passive and active income of the CFC, and a foreign tax credit (FTC) applies.

- **Response**

Based on Article 24(6) of the Directive, the allocation of CFC taxes in relation to passive income is limited to the lesser of:

- (a) the actual amount of covered taxes in respect of such passive income; or
 - (b) the top-up tax percentage that applies in the subsidiary jurisdiction, multiplied by the amount of the subsidiary’s passive income that is includible under the CFC tax regime.

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

It seems that further illustration may be found in the document *Tax Challenges Arising from the Digitalisation of the Economy – Global Anti-Base Erosion Model Rules (Pillar Two) Examples (2022)* (on pages 38 and 39).

- **Question 3**

A constituent entity that made a distribution during the fiscal year shall be allocated the amount of any covered taxes accrued in the financial accounts of its direct constituent entity-owners on such distribution.

Does this rule cover a situation where CIT is due, by the constituent entity-owner (a shareholder of a non-tax transparent partnership), on the requalification of profit of a constituent entity (partnership) to its registered share capital? Does the covered tax remain within the constituent entity-owner (shareholder)?

- **Response**

Article 24(5) of the Directive deals with the allocation of taxes on dividends and other distributions.

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

As explained in the Commentary to the OECD Model Rules (Chapter 4, paragraph 60 and 61), *“this includes withholding tax and net basis taxes incurred by direct Constituent Entity-owners on distributions by Constituent Entities in respect of their stock which are allocated to the distributing Constituent Entity.(...) The rule applies to Taxes with respect to any type of distribution with respect to the stock of the distributing Constituent Entity.”* In general, a requalification of profit of a constituent entity (partnership) to its registered share capital or other type of equity would not be considered as a type of distribution with respect to the stock of the distributing constituent entity.

However, considering the Commentary to article 4.3.2.(e) of the OECD Model Rules as amended by the Administrative Guidance [AG22.04.T11], if such requalification is considered a deemed distribution and the interest in the partnership is treated as an equity interest in the jurisdiction that is imposing the CIT both for tax purposes and for financial accounting purposes, Article 24(5) of the Directive would apply.

ARTICLE 25

• **Question 1**

Based on Article 25(3) 1st subparagraph of the Directive should the adjustment to a constituent entity’s liability for relevant covered taxes claimed for a previous fiscal year be made in respect of:

- the fiscal year in which the tax is paid; or
- the fiscal year in which the deferred tax expense is established?

○ **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

It seems that paragraphs 130 and 131 of the Commentary to Article 4.6.3. of the OECD Model Rules on adjustments on deferred tax accounts provides the proposed approach.

Chapter 5: Computation of the ETR and the top-up tax

ARTICLE 28

• Question 1

Article 5.3.4 of the OECD Model Rules, *in fine*, states that “*The carrying value of tangible assets attributable to a Constituent Entity’s excess income over the cap for Qualified Ancillary International Shipping Income under article 3.3.4 shall be included in the tangible asset carve-out computation*”. How is this reflected in the Directive?

○ Response

In accordance with Article 28(4)(b) of the Directive, the excluded carrying value of tangible assets is limited to tangible assets that are used to derive income that is excluded in accordance with Article 17.

• Question 2

How, should the substance-based income exclusion (SBIE) be computed for stateless entities?

○ Response

Article 28(8) of the Directive requires that the SBIE for each stateless entity is computed on a standalone basis for each fiscal year. In the context of calculating SBIE each stateless entity is treated as a separate jurisdiction, and its payroll carve-out and the tangible asset carve-out are calculated pursuant to Article 28, provided the amounts taken into consideration in the computation of stateless entity SBIE are not taken into consideration for other jurisdictions.

ARTICLE 32

• Question 1

Are (all) Member States deemed to have consented to the QDMTT Safe Harbour, UTPR Safe Harbour, the temporary CbCR Safe Harbour since they were adopted by the Inclusive Framework?

○ Response

All Member States that form part of the IF are considered to have agreed to a ‘qualifying international agreement on safe harbours’ as referred to in article 32 of the Directive. That agreement includes the CbCR Safe Harbour as agreed in December in 2022, QDMTT Safe Harbour and the UTPR Safe Harbour as described in the Administrative Guidance of July 2023. As Cyprus is not a member of the IF, Cyprus should consent to the relevant Administrative Guidance.

All MS have consented to a qualifying international agreement on safe harbors, as defined in Article 32, because:

1. All MS, except for Cyprus, are members of the OECD/G20 Inclusive Framework on BEPS (IF): <https://www.oecd.org/tax/beps/inclusive-framework-on-beps-composition.pdf>
2. On December 15, 2022, the members of the IF have approved the guidance “Safe Harbours and Penalty Relief: Global Anti-Base Erosion Rules (Pillar Two)”, see: <https://www.oecd.org/tax/beps/safe-harbours-and-penalty-relief-global-anti-base-erosion-rules-pillar-two.pdf> ;
3. On July 13, 2023, the members of the IF have approved the AG “Tax Challenges Arising from the Digitalisation of the Economy – Administrative Guidance on the Global Anti Base Erosion

Model Rules (Pillar Two), July 2023”, notably stating that: “*This document was approved by the OECD/G20 Inclusive Framework on BEPS on 13 July 2023 and prepared for publication by the OECD Secretariat*”, see: <https://www.oecd.org/tax/beps/administrative-guidance-global-anti-base-erosion-rules-pillar-two-july-2023.pdf>, page 2;

4. On March 22, 2023 and on October 23, 2023, the Minister of Finance of Cyprus has sent two letters to the European Commission (DG TAXUD) confirming that Cyprus consents to the December 15, 2022 and the July 13, 2023 AG respectively;
5. On November 9, 2023, Council of the European Union unanimously adopted the statement “Two-pillar solution to address the tax challenges arising from the digitalisation of the economy”, in which the Council stated that it “*welcomes and supports the agreement reached by the Inclusive Framework on the clarifications concerning application of Pillar Two contained in the administrative guidance endorsed by the Inclusive Framework in December 2022, in February 2023 and in July 2023 – including the transitional Undertaxed Profits Rule and Qualified Domestic Minimum Top up Tax Safe Harbours, the new guidance on Transferable Tax Credits, as well as the transitional Country-by-Country Reporting Safe Harbour and the GloBE Information Return*” (see the Statement, Annex I, Para IV).

- **Question 2**

Can the safe harbours be implemented also with reference to large-scale domestic groups, including the temporary CbCR safe harbour if an obligation is introduced to provide data necessary for the simplified calculations?

- **Response**

In Article 32 of the Directive reference is made to ‘a group’ in general, and no distinction is made between an MNE group or large-scale domestic group. Therefore, the safe harbour provision also applies to large-scale domestic groups, which is in accordance with the objective and purpose of the Directive. For the first 5 years when the large-scale domestic group falls within the scope of the Directive, the initial phase of exclusion for large-scale domestic groups (of Article 49 of the Directive) has to be taken into consideration.

Chapter 6: Special Rules for corporate restructuring and holding structures

ARTICLE 33

• Question 1

How to deal with demergers that have taken place prior to the application of the Directive?

○ Response

As in the provisions of Article 33(4) of the Directive reference is made to ‘a single MNE group or large-scale domestic group within the scope of this Directive’ that demerges, Article 33(4) of the Directive would not apply to demergers that have taken place prior to the application of the Directive. In such case the general revenue threshold test of Article 2(1) of the Directive would apply. See example next slide.

Article 33 Pillar 2 Directive

Example Demerger

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- **Demerged Group A consolidated revenues:**

	Demerger in 2024	Demerger in 2022	
Year 1	2025	2023	400
Year 2	2026	2024	500
Year 3	2027	2025	300
Year 4	2028	2026	300

- **Demerged Group B consolidated revenues:**

	Demerger in 2024	Demerger in 2022	
Year 1	2025	2023	850
Year 2	2026	2024	400
Year 3	2027	2025	200
Year 4	2028	2026	250

- If the demerger would have taken place in 2024, Demerged Group B meets the test in the first fiscal year (Demerged Group B has consolidated revenues of EUR 750 million or more in Fiscal Years 1 following the demerger).
- If the demerger would have taken place in 2022, Demerged Group B would not fall within the scope of the Directive.

• Question 2

Does the proportionality rule of Article 2(2) of the Directive apply to Article 33 of the Directive in the case of group mergers and demergers?

○ Response

Although Article 2(2) of the Directive refers directly to the fiscal years mentioned under Article 2(1) of the Directive, it is understood as setting a rule of general application within the Directive, therefore the proportionality rule set under Article 2(2) applies also in the case of mergers or demergers.

ARTICLE 35

• Question 1

Is the election of Article 35(5) of the Directive a one-time, irrevocable election?

○ **Response**

The Directive does not specify whether the election at stake is irrevocable or revocable. The election considered under Article 35(5) of the Directive refers to a specific event, relevant for tax purposes (i.e. the transfer of assets and liabilities). The tax consequence of this choice (i.e. of the election) should therefore be limited to the tax year when this event is computed (Article 35(5)(c)) although its (tax) effects will be relevant for other fiscal years (Article 35(5)(b)). Therefore the election is naturally irrevocable as it is a one-time choice with effects naturally lasting for subsequent fiscal years.

ARTICLE 36

• **Question 1**

According to Section 118.8 of the OECD Administrative Guidance agreed on 1 February 2023 a jurisdiction that has introduced the QDMTT has 2 options regarding the application of the QDMTT in respect to the joint venture and its affiliates:

- not to impose the QDMTT tax liability on joint ventures and JV subsidiaries, or
- to impose the QDMTT on another constituent entity of the MNE Group located in the jurisdiction.

Can a Member State apply the QDTT on a joint venture? If yes, should the ownership interest of the parent entity be taken into account or not? Can a tax liability be imposed directly on the joint venture irrespective if there is another constituent entity of the MNE group located in the same jurisdiction?

○ **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

Reference is made to the Commentary on Article 10.1 of the OECD Model Rules (as modified by the Administrative Guidance) with respect to the QDMTT and Joint Ventures (paragraph 118.8 and further).

Chapter 7: Tax neutrality and distribution regimes

ARTICLE 38

- **Question 1**

Is the qualifying income of a flow-through entity that is an UPE only reduced pursuant to Article 38(1) of the Directive if the amount of qualifying income of the ownership holder is taxed at or above the minimum rate?

- **Response**

It's confirmed that under Article 38 of the Directive, the qualifying income of the UPE cannot be reduced in proportion to the income taxed in the hands of the owners if the later are not subject to tax at or above the minimum rate of 15%. There is no mechanism to take into account the taxes paid by the owners that have a rate below 15%.

- **Question 2**

How are investment entities treated under the QDIT?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

Further guidance on the above issues can be found in the Commentary to Article 10.1 of the OECD Model Rules (as modified by the Administrative Guidance issued in February) with respect to the QDIT and investment entities (paragraph 118.40.3 and further).

ARTICLE 40

- **Question 1**

What is definition of deemed distribution in Article 40 of the Directive?

- **Response**

The term deemed distribution in Article 40 of the Directive is not defined in the Directive nor in the OECD Model Rules independently from the notion of deemed distribution tax. One could take inspiration from the definition of deemed distribution tax in this Article.

ARTICLE 42

- **Question 1**

Does a mutual insurance company qualify for the election of Article 42(2) of the Directive?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

The updated Commentary to Article 7.5 of the OECD Model Rules (paragraph 91 as revised by [AG22.04.T7]) clarifies that mutual insurance companies are eligible to make the election of Article 7.5

with respect to investment entities and insurance investment entities that they control, because this is necessary to ensure that the GloBE Rules reflect the underlying economics of these arrangements, and in particular the fact that all profits earned by mutual insurance companies on behalf of policyholders are immediately expensed by the MNE Group in the consolidated financial statements.

ARTICLE 43

- **Question 1**

Does the reference to investment entity in Article 43 of the Directive also include insurance investment entities?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

The updated Commentary to Article 7.6 of the OECD Model Rules (paragraph 99 as revised by [AG22.04.T11]) clarifies that insurance investment entities can make an election to use the taxable distribution method.

Chapter 8: Administrative provisions

ARTICLE 44

- **Question 1**

In case there is a need to file an amended top-up tax information return (for example, in order to correct an error), can Member States provide a deadline for its filing which is longer than the one prescribed for the filing of the regular return (15 months)? Are corrections permitted at all?

- **Response**

There are indeed circumstances under which an amended top-up tax information return could be required.

While the Directive provides rules on how to deal with post-filing adjustments and tax rate changes (Article 25 of the Directive) and on how to account for additional top-up tax (Article 29 of the Directive), it is silent on the administrative side of submitting an amended top-up tax information return. However, the consistency of deadlines for amended top-up tax information returns among jurisdictions would be a desirable outcome and further work may be dedicated to this issue.

ARTICLE 45

- **Question 1**

Do the elections in Articles 23 and Article 35 of the Directive fall under the scope of Article 45 of the Directive?

- **Response**

Article 23 and 35 of the Directive are stand-alone elections which are not subject to a certain time limit, and as such there is no need to include a reference to these articles in Article 45 of the Directive.

- **Question 2**

Article 45(2) of the Directive determines that *“The election shall be renewed automatically unless the filing constituent entity revokes the election at the end of the year.”*

Does the term “year” mean “fiscal year”?

- **Response**

Yes, the reference is to fiscal year.

- **Question 3**

With respect to the automatic renewal of the annual elections as stipulated in Article 45(2) of the Directive, can Member States, in compliance with EU law, adopt a solution in line with what is prescribed by the Model Rules and is the structure of the Globe Information Return, recognising that the election is valid for a fiscal year and simultaneously assuring that the filing constituent entity is free to re-elect it in relation to any following fiscal year, even successively?

- **Response**

A Member State is free to do so. ‘Ticking the box’ in the GIR could be considered a way of automatically renewing the election. As the GIR doesn’t provide for the revocation of an annual election, it is left to the discretion of the Member States to adopt a procedure for the revocation of such election. For example, this could be done by clarifying that if a filing constituent entity doesn’t tick the box for an

annual election in the GIR, that is considered a revocation of the election for that fiscal year which is deemed to have been made by the end of the preceding fiscal year.

Chapter 9: Transition rules

ARTICLE 47

- **Question 1**

Do deferred tax assets upon transition (Article 47(2) of the Directive) include recast tax credits? If so, does Article 22 (5)(e) of the Directive not apply to these tax credits?

Are qualified refundable tax credits and non-qualified refundable tax credits arising prior to the transition year treated the same for purposes of article 47(2) of the Directive?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

The Administrative Guidance [AG22.04.T12] on Article 9.1 of the OECD Model Rules on deferred tax assets ('DTA') upon transition explains that there are no compelling reasons to exclude particular DTAs from deferred tax attributes to be taken into account in the transition year and used in the effective tax rate calculation for a jurisdiction. It allows DTAs attributable to tax credit carry-forwards to be taken into account in computing adjusted covered taxes in the transition year and subsequent fiscal years.

- **Question 2**

Should all transactions and corporate restructurings that are accounted for similar to an asset transfer, regardless of their form and whether they take place within an entity or among entities, be regarded as a transfer of assets within the meaning of Article 47(4) of the Directive?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

The relevant part of the Administrative Guidance [AG22.04.T16] on Article 4.2.3 of the OECD Model Rules states: *"The integrity of the GloBE Rules would be undermined if MNE Groups were allowed to engage in asset transactions during the Pre-GloBE Period where the income from the transaction is taxed below the minimum rate without the risk of Top-up Tax and the corresponding increase in carrying value shields future income from potential Top-up Tax"*.

- **Question 3**

Do the words “on that basis” in Article 47(4) of the Directive mean: ‘the carrying value upon disposition of the transferred asset on the day of the transfer adjusted for capital expenditures, amortisation or depreciation after the transaction and before the commencement of the transition year’? Should a transfer of assets be interpreted broadly? May an acquiring constituent entity take into account a DTA to the extent the disposing entity paid tax in respect of the transaction?

- **Response**

In accordance with Recital 24 of the Preamble to the Pillar 2 Directive, the Commentary to the OECD Model Rules could be used as a source of illustration or interpretation for implementation of the Pillar 2 Directive in order to ensure consistency in application across Member States to the extent that those sources are consistent with this Directive and Union law.

The Administrative Guidance [AG22.04.T2] Par.4.3.3 on Article 9.1.3. of the OECD Model Rules provides additional explanations on the term “basis” and allows that an acquiring constituent entity takes into account a DTA to the extent the disposing entity paid tax in respect of the transaction.

ARTICLE 49

- **Question 1**

Are large-scale domestic groups in the scope of the Directive in the first five years, or does the initial phase exclusion of Article 49(1) of the Directive result in the outcome that large-scale domestic groups are not in scope of the Directive?

If Article 49 of the Directive applies, does this impact the ‘transition year’ as defined in Article 47(1) of the Directive?

- **Response**

Large-scale domestic groups, are in scope of the Directive. They shall benefit from the initial phase exclusion stipulated in Article 49(1) of the Directive for the first five years starting from the first day of the fiscal year in which they fall within the scope of the Directive for the first time.

The transition year as defined in Article 47(1) of the Directive is concerned starts from the first fiscal year in which the MNE group or large-scale domestic group first falls within the scope of the Directive in respect of a jurisdiction, regardless of the exclusion provided under Article 49 of the Directive.

- **Question 2**

Does Article 49(5) apply to large-scale domestic groups? Should these groups also inform the tax administration of their Member State what is the first year of exclusion from IIR?

- **Response**

As Article 49 of the Directive deals with both MNE groups and large-scale domestic groups, we consider this provision to also apply to large-scale domestic groups, with the clarification that in their case, the communication has to be about the start of the in-scope status.

- **Question 3**

If a Member State that elects to apply Article 50(1) of the Directive introduces a qualified domestic top-up tax, should the information necessary for other Member States to determine whether UTPR may be due still be provided to the designated filing entity of the MNE group?

- **Response**

The designation procedure ensures that information that has to be included in the top-up tax information return (ie, Article 44(5) of the Directive) is made available by the UPE that is located in the Article 50(1) Member State to the designated filing entity. As such, Article 44 of the Directive should be transposed in full and local law should facilitate the assignment of a designated filing entity outside of the Member State that elects to apply Article 50(1) of the Directive. This is also the case if a qualified domestic top-up tax is enacted by the jurisdiction applying Article 50(1) of the Directive.

ARTICLE 50

- **Question 1**

If a Member State elects the application of Article 50(1) of the Directive do they still have the right to introduce a qualified domestic top-up tax?

- **Response**

Based on Article 50 of the Directive Member States can elect not to apply the IIR and the UTPR temporarily. However, in accordance with the objective and purpose of the Directive, it is acceptable for a qualified domestic top-up tax system to already be transposed if an election under Article 50 has been made.

- **Question 2**

Article 50(3) of the Directive states that the UTPR-percentage of a Member State that has made an election pursuant to article 50(1) of the Directive shall be deemed to be zero. Should that Member State also be deemed not to be an UTPR jurisdiction for the purpose of Article 14(5) of the Directive?

- **Response**

Article 50(3) of the Directive determines that the UTPR percentage determined for a Member State that has made an election not to apply the IIR and the UTPR during a transitional period, shall be deemed to be zero. Based on the objective and purpose of the Directive and in line with Article 14(8) 2nd paragraph of the Directive, the UTPR-top-up tax of the MNE group should be allocated to jurisdictions that have an UTPR in force and for which no election pursuant to Article 50(1) Directive is made.

- **Question 3**

For which year should the test to determine whether the 12 ultimate parent entities of groups within the scope of the Directive be performed - i.e., first year of application (2024) or the year when the Commission is notified (2023)?

- **Response**

In accordance with the wording of Article 50(1) of the Directive the aforesaid condition needs to be met on 31 December 2023.

- **Question 4**

Should large-scale domestic groups be taken into account in order for a Member State that wants to elect the application of Article 50(1) of the Directive to determine whether there are no more than twelve ultimate parent entities located in its jurisdiction?

- **Response**

Yes, large-scale domestic groups that fall within the scope of the Directive have to be taken into account for the purposes of Article 50(1) of the Directive.

- **Question 5**

If a Member State does not elect to apply Article 50(1) of the Directive, then should that Member State transpose Article 50(2) of the Directive for cases where the ultimate parent entity of an MNE group is located in a Member State that has elected to delay the application of the IIR and UTPR?

- **Response**

Yes, Article 50(2) and 50(3) of the Directive should be implemented in order to ensure that UTPR can be charged by other Member States when the ultimate parent entity is located in a Member State that opts to apply Article 50(1) of the Directive.

ARTICLE 51

- **Question 1**

Can a Member State set in its national legislation a shorter deadline for the filing of the top-up tax information return than the 18 months mentioned in Article 51 of the Directive, for example, 9 months after the end of the tax year in the respective Member State?

- **Response**

Article 51 of the Directives provides for a transitional relief for filing obligations according to which the top-up tax information return shall be filed no later than 18 months after the last day of the transition year instead of the normal 15 months after the end of the reporting fiscal year.

From a practical point of view, if a MS were to provide in its national legislation a shorter deadline than the one offered by other participating jurisdictions in accordance with the Directive or the Model Rules, this could lead to timing issues for MNE groups, especially when the filing is centralised and subject to exchange of information by the group in another jurisdiction which would apply the 18 months delay while a specific constituent entity would be subject to a shorter deadline in a specific MS.

Chapter 10: Final provisions

ARTICLE 56

- **Question 1**

Article 56 of the Directive states that Member States “*shall apply those measures in respect of the fiscal years beginning from 31 December 2023*”.

What does “beginning from 31 December 2023” mean in practical terms?

- **Response**

In practical terms, in very exceptional circumstances a MNE group that falls within the scope of the Directive may have a fiscal year starting on 31 December 2023. For those MNEs, this would be the first fiscal year falling in the scope of the Directive.