

## OECD Pillar Two – consolidated commentary

On 25 April 2024, the OECD/G20 Inclusive Framework ('OECD Inclusive Framework') published its [consolidated commentary](#) to the Pillar Two global minimum tax rules ('Pillar Two'). The consolidated commentary incorporates guidance that had been approved and published by the OECD Inclusive Framework before the end of December 2023.

The components of the Pillar Two global tax reform rules have been agreed by 140 members of the OECD Inclusive Framework. Countries are in the process of implementing the Pillar Two model rules in their domestic legislation, and the rules will begin to apply from January 2024.

### Deloitte comments

The OECD Inclusive Framework has published, as promised, an updated consolidated version of the commentary on the Pillar Two rules. The updated commentary puts in one document the original commentary (first published in March 2022) with subsequent further releases including on the country-by-country reporting safe harbour (first published in December 2022) and the three sets of Agreed Administrative Guidance on Pillar Two (originally published in February, July and December 2023). There is also an accompanying set of examples (first published in March 2022) which have also been updated for examples subsequently included in published guidance. As such, there is no 'new' technical guidance included in this update.

The consolidated commentary runs to some 330 pages, which is notably shorter than the sum of pages in the original commentary and all the published guidance to date. The reason for this is that the Agreed Administrative Guidance sets out issues to be considered, and then concludes with amendments or additions to be made. The consolidated commentary only includes those amendments or additions, and not the explanation of the issues. In some cases, especially those which remain in any way unclear, it may in future still be helpful to refer to the Agreed Administrative Guidance to give context.

Implementation of the consolidated commentary and matters covered by guidance may vary depending on how countries have introduced Pillar Two into their domestic law (some will have a flexible approach to automatically bring in new guidance from the OECD Inclusive Framework, others will require law changes). In some cases, where the commentary is providing a better or clearer explanation of the model rules and their local implementation, no law changes will be needed.

The consolidated commentary includes all Pillar Two technical guidance published up until the end of 2023. As the OECD Inclusive Framework plans to issue more guidance on specific areas of Pillar Two, it is expected that the commentary will be further updated and consolidated in future.

### Components of the Pillar Two rules

The OECD Inclusive Framework's Pillar Two model rules, applicable to large multinational groups with annual consolidated group revenue of at least EUR 750 million, will result in 'top-up' tax amounts to bring the overall tax on profits in each country where a group operates up to a minimum effective tax rate of 15%. The key components of the model rules are: **qualified domestic minimum top-up taxes (QDMTT)** which allow countries to charge any top-up taxes due in respect of 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.

## **Consolidated commentary**

The introduction to the consolidated commentary provides an overview of each of its chapters. It now incorporates guidance on currency conversion, and on rebasing monetary thresholds in local currencies.

### **Scope**

Chapter 1 of the consolidated commentary sets out the scope of the model rules.

Guidance has been incorporated on the definition of 'excluded entity'; the application of the ultimate parent entity definition to sovereign wealth funds; and the meaning of 'ancillary' for subsidiaries of non-profit organisations. Further detail has also been added on the meaning of revenue for the purposes of the EUR 750 million consolidated revenue threshold; and how to address mismatches between the financial year of the ultimate parent entity and other group entities.

### **Charging provisions**

Chapter 2 contains the operating mechanics for the IIR and UTPR. Updates include commentary on the exclusion of insurance investment entities from the definitions of 'intermediate parent entity' and 'partially-owned parent entity'.

### **Computation of Pillar Two income or loss**

Chapter 3 sets out the rules for calculating each group entity's income or loss for Pillar Two effective tax rate computation purposes.

The commentary has been updated to incorporate guidance on topics including: how the excluded equity gains/loss rules apply to hedges of investments; the treatment of debt releases; the scope of the accrued pension expense adjustment; the equity investment inclusion election; and the election to include all dividends from portfolio shareholdings in the computation of Pillar Two income or loss.

Other additions include guidance on the treatment of 'qualified refundable tax credits', 'marketable transferable tax credits', and 'qualified flow through tax benefits'; and the requirement that Pillar Two calculations should generally be prepared using the presentational currency of the ultimate parent entity's consolidated financial statements.

### **Computation of adjusted covered taxes**

Chapter 4 sets out the mechanics for determining the amount of 'covered taxes' for each group entity. Updates to the chapter include guidance on: consolidated deferred tax amounts; the carry forward of 'excess negative tax expense'; loss-making parent entities of controlled foreign companies (CFCs); and the allocation of taxes arising under blended CFC tax regimes (e.g. US GILTI).

### **Computation of effective tax rate and top-up tax**

Chapter 5 sets out the steps to be taken in determining whether any countries' effective tax rates are less than 15%, and any amounts of top-up tax due.

Updates include additional guidance on the substance-based income exclusion (SBIE) rules, including in respect of 'eligible employees' and 'eligible tangible assets' that spend time outside of the country of the relevant group entity.

### **Corporate restructurings and holding structures**

Chapter 6 includes guidance dealing with corporate restructurings, such as mergers, acquisitions and demergers. The updated commentary now incorporates guidance on intra-group transactions accounted for at cost.

## **Tax neutrality and distribution regimes**

Chapter 7 provides specific rules where groups are subject to tax neutrality or distribution-based regimes. Updates include guidance in relation to the application of the taxable distribution method election to insurance investment entities, and the application of the investment entity tax transparency election to mutual insurance companies.

## **Administration**

Chapter 8 sets out commentary on the administration of the model rules. Minor changes have been made to the commentary to refer to the four Pillar Two safe harbours that have been agreed by the OECD Inclusive Framework.

## **Transition rules**

Chapter 9 provides guidance on transition rules, including rules for taking into account losses and tax attributes that arose prior to the application of Pillar Two, and for the treatment of intra-group asset transfers occurring before Pillar Two applies to a transferor.

Updates include more detailed commentary on transactions similar to intra-group asset transfers, the use of asset carrying value and deferred taxes, and transitional filing deadlines for groups with short reporting fiscal years.

## **Definitions**

Chapter 10 sets out commentary on terms used in the Pillar Two model rules. Guidance on the definitions of 'consolidated financial statements' and 'ownership interest' have now been included.

The commentary also now incorporates guidance on QDMTTs, including in respect of how QDMTTs should apply to specific types of entities (e.g., joint ventures, minority-owned constituent entities, stateless entities, flow through entities).

## **Annex A – safe harbours**

A new annex has been added to the consolidated commentary, comprising four chapters collecting together guidance on each of the four safe harbours agreed by the OECD Inclusive Framework to date.

### **Transitional country-by-country (CbC) reporting safe harbour**

The transitional CbC reporting safe harbour uses information taken from a business's CbC report and/or financial statements to exclude a group's operations in lower-risk countries from the compliance obligation of preparing full Pillar Two calculations for up to three years.

The chapter includes the guidance from the original December 2022 safe harbours document, as updated by the December 2023 Agreed Administrative Guidance, such as on the requirement that the business's CbC report must be prepared and filed using qualified financial statements and the inclusion of the 'hybrid arbitrage arrangements' anti-avoidance rule.

### **Permanent safe harbour**

Chapter 2 of Annex A incorporates guidance in the December 2022 safe harbour document which set out a framework for the development of future permanent 'simplified calculations safe harbours' to reduce the number of computations and adjustments a business is required to make. It also includes the December 2023 guidance on a permanent simplified calculation safe harbour for non-material constituent entities (NMCEs).

## QDMTT safe harbour

Guidance on the permanent QDMTT safe harbour has been included as Chapter 3 of Annex A to allow businesses to elect to prepare a single QDMTT computation for a country. Where the safe harbour applies, no additional top-up tax will arise under the IIR or UTPR.

## Transitional UTPR safe harbour

Under this temporary safe harbour, no top-up tax will be payable under the UTPR in respect of any undertaxed profits of a business in its ultimate parent entity country if that country applies a nominal statutory corporate income tax rate of at least 20%. The safe harbour will defer the application of the UTPR to such profits until 2026.

## Examples

The OECD has also released an updated version of its document of [examples illustrating the application of the model rules](#). The new version incorporates the 30 additional examples that had previously been included within the Agreed Administrative Guidance documents. One new example – a further example of the application of the special rules for flow-through ultimate parent entities – has also been included.

## Next steps

The OECD Inclusive Framework will continue to release further agreed guidance on an ongoing basis. More guidance is expected to be released in the next few weeks, before summer 2024. It is expected that the consolidated commentary will be further updated for any new guidance published in due course.

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