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Why Pillar Two Top-Up Taxation Requires Tax Treaty Modification

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Summary

On 20 December 2021, the OECD published the announced Pillar Two Model Rules, as part of the envisaged establishment of a global 15% minimum level of company taxation for large multinationals (Pillar 2). No mechanism has been considered to provide for a parallel adaptation of countries' tax treaty networks to support the top-up taxation mechanism with a corresponding distribution of additional taxing powers. This raises the question as to whether the envisaged top-up taxation under the income inclusion rule (IIR) and the undertaxed payments rule (UTPR) can be effectuated in tax treaty scenarios. That is important, because if the treaty compatibility proves problematic here, the complication arises that any Pillar Two top-up taxation charge under domestic law would become a paper tiger in those countries that do not allow for treaty overrides under their constitutional law. Please read further below for some analysis.

1 Introduction

On 20 December 2021, the OECD published the long-awaited Pillar Two Model rules, as part of the envisaged establishment of a global 15% minimum level of company taxation for large multinationals and accompanying top-up taxation by countries up to that level where other countries do not adhere to the new standard (Pillar 2).[2] The Model Rules, also referred to as the Anti Global Base Erosion Rules or GloBE Rules, provide template legislation to the countries that joined the political agreement within the Inclusive Framework of 8 October 2021 and address the so-called income inclusion rule (IIR) and the undertaxed payments rule (UTPR). My previous contribution to this blog was after the publication of the Report on the Pillar Two Blueprint in October 2020 in which I wrote on the question whether the Pillar Two system may be prone to be gamed.[3] My observation was that it was. In the now published Model Rules, I saw, the issue is addressed with a specific anti-mismatch measure in the form of a 'GloBE-Tax Linking Rule' that limits deduction for GloBE purposes in relation to a so-called Intragroup Financing Arrangement at the level of the payer if there is no commensurate increase in the taxable income at the recipient's end.[4] We will have to see whether this anti-mismatch rule will prove sufficient to address any identified gaming-the-system issues.

I would like to devote this contribution to a question that has been running through my head for a while now,[5] and that resurfaced when I read through the Model Rules, namely that of the (in)compatibility of the Pillar Two top-up tax under the IIR and UTPR with the tax treaty networks of countries, more specifically the distributive rules for business profits under the treaty equivalents of Article 7 OECD Model Convention (2017). Can the envisaged Pillar Two top-up taxation be effectuated in tax treaty scenarios? This is a relevant matter, because if the treaty compatibility of the Pillar Two system were to pose a problem at some point, the perhaps thorny issue would emerge that any top-up tax would become a paper tiger in the many countries that do not allow for tax treaty overrides under their constitutional law. That would undermine the very foundation of the Pillar Two system. Although the Pillar Two Blueprint says that there is no problem here, pointing to an analogy with the approach taken in the OECD Commentary in relation to Controlled Foreign Company (CFC) measures and the Saving Clause,[6] I respectfully disagree with this and on the contrary think that we do have an issue here. Here are some further analyses, for the development of some thoughts on the matter, and for the enthusiast.[7]

2 Why IIR and UTPR are incompatible with the tax treaty distributive rules for business profits

2.1 Pillar-Two-Top-Up Tax mechanism

The Pillar Two system provides, where relevant, for a mechanism under which those countries in which the targeted multinational firm involved operates proceeds to levy additional tax up to the 15% minimum company tax level. This is the case if and to the extent that the effective tax rate imposed on the firm involved in any of the other countries where this firm is operational falls below the minimum rate.

The additional charge to tax comes in the Model Rules in two variants, the IIR and the UTPR. The IIR concerns an additional tax charge mechanism for the benefit of the country of residence of the ultimate parent entity of the multinational firm. The IIR is sometimes considered to operate like a CFC-like measure, but then applicable also in relation to low-taxed active (i.e., operational) income instead of top-up taxation as we generally recognize it under CFC-regimes on low-taxed passive (i.e., portfolio investment) income of controlled letter box companies (hence the usage of the ‘income inclusion’ terminology). The UTPR concerns an additional tax charge safety net mechanism for the benefit of other countries. The UTPR is sometimes compared to a deduction limitation-like measure, at least until the envisaged top-up tax distribution mechanism’s design was modified into a tax sharing key dividing tax among countries by reference to a two-factor allocation mechanism. Under the Model Rules, the UTPR distributes any additional tax due among countries on a pro rata parte basis in proportion to the costs of employees present and the value of the tangible fixed assets present in the countries. Up to and including the Pillar Two Blueprint the UTPR was divided among countries from which any of the present constituent group entities made some outbound payments, directly or indirectly, to low-taxed constituent group entities abroad (hence the usage of the ‘undertaxed payments’ terminology).

In terms of the ordering of these measures, it is primarily up to the residence jurisdiction of the parent entity to levy top-up tax under a qualifying IIR, subject to the application of the so-called subject to tax rule (STTR) under the relevant tax treaties (which is not further taken into account here), the so-called primary rule. Secondly, it is up to the other jurisdiction where the multinational firm is operational to levy top-up tax under the UTPR tax distribution system, the so-called backstop rule. Countries are free to regulate the technique of the additional tax mechanisms at their discretion, and, for instance, base the tax charge on an inclusion rule, an additional levy, a deduction limitation mechanism, or as fictitious income, et cetera. Please note that with this any CFC and deduction limitation analogies on this basis immediately fail. For some further details on the operation of the measures, I refer to my previous contribution on the Pillar Two system in this blog.

2.2 A numerical example

The operation of the top-up tax charge under the IIR and UTPR variants can be illustrated with a stylized numerical example. Multinational Enterprise 'Group Q' consists of three group companies, ParentCo in Country X, Sub1 OpCo in Country A and Sub2 OpCo in Country B. Group Q falls within the scope of the Pillar 2 system. Bilateral tax treaties are in place between Countries X, A and B, the provisions and distributive of which are, where relevant, the same as those in the OECD Model Tax Convention (2017).

- *Country A*. In Country A, the corporate tax base is $1,000. The corporate tax due by Sub1 OpCo in Country A is $80. For the sake of convenience, let us assume that the GloBE-base in Country A is also $1,000. The effective tax rate for GloBE purposes (covered tax / GloBE-base) is 80/1,000 * 100% = 8%. The minimum tax level of 15% is not met. The effective rate is 7 percentage points too low (8% instead of 15%). Additional tax on the relevant GloBE-income will be levied under the Pillar Two system elsewhere.
- *Country B*. In Country, B the corporate tax base is also $1,000. The corporate tax payable by Sub2 OpCo in Country B is $180. The corporation tax due by Sub2 OpCo in Country B is $180. The GLOBE base in Country B is also $1,000. The effective tax rate for GloBE purposes (covered tax / GloBE-base) is 180/1,000 * 100% = 18%. The minimum tax level of 15% is met. Top-up taxation on the relevant GloBE-income elsewhere is not at issue. Country B has implemented a Pillar Two modelled qualifying undertaxed payments rule (UTPR).
- *Country X*. Country X applies a Pillar Two modelled qualifying Income Inclusion Rule (IIR).
- *Effect*. ParentCo is subject to Pillar Two style top-up taxation. The effective tax rate in Country A, as mentioned, is 7 percentage points too low (8% instead of 15%). ParentCo therefore owes the Country X tax authorities $70 additional top-up tax (7/100*1,000 = 70), i.e., under the IIR as implemented in Country X. For the sake of completeness, if Country X were not to apply a qualifying IIR, then Sub2 OpCo in Country B would owe the Country B tax authorities $70 backstop top-up tax, in addition to the $180 corporate tax already due, under the qualifying UTPR as implemented in Country B.

No corresponding alignment with additional taxing powers

The envisaged Pillar Two system does not provide for a parallel alignment of countries' tax treaty networks to support the top-up tax charge as created in countries by reference to the Model Rules with a corresponding adaptation of the distribution of taxing powers under the tax treaties in place, for instance, through a multilateral tax convention. In treaty scenarios this raises the question of whether, absent any such establishment of supporting additional taxing powers, the equivalent of Article 7 OECD Model Tax Convention in the relevant applicable tax treaty precludes additional taxation at local taxpayer levels on business profits produced by foreign group entities abroad.

Turning to the numerical example above, at stake here is the $70 top-up tax due by ParentCo in Country X under the IIR (primary rule), or, alternatively, by Sub2 OpCo in Country B under the UTPR (backstop rule) on the $1,000 profit produced by Sub1 OpCo in Country A. Should it not first be established for this purpose that the respective group entity established abroad, in the example Sub1 OpCo established in Country A, carries on any business activities within the territories of the relevant taxing jurisdiction(s) involved, in the example Countries X and B respectively, through a permanent establishment (PE) situated therein and to which any such taxable profits are functionally attributable? This is clearly not the case in the current example Sub1 OpCo does not operate PEs in either Country B or Country X. So, on what basis would these countries have any jurisdiction to levy top-up tax from, effectively, the Country A resident taxpayer Sub1 OpCo's $1,000 profit produced in Country A?

This, as mentioned, is a relevant matter. Treaty incompatibility at this point would mean that in the many countries where the charge to tax as created under domestic law may not interfere with the distribution of taxing powers under any operative public international law instruments such as any tax treaties in place – for such being precluded under their constitutional law – the said $70 top-up liability would become ineffective, null and void that is, under the constitutions of these countries. In the author's home-country, the Netherlands, it would be Articles 93 and 94 of the Constitution of the Kingdom of the Netherlands that would preclude any top-up taxation in such cases.

2.3 No problem…

The OECD forwards a treaty analysis to this end in its Pillar Two Blueprint.[8] The Blueprint forwards the observation that the IIR and UTPR do not pose any tax treaty incompatibility issues and can therefore be simply be implemented in the tax systems of countries, without any need for any accompanying or otherwise supporting tax treaty modification. Any IIR and UTPR top-up tax charges, the document says, would be compatible with any existing distributive rules – 'because countries can tax their residents, analogous to the OECD thinking in this regard in the OECD Commentary in relation to CFC-measures, and as is confirmed by the Saving Clause that merely codifies this principle' –, for IIRs and UTPRs do not conflict with any non-discrimination provisions – 'because from a tax legal point of view no distinction is made on the basis of taxpayer residence: the additional levy hinges on an ETR test' – nor do these conflict with TP rules (transfer pricing) – 'because the UTPR is a deduction-limitation-mechanism and not a pricing adjustment according to the at arm's length standard'.

Such a position is convenient in practical terms and perhaps politically as well. That is because – although not an argument – any absence of a need to modify tax treaty networks to cater for IIR and UTPR implementation, for instance via a multilateral instrument, immediately makes the implementation of the Pillar Two system into the tax systems of countries a lot less complicated. Otherwise, such a multilateral convention would be required here too, in addition to the multilateral tax treaty instrument already foreseen for the STTR (and the switch-over rule, which was also there at some point) and the multilateral treaty for Pillar One purposes that are already coming, and on top of the multilateral anti-BEPS convention already in place. A treaty for IIR and UTPR purposes, too, would create an administratively inconvenient additional layer of public law instrumentation.

2.4 Or is it?

To be honest, I wonder whether the IRR and UTPR application will go well under the tax treaties in place. I also have some difficulty accepting an affirmative answer here on the treaty compatibility question. The reason for this is that an affirmative answer to this end, all things considered, would necessarily entail – *reductio ad absurdum* – that countries worldwide would be enabled to subject any taxable group entity to corporate tax on effectively the worldwide profits of the multinational firm involved – and the truth is, on any arbitrarily founded taxable basis or just any basis of tax assessment for that matter – without any restriction under the tax treaties concluded (except for any profits obtained by a foreign permanent establishment or a head office). This would hold as long as 'such a levy on a resident does not reduce the profit of a non-resident', as the OECD's puts it, or paraphrasing the organization's observations to this end to be more precise. That would basically erode the effective operation of the double tax treaty networks of countries in business income taxation, the international tax regime as it currently stands, to marginal proportions. It would de facto give countries carte blanche to arbitrarily subject large multinational firms' global investment returns to extraterritorial taxation. If such were to be allowed, we might as well abolish the tax treaties immediately. Nor does this fit well, I think, with the notion of securing a single taxation of business income under the treaties.

From a more legal perspective, the line of thought and reasoning is the following. The CFC-analogy as utilized by the OECD here is not appropriate and the same applies to the extra-contextual interpretation of the Saving Clause in this regard. The top-up tax under the IIR-mechanism is not a CFC-like measure and the top-up tax under the UTPR-mechanism is not a deduction limitation. Contrary to CFCs and deduction limitation mechanisms, Pillar Two is not about a securing of taxation of domestic income. Boiled down to its essence, the envisaged Pillar Two top-up taxation effectively is an extraterritorial tax on foreign corporate profits produced by foreign group member companies, regardless of the mechanism variant used for this purpose. The underlying thinking here differs from that of a traditional CFC-measure or a traditional deduction limitation mechanism.

CFC-measures and deduction limitation measures address tax abuse and seek to protect domestic tax base against any tax-induced artificial erosion thereof and/or any artificial relocation or shifting abroad – within the existing international tax framework. CFC-measures and deduction limitation measures aim to redress an anomaly where the TP safety net (apparently) does not provide any solution or relief. The thinking focuses on the consideration that corporate profit, viewed in its implicitly assumed true nature, geographically belongs to the jurisdiction(s) where the value was created, and where it is then up to that jurisdiction to decide on whether or not to tax the income concerned or at a level of its autonomous choosing, for the income being respected as being produced within its geographical territories. The rationale here focuses on (i) the location of value creation and (ii) the addressing of any aggressive tax planning or artificial tax avoidance. Any tax-induced competition for operational investments is permitted without any restriction because such is considered to fall within the autonomous area of competences of the relevant jurisdiction(s) concerned ('BEPS 1.0').

Pillar Two addresses something else, namely all tax-competitive country responses, as we have recently come to know[9] – beyond the existing international tax framework towards a new one. The Pillar Two top-up taxation system aims to subject foreign source income, regardless of its nature, to a minimum tax-charge. From the perspective of the existing situation, the international tax framework as it currently stands that is, the envisaged additional tax aims to create an anomaly. The thinking here addresses the consideration that corporate profit, viewed in its implicitly assumed true nature, geographically belongs primarily to the jurisdiction(s) where the value was created, and then – and it is to this end that we now introduce Pillar Two – to another jurisdiction to guarantee an imposition of company taxation at a certain minimum level, i.e., if and to the extent that the former jurisdiction does not do so ("I'll tax if you don't").[10] The rationale here focuses on (i) the location of value creation and (ii) the addressing of tax-competitive responses of countries. Any tax-induced competition for operational investments is no longer permitted without any restriction because such is no longer considered to fall within the autonomous area of competences of the relevant jurisdiction(s) concerned, regardless of whether the income has been produced within its geographical territories ('BEPS 2.0'). This is a fundamental difference. Notably, the flat-rate tax-free allowance provided for in the Model Rules by reference to a percentage of labour costs and property, plant and equipment, the so-called Substance-based Income Exclusion, does not make things any different here.[11]

The point here is that the new Pillar Two anti-tax competition thinking is not part of the context of the networks of bilateral tax treaties of countries as these currently stand. The country tax treaty networks have been created and brought into existence before we started to think differently about 'putting a floor on tax competition'. The tax treaty language in the distributive rule on business profits, the phrase 'Profits of an enterprise' in the tax treaty equivalent of Article 7 OECD Model Tax Convention that is, can therefore only be interpreted grammatically, or at least not beyond the traditional existing tax framework lines of thinking in terms of separate accounting and arm's length pricing, in such a way that these profits are limited to that part of the multinational firm's investment return that is functional-analytically attributable to the respective taxable group entity involved (location of value creation, anti-tax abuse). Any Pillar Two top-up tax charge imposed on corporate taxpayers – in whichever of the variants (IIR UTPR, SOR, STTR) – ignores this, as it extends the scope of taxation to that part of the multinational firm's investment return that cannot be attributed to the respective taxable group entity, the corporate taxpayer concerned, in a functional-analytical sense.

This means that absent any explicit amendments or modifications of treaty contexts and distributive rules to this end, any additional tax charge under the Pillar Two top-up tax system in all its variants thus comes into conflict with the existing tax treaties. This also means that to enable an effectuation of any additional extraterritorial levy under the Pillar Two top-up tax system, the new BEPS-2.0 anti-tax competition thinking should therefore first be incorporated into the treaty texts, and not just regarding the STTR as currently foreseen. While some creative dynamic interpretative bending of distributive rules in CFC-matters could perhaps be considered equitable and justified for reasons of combating tax abuse and domestic tax base protection, it seems to me that this should be rather different when it concerns a putting in place of any extraterritorial top-up taxation mechanisms for anti-tax competition reasons beyond the corporate veil. For that we will really have to take up the treaty texts first and start working on some textual modifications to facilitate any such cross-border top-up tax endeavors.

For the sake of completeness, already the treaty (in)compatibility of CFC measures is viewed and assessed rather differently in countries in practice.[12] From that perspective it does not seem unlikely to imagine that tax courts and judges in countries – *a fortiori* – may perhaps turn out to consider and rule on the treaty (in)compatibility of their countries' IIRs and UTPRs at least as differently as currently is the case with their CFC-measurers; at least if these tax courts and judges would not wish to marginalise the effective scope of application of the tax treaty networks of the countries they are institutionally part of. In the light of the envisaged global coordination of the Pillar Two system, or at least in view of some of the expressions that have been made into that direction, the potential of a global fragmentation of court rulings in this area seems to me to be a relevant matter, or at least not a matter to be taken too lightly.

2.5 Putting strain

Maybe I am a tax treaty purist or tax treaty nostalgic, that is very possible, but my feeling is that the OECD is putting quite some strain here when it comes to an effective future operation of the envisaged new tax framework. Assuming Pillar Two should be the route to pursue, it would be preferable in my view to then also proceed to secure a parallel distribution of taxing rights in relation to all Pillar Two top-up tax mechanisms in an instrument of public international law. Reasons for doing so lie in the principles of legality and legal certainty and may also be found in more pragmatic considerations, such as to avoid any risk of regret afterwards in advance when confronted with the effects of any omissions here. Without a legal basis in international public law such as a multilateral tax treaty that provides for a parallel adaptation of tax treaty networks of countries to support the envisaged creation of charges to additional tax with some corresponding taxing powers, a slippery slope will be embarked upon towards arbitrary company taxation lacking any legitimization.

If this were not to be addressed, chances are that legal proceedings may be lying in wait, and if so on a global scale. Companies that were to be confronted with a Pillar Two top-up tax assessment in a country in due course will have no legal reason at that time not to object and appeal against this and to litigate the matter through the court system of the country concerned. It could very well be the case that the first company to be confronted with such a tax assessment immediately goes to court. And then it could just be that within a few years we will see legal proceedings to start running worldwide with all kinds of different outcomes. The latter alone seems to me to provide sufficient reason for the committing countries within the Inclusive Framework to perhaps for instance re-visit the tax treaty aspects of the envisaged new tax framework, particularly now that we are still at the front end of the technical discussion.

For the sake of completeness, the consideration that yet another multilateral treaty will make things very complicated does not seem to me to be an argument, just because this is merely the logical consequence of the choices that have been made to stack business income tax systems and benchmark shadow business income tax systems. If such complications were to be considered to be in need of being avoided, then perhaps a simpler tax reform than the two-pillar solution should have been devised and developed within the Inclusive Framework. International tax literature provides a wide range of alternative solutions and reform options to address the matter of the outdated century old company tax framework, such as cash flow taxes, formulary systems, and residual profit split models.[13] But who knows, perhaps things will turn out not quite as bad as they seem. Perhaps countries will turn out to have nudged each other just enough that we will end-up in a scenario where countries worldwide subject business income to corporate tax levels in adherence to the global minimum level so that the top-up tax will never be applied. Or, perhaps, countries will discover that the additional tax is in violation of the tax treaties they concluded with each other and then use this to shatter any newly established company tax equilibrium to continue the tax competition game.

Closing comments

Is the envisaged Pillar Two top-up tax system under the IIR and UTPR at odds with the distributive rules for business profits in the tax treaty networks of countries worldwide? It looks a bit like it, although we never know of course what the future holds for us. Whatever the case may be, as far as I am concerned, any extensively dynamic extra-contextual CFC analogies and ditto Saving Clause interpretations are not a panacea for a non-addressing of the misalignment we see arising here between taxing right creation (domestic legislation) and taxing power distribution (tax treaties). Perhaps therefore we should reconsider, also in view of a safeguarding of the systemic integrity of the tax treaty networks of countries. If we really want to continue the two-pillar path we have taken, my perspective would be to devise an international public law mechanism that provides for a parallel adaptation of countries' tax treaty networks to support, and legitimize, the top-up taxation mechanism with a corresponding distribution of additional taxing powers. And otherwise, we may probably be looking forward to be seeing some developments in the judiciary in future. We will see.

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[2] See OECD (2021), Tax Challenges Arising from the Digitalisation of the Economy – Global Anti-Base Erosion Model Rules (Pillar Two): Inclusive Framework on BEPS, OECD, Paris, https://www.oecd.org/tax/beps/tax-challenges-arising-from-the-digitalisation-of-theeconomy-global-anti-base-erosion-model-rules-pillar-two.htm (Model rules).

[3] *See* Maarten de Wilde, 'Is there a Leak in the OECD"s Global Minimum Tax Proposals (GLOBE, Pillar Two)?', Kluwer International Tax Blog, March 1 2021, http://kluwertaxblog.com/2021/03/01/is-there-a-leak-in-the-oecds-global-minimum-tax-proposals-globe-pillar-two/.

[4] *See* Article 3.2.7 Model Rules.

[5] *See* Elmer Smaling, ' Why abolishing tax havens could lead to chaos, Erasmus Magazine, 30 September 2021, https://www.erasmusmagazine.nl/en/2021/09/30/why-abolishing-tax-havens-could-lead-to-chaos/?noredirect=en_US.

[6] See OECD (2020), Tax Challenges Arising from Digitalisation – Report on Pillar Two Blueprint: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, https://doi.org/10.1787/abb4c3d1-en (Pillar Two Blueprint), at Sec. 10.4. 'Treaty compatibility'.

[7] Some literature on the interaction between Pillar Two and the tax treaties has been published on which this contribution aims to build. See for example Vikram Chand, Alessandro Turina, Kinga Romanovska, 'Working Paper – Tax Treaty Obstacles in Implementing the Pillar Two Global Minimum Tax Rules and a Possible Solution for Eliminating the various challenges', 23 Nov 2021, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3967198, Aitor Navarro, 'Jurisdiction Not to Tax, Tax Sparing Clauses and the Income Inclusion Rule of the OECD Pillar 2 (GloBE) Proposal: The Demise of a Policy Instrument of Developing Countries?', Copenhagen Business School, CBS LAW Research Paper No. 20-22, 24 Aug 2020, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3678169, Pasquale Pistone, João Félix Pinto Nogueira, Betty Andrade and Alessandro Turina, 'The OECD Public Consultation Document "Global Anti-Base Erosion (GloBE) Proposal – Pillar Two": An Assessment', *Bulletin for International Taxation*, 2020 (Volume 74), No. 2, Joachim Englisch and Johannes Becker, 'International Effective Minimum Taxation – The GLOBE Proposal', *World Tax Journal*, 2019 (Volume 11), No. 4. The current analysis also builds on my comments in the Dutch tax weekly Nederlands Tijdschrift Fiscaal Recht on the Inclusive Framework Tax Deal of 8 October 2021 (*NTFR* 2021/3793).

[8] See Pillar Two Blueprint, *supra note* 3, at Sec. 10.4. 'Treaty compatibility'.

[9] *"The global minimum tax agreement does not seek to eliminate tax competition, but puts multilaterally agreed limitations on it"*, 'International community strikes a ground-breaking tax deal for the digital age', OECD, 8 October 2021, https://www.oecd.org/tax/international-community-strikes-a-ground-breaking-tax-deal-for-the-digital-age.htm.

[10] See for a comparison, Maarten Wilde and Ciska Wisman, 'OECD Consultations on the Digital Economy: "Tax Base Reallocation" and "I'll Tax If You Don't"?', in: D.M Weber & P. Pistone (Eds.), *Taxing the Digital Economy; The EU Proposals and Other Insights*,IBFD, Amsterdam, 2019, at 3-23.

[11] Note that the Pillar-Two-system were to actually focus on top-up taxing excess profits only (what in such a case may lead to a follow-up question on the merits of the Amount A calculation under Pillar One as this mechanism, too, seeks to calculate and geographically distribute excess earnings, or non-routine profits in transfer pricing terminology, however, too, on the basis of a flat rate mechanism yet different from the one as used for Pillar Two top-up tax purposes), this does not mean that by, inference, any division thereof under the transfer pricing model to countries that tax below the minimum level should be labelled tax avoidance to subsequently justify top-up taxation in other countries elsewhere on this basis. That seems to me going a few steps too far. And should this be different, this rather says something on the functioning, or non-functioning perhaps, of the arm's length standard as a methodical building block of international company taxation and with that, at least potentially, an argument perhaps for reforming existing tax base division methodologies here. This, however is not what Pillar Two does, as it actually embraces arm's length pricing as the central GloBE-income-division mechanism under the jurisdictional blending approach, and then it cannot be something else but either A or B, i.e., A: Pillar Two addresses tax avoidance rather than tax competition bringing into a questioning of the conceptual validity of the arm's length principle, or B: the arm's length principle is conceptually valid and with that Pillar Two addresses tax competition rather than tax avoidance.

[12] *See*, in addition to the literature referred to above Daniele Canè, 'Controlled Foreign Corporations as Fiscally Transparent Entities. The Application of CFC Rules in Tax Treaties, *World Tax Journal*, 2017 (Vol. 9), No. 4.

[13] I myself came-up with a tax model that divides global economic profits of business enterprises among countries on the basis of a destination-based revenue key, *see* M.F. de Wilde, 'On the Future of Business Income Taxation in Europe', World Tax Journal, Vol. 12 (2020), No. 1.

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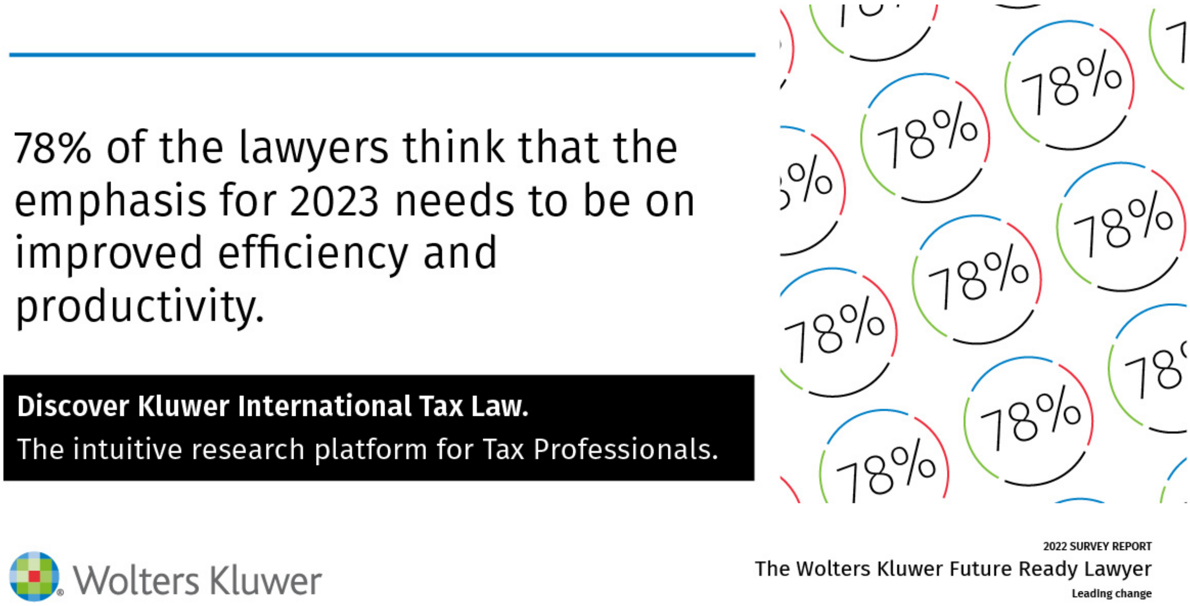

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