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Fiscal Subsidies Aspirers Beware of the No Benefit Requirement in Pillar Two

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Summary

Vietnam reportedly considers granting subsidies to large multinationals with direct investments in the country, to compensate them for the higher taxes they may have to face there following the country's introduction of Pillar Two domestic minimum top-up taxation rules per 2024. The OECD warned Vietnamese government officials that if subsidies to multinationals were found to constitute a direct compensation for the higher levy under Pillar Two, the domestic top-up tax would be disqualified. Multinationals would then still have to pay top-up levy regardless, in other jurisdictions that is, to meet the envisaged global minimum 15% tax level. This article elaborates on the No Benefit Requirement ('NBR'), an underexposed element of Pillar Two. If a country were to observe that some other country's Pillar Two top-up tax rules disqualify as such, on the basis that this other country provides benefits to companies in relation to its top-up tax, the first-mentioned country would proceed to top-up taxing those companies on their foreign earnings itself: "I'll tax if you don't". One might expect that such a far-reaching fiscal intervention by one sovereign nation in the economy of any of its sovereign peers would only be possible and legitimized on the basis of a principled clear-cut bright-line test, founded and legitimized in the rule of law and embedded in an institutional framework governed by international public law. That, however, is not the case - at all.

1 Introduction

Vietnam reportedly considers granting subsidies to large multinationals with direct investments in the country, to compensate them for the higher taxes they may have to face there following the country's introduction of Pillar Two domestic minimum top-up taxation rules per 2024.[1] Without some sort of compensation for the increased corporate tax burden imposed, the fear of the

Vietnamese government is that the higher levy would make the country a less attractive investment jurisdiction for large multinationals. Multinationals that operate in the country reportedly have been asking for compensation in private talks with government officials. In response to Vietnam's considerations, the OECD warned Vietnamese government officials that if subsidies to multinationals were found to constitute a direct compensation for the higher levy under Pillar Two, *"the domestic top-up tax would be disqualified"*. The news report says that the OECD has been making it clear that large companies would then still have to pay top-up levy regardless, in other jurisdictions that is, to meet the envisaged global minimum at a fixed 15% tax level. Such top-up tax would be collected, for instance in the respective multinationals' headquarters jurisdictions under the envisaged income inclusion rule ('IIR'), or elsewhere under the envisaged Undertaxed Profits Rule ('UTPR').

The news report illustrates a significant yet to this date rather underexposed element of the envisaged Pillar Two global minimum company taxation regime: the No Benefit Requirement ('NBR').[2] The NBR is an anticipated anti-abuse rule in the Pillar Two system that establishes the notion that jurisdictions may not provide any benefits to multinationals related to the implementation of Pillar Two top-up taxation rules in their domestic tax system. Any non-meeting of the envisaged NBR by a country – allegedly Vietnam in the news report – will result in that country not having a *"qualified"* domestic set of Pillar Two top-up taxation rules in the view of other countries under the internationally politically endorsed Pillar Two framework. A disqualification of domestic top-up taxation rules on that basis may subsequently render any business profits produced in the first-mentioned country subject to top-up taxation by these other jurisdictions. Such a top-up taxation may negate any anticipated effects of any such benefits granted to the respective business enterprises by the first-mentioned country.

The NBR in the Pillar Two system lies at the heart of perhaps the biggest hurdle to overcome politically when it comes to establishing a pursued floor in country tax competition: nation state fiscal autonomy. Do countries really want to give up their autonomous competences in establishing their policies, where the rubber hits the road, when it comes to the instrumentalization of their tax systems to attract and sustain domestic business investment? This is a thorny issue, also considering for instance the launch this summer by the OECD's Inclusive Framework ('IF') of a temporary safe harbor mechanism in the envisaged Qualified UTPR.[3] The newly established transitional UTPR allows for a calculation of the UTPR top-up tax amount to be nil if the jurisdiction of the ultimate parent entity ('UPE') of the multinational involved operates a nominal statutory 20% tax rate (and accounting for subnational taxes).[4] The UTPR effectively replaces the effective tax rate ('ETR') calculations for Pillar Two UTPR purposes in UPE jurisdictions with a subject-to-a-nominal-20%-tax-rate-test. It is generally known that a whole world exists between statutory tax rates and effective tax rates. The UTPR safe harbor accordingly effectively creates room for maneuver for headquarters jurisdictions (read: the biggest economies[5]). The effect of the UTPR Safe Harbour is that it allows UPE jurisdictions to continue competing for investment via their tax systems, without having to worry about facing any subsequent tax subsidy neutralizing backstop UTPR top-up taxation implications in countries abroad – as long as these countries meet the 20% headline tax rate test. The UTPR Safe Harbour has been pitched by the IF as a temporary measure and is said to operate effectively only during the first couple of years in which Pillar Two comes into effect.[6] We will have to see if the safe harbor will actually be rolled back when the term has expired, or whether it will survive a little while longer – our bet would be on the latter. This begs the question as to the underlying merits of the OECD's warnings towards Vietnam, a lower middle income country seeking ways to continue competing for investment and economic growth too, considering the concurrent legitimization of some similar aspirations of headquarters jurisdictions in the developed world. The authors elaborate on the NBR, its underlying thinking and operation, as well as some potential implications of falling foul under the set conditions.

2 The Collide of Pillar Two with Country Tax Incentives

2.1 Level Playing Field

As part of the two-pillar solution to address the challenges raised by the digitalization of the economy, and to bring fairness to the corporate tax world, Pillar Two introduces a new alternative worldwide business income taxation framework for large multinationals (consolidated revenue above €750 million) at a rate of 15%.[7] The envisaged measures set a global 15% minimum tax rate, a new standard, and top-up taxation to this new standard by countries if and insofar as other countries, low-tax jurisdictions that is, do not conform ("*I'll Tax If You Don't*").[8] With a view to the globally centralized Pillar Two framework's decentralized implementation, the OECD published Pillar Two Model Rules on 20 December 2021.[9] These rules were followed, on 14 March 2022, by the Pillar Two Model Rules Commentary,[10] while the introduction of Pillar Two within the EU has been provided for in the EU Directive of 14 December 2022.[11] The OECD released batches of additional administrative guidance documents on 2 February 2023[12] and on 17 July 2023.[13]

The objective of the envisaged global minimum tax framework is to address any remaining issues of Base Erosion and Profit Shifting ('BEPS') and to ensure a level playing field between countries.[14] The level-playing-field-language notably echoes EU internal market language on which the fundamental freedoms, state aid rules and intra-EU tax harmonization efforts have been built. Pillar Two seeks to bring the hypothesized race to the bottom to a halt through the introduction and establishment of a floor to tax competition. Pillar Two accordingly effectively entails the introduction of a globally coordinated minimum company taxation system. To the extent effective, the establishment of a worldwide baseline corporate tax regime will render moot any individual countries' aspirations to compete for business investment via their company tax systems below the newly established global tax bar. And that of course has a significant impact on the ability of jurisdictions to stimulate, attract and sustain (foreign) direct investment via tax incentives and tax subsidies. Viz., any tax incentivization of investment below the bar would be neutralized as to its effectiveness with a corresponding top-up taxation to the minimum level, in the relevant tax-subsidizing country involved for instance, via a domestic top-up tax (Qualified Domestic Minimum Top-up Tax; QDMTT), or in any other country where the in-scope multinational firm is operational, via an extraterritorial top-up tax in the appearance of the envisaged IIR or UTPR.

2.2 Incentives

The Pillar Two measures target countries' behavioral responses relating to what has traditionally been considered harmful tax competition (for paper investment and for paper profits) as well as what has traditionally been considered fair tax competition (for real investment and for real profit).[15] The minimum tax, in principle, targets investment returns in countries both in relation to direct investment (active income) and in relation to portfolio investment (passive income). The traditional thinking however, in the pre-Pillar Two age that is, differs from the current approach and has been that sovereign nation states should be entitled to autonomously decide on the establishment of their tax policies, their tax levels, their tax mixes and their (tax) expenditures; their public finances basically. And that includes any tax incentivization efforts and aspirations thereto relating to real economic activity and real investment within their territories. The traditional thinking is that only those predatory tax regimes seeking to attract paper profits and to stimulate aggressive tax planning responses of businesses enterprises (harmful tax competition) are to be considered problematic and to be properly addressed and countered. This also is the line of thinking that lies at the heart of the BEPS project of the G20/OECD of which the outcomes were released in October 2015.[16] The same holds for the double tax conventions. These too typically do not establish a general effective minimum tax rate standard as a gateway criterion for tax relief.[17] With the emergence of Pillar Two the thinking here has implicitly yet paradigmatically shifted. The thinking today, it seems, is that any tax competition or perhaps even any fiscal competition for corporate investment – see further below – below a certain bar is to be considered problematic, also when it comes to attracting real economic activity, and accordingly a matter to be addressed.

This said, concurrently, many countries – of which many politically committed themselves to the global two-pillar solution in 2021 – nevertheless have put various tax incentive mechanisms and subsidy mechanisms in place in their fiscal systems.[18] Such mechanisms are typically devised to attract and sustain certain economic activities, sectors, or industries, i.e., to address any economic, social, or environmental policy goals and objectives, which the respective country politically considers of sufficient societal relevance to promote these via fiscal interventions. The incentives countries utilize to reduce the costs of doing business to that end come in great varieties. At the expenditure side of fiscal policy one may typically see subsidies and grants and at the revenue side of fiscal policy one may typically see tax incentives in various forms and shapes, such as special tax zones and economic zones for production and manufacturing activities for instance, tax holidays, tax breaks, tax exemptions, reduced rate regimes like 'box regimes' for patents and the likes for instance, as well as tax credits of which some may even be refundable. Tax incentives can be found in company tax systems addressing both the cost side of business (investment incentives, super deductions, et cetera) as well as the revenue side of business (reduced rate regimes, tax credits, et cetera). Tax incentives may also be found in other types of taxes, in wage tax regimes for instance allowing for a lowering of wage costs in certain ranges of economic activity.

2.3 Tension

The reality of a global pursuit of a Pillar Two reform to mitigate tax competitive responses, while individual countries' concurrently pursue tax subsidizing aspirations to compete for business investment, creates tension. Unlike individual country company taxation systems, the envisaged Pillar Two system does not contain that many openings that cater for sustaining country tax competitive responses, outside perhaps some room for accelerated depreciation allowances, some room created relating to the cost-plus oriented tax allowance developed in the Pillar Two context named Substance Based Income Exclusion ('SBIE'),[19] as well as via the openings created in the Pillar Two rulebooks for so-called Qualified Refundable Tax Credits ('QRTCs'[20]) including its recently devised variants (Marketable Transferable Tax Credits; 'MTTCs').[21] Pillar Two seeks to comprehensively address tax competitive responses, as competing for investment via government fiscal interventions pressurizes the very objectives pursued of establishing a global level playing field in company taxation.

Tax incentives, grants, and subsidies in company tax rules produce permanent differences in comparison to Pillar Two rules and accordingly have a downward impact on Pillar Two jurisdictional ETRs. Any government incentive driven givebacks which are not equivalently catered for under Pillar Two may either result in an increase of income – the denominator of the Pillar Two ETR fraction – or in a reduction of taxes – the numerator of the Pillar Two ETR fraction – for purposes of calculating the Pillar Two ETR in the respective country involved. Wherever these jurisdictional ETRs were to drop below the 15% minimum level in a country, top-up taxation implications will subsequently be called upon to kick-in and neutralize these. Such a top-up taxation may become due in the relevant country granting the subsidy or incentive itself via a QDMTT (if the country involved were to decide to implement such), or elsewhere, via an IIR in the multinational's headquarters jurisdiction abroad for instance, or via a UTPR in any of the multinational's subsidiary jurisdictions abroad.

The point is that analytically one cannot have both: incentives in individual countries to compete for investment and a worldwide minimum tax framework to level the global playing field. Essentially, any tax incentive mechanism creates some foundational tension with the objectives pursued under Pillar Two. This also holds if the incentive involved is designed in a way to be geared to facilitate substantial operational (i.e., non-artificial, transparent) investment in a country in a proportional, well-targeted and well-substantiated manner, for instance in terms of any such incentives addressing any relevant economic, social and/or environmental goals. One just cannot simultaneously desire putting a floor to tax competition by neutralizing disparities and ensuing behavioral responses on a global macro-level basis, and desire a sustaining of tax incentives by fostering disparities and ensuing behavioral responses on a per-country micro-level basis. It is either or. Countries nevertheless seem to be seeking both regardless. And there we have the fundamental problem.

3 The No Benefit Requirement

3.1 Countering Any Neutralization of Neutralization Efforts

Where does the NBR fit in? The news article reports on Vietnam being transparent in seeking ways to channel any raised Pillar Two top-up tax revenue back to business communities via tax subsidies, grants or incentives. Such would basically create a cash carousel, i.e.: (i) taxing business profits subpar under the country's company tax system, (ii) subsequently proceeding to top-up taxing such low-taxed business profits on par under a Pillar Two style domestic minimum top-up tax mechanism, while (iii) sub-subsequently channeling the tax money back to businesses via subsidies. Such a government response would be a clever way to unilaterally neutralize, or undermine, the globally coordinated tax competition neutralization objectives underlying the Pillar Two system. If such a unilateral exercise were to be effective it would reintroduce the fiscal race for investment, while transforming Pillar Two into a paper tiger, at least to a certain extent. Such a move, a fiscal Whac-A-Mole exercise basically, would hold, if not for the NBR in the Pillar Two rulebook.

The Pillar Two rulebook says that a domestic top-up tax should be *"implemented and administered in a way that is consistent with the outcomes provided for under the GloBE Rules and the Commentary"*.[22] Such a top-up tax would not qualify as such if the jurisdiction involved *"provides any benefits that are related to such rules"*, i.e., the NBR.[23] Then *"[t]he domestic top-up tax would be disqualified"*, as the OECD officials reportedly warned Vietnamese government officials.

What is basically said here is that only a top-up tax that qualifies as such under Pillar Two will have as a consequence that other countries shall adhere to the Pillar Two ordering rules and let go of any backstop extraterritorial top-up tax aspirations. Notably, any top-up tax in a country and in any of its appearances (DMTT, IIR, UTPR), needs to qualify, making such a top-up tax a 'qualifying' DMTT, IIR, or UTPR. The "Q" comes in all variants and all embed the NBR, i.e., not only the QDMTT. This also means that DMTTs in countries only take priority over IIRs while IIRs in UPE countries only take priority over IIRs and UTPRs in other countries if the top-up taxes involved certify. Countries seeking to secure a non-surrendering of tax revenue to foreign countries, hence, need to ensure that any introduced domestic top-up taxation systems pass muster under peer scrutiny. Given that Pillar two introduces a global minimum tax to be operated on decentralized domestic bases, jurisdictions will have to proceed to review any top up taxes introduced by their peers as to their merits and assess whether these meet the requirements as outlined in the Pillar Two Model Rules and the Administrative Guidance. In the event that such an assessment would lead to the observation that a top-up tax introduced by a peer jurisdiction does not qualify as such, top-up tax will be due in the assessing jurisdiction(s).

It should be noted that an exception to this approach has recently been launched in relation to the UTPR.[24] The transitional UTPR Safe Harbour that was released by the IF this summer as part of the second batch of Administrative Guidance has created an exception to the operation of the UTPR in this regard. The UTPR Safe Harbour effectively replaces the Pillar Two ETR calculations in the UPE jurisdiction for UTPR purposes, including the NBR, with a 20% statutory tax rate test, thereby negating the NBR in the UTPR context. The effect of the recent intervention is that UPE jurisdictions now have been granted some significant leeway, allowing these jurisdictions to effectively escape Pillar Two top-up taxation to some significant extent under any operational UTPRs abroad, and thereby sustain their tax subsidies for domestic investment, at least as long as the safe harbor is kept in place. This said, it should be noted that the EU Directive implementing Pillar Two in the EU, as it currently stands, does not cater for such a safe harbor, meaning that if an EU Member State were to adhere to the UTPR Safe Harbour that Member State may concurrently infringe its legal obligations under supranational EU law.

3.2 Little Interpretative Guidance

The OECD's commentary to the Pillar Two Model Rules provide little interpretative guidance as to the meaning of the phrase *"provides any benefits related to such rules"*. The available OECD materials dealing with the matter use very broad language in this regard, saying that the term 'benefits' would include not only tax incentives but also any grants or subsidies, indicating that the term is comprehensive enough to cover any kind of advantage provided by a jurisdiction.[25] The reference to 'any kind of advantage' implies that not only incentives at the revenue side of fiscal policy would be eligible to fall within the scope of the rule, taxes that is. The NBR would potentially include incentives in corporate taxation, withholding taxation and any other taxes in lieu of income taxes, and potentially also in other types of taxes like wage taxes and payroll taxes. In addition, the language used is extensive enough to also encompass incentives at the expenditure side of fiscal policy, subsidies that is, and grants and their likes. If such were proven to be true, the scope and potential impact of the NBR would not only encompass any tax incentives outside business income taxation but would also encompass any government subsidizing interventions at the expenditure side. Indeed, such a pulling-in of the expenditure side into the realm of Pillar Two would be far-reaching. Then, Pillar Two would not only put a break on country autonomy in company taxation, it would basically intervene in country fiscal autonomy altogether. Moreover, such an intervention in a country's power of the purse would effectively occur via OECD model rules and OECD interpretative language to which IF countries have politically committed; interventions, that is, from sources outside the realm of the rule of law.

The OECD's outputs so far are also rather silent on the required causality, the relationship that is, between any benefits granted in the country and the Pillar Two domestic top-up taxation rules in that country. The OECD materials forward that the phrase *"related to such rules"* is intentionally drafted with broad language to take into account different mechanisms through which the benefit may be provided.[26] The OECD also forwards that the relationship should be determined on the basis of facts and circumstances.[27] In this regard, the OECD notes that the underlying principles are to be taken into account which is to 'provide a level playing field among all jurisdictions and to avoid inversions incentivized by differences in the implementation and application of the GloBE Rules'.[28] This, does not seem that helpful as any unilaterally introduced fiscal incentive, ceteris paribus, affects investment location decisions and, hence, in a strict analytical sense distorts the pursued level playing field. Such would imply that potentially any fiscal benefit provided would suffice to render the top-up tax involved to potentially fall foul under the envisaged Pillar Two rules. The OECD also considers it of relevance though indecisive (i) whether the tax incentive involved only benefits taxpayers subject to Pillar Two, (ii) whether the tax incentive is marketed as part of Pillar Two, and/or (iii) whether the tax incentive has been introduced after the OECD started discussing the Pillar Two rules.[29]

3.3 A Wide Range of Candidate Interpretations

The explanatory language that the OECD makes use of consequently opens the door for a wide range of candidate interpretations of the NBR and its scope of operation. The spectrum comprises a variety of interpretations that countries may pick and choose from, with some narrow interpretative approaches available on the one outer end of the spectrum to the availability of some extensive interpretative approaches on the other outer end of the spectrum. If interpreted narrowly the phrase 'related to' may be understood to require a very strict or direct and explicit or explicated relationship between the benefit provided and the top-up tax collected, for instance some explicit language connecting the two in the relevant legislation, in the country's parliamentary papers, or perhaps in any expressions of responsible ministers, government officials or tax authorities executives. As noted, the OECD considers the marketing of an incentive as part of Pillar Two a relevant but indecisive indicator. If interpreted extensively, the phrase 'related to' may be understood to require just some marginal relationship between the benefit and the top-up tax, for instance in terms of the timing of the legislative instruments. Then, a mere existence of any grants, incentives or subsidies at the time of the putting in place of the Pillar Two top-up tax system may be considered sufficient. The same may be the case in the event of an introduction of such benefits in the legislation of the country involved subsequent to the introduction of Pillar Two in the country's tax system. The OECD, as noted, seems to consider the timing of the rules a relevant yet indecisive indicator. One may potentially even arrive at a point observing that a mere connection in terms of the economic operator being subject to Pillar Two rules being the same economic operator benefitting from the respective grant involved would suffice to arrive at the discovery of some perceived causality triggering a disqualification of the peer country's domestic top-up tax involved. As noted, the OECD considers a connection of tax and benefit at taxpayer level a relevant but indecisive indicator.

The available OECD materials forward that further guidance from the OECD on the operation of the NBR is anticipated.[30] So far, however, it is not there. Accordingly there is no white spot, there is no bright-line test or safe harbor available, nor has such been put into place, that can be inferred or be pointed at for purposes of interpreting the NBR in a clear and concise manner. Worthy of note is that the Commentary to the Pillar Two Model Rules outlines an example (referring to the assessment of the "Qualified", the "Q" that is, in the IIR, which, as noted, equivalently applies to the "Q" in the "Qualified" DMTT).[31] The OECD's example is a rather obvious one to be honest, connecting the quantity of the benefit provided in a strict relationship with an equivalent quantity of the top-up tax collected, in the form of a top-up tax credit in the top-up tax system: *"for instance, assume a jurisdiction has adopted all of the provisions of Pillar 2 in its legislation. […], but it provides a tax credit equivalent to a portion of the tax paid under the IIR to be used against other taxes. In this case, the jurisdiction has not adopted a Qualified IIR."* The OECD materials also say that *"a tax benefit or grant provided to all taxpayers is not related to the GloBE Rules"*.[32] Indeed, illustrative though rather obvious perhaps, and, hence, rather unhelpful. A perhaps related question may be what would happen if a country introducing Pillar Two were to concurrently introduce a QRTC in its (top-up?) tax system in conformity with the parameters set out in the Pillar Two Model Rules and explicitly as a benefit provided to mitigate any effective Pillar Two domestic top-up tax exposure? Would such a tax credit disqualify the top-up tax under the NBR? Is an "RTC" only a "QRTC" for Pillar Two purposes if put in place in a mainline corporate tax, instead of for instance an alternative minimum tax (or an alternative minimum Pillar Two tax)? Would not that potentially create some circularity issues? We would not be sure to be honest.

Nevertheless, under the NBR in the envisaged Pillar Two rules, countries will need to proceed and assess each others' domestic top-up taxation rules in combination with any existing and new grants, subsidies, tax incentives, and any other government support, as made available and made use of by multinationals in any of the countries involved in which the multinational is operational to determine NBR (non-)conformity. Such an assessment would need to be made in view of any consecutive qualification or disqualification of peer country top-up tax rules. The consequence, as noted, could be an opening to any subsequent top-up taxation implications in the respective assessing countries under their own top-up taxation rules. To this end it should be kept in mind that Pillar Two will be implemented on a decentralized basis by individual countries in their domestic tax legislation. At the end of the day, Pillar Two will be operated along the rules of individual countries' domestic laws, local tax practices and local tax and legal cultures. Jurisdictions may likely take on and develop autonomous interpretations, rulebook operations and dispute resolving mechanisms. Absent a body having a central authority involving Pillar Two – the OECD does not have any legislative, executive, and/or interpretative authority – taxpayers and tax authorities will both have to analyze and assess both existing and new incentives, grants and any other government support in place in countries across the world to determine any conflict or compatibility with the NBR.

3.4 A Wide Range of Candidate Approaches

The approaches of countries towards their peers in relation to the NBR-operation may likely range widely as well, from those adopting strict interpretations to those adopting extensive interpretations. There too, incentives emerge for countries to strategise upon. Note that a strict interpretation of the NBR by countries implies a lenient approach towards other countries' top-up tax rules. The consequence of a lenient approach would be that countries involved would be enabled to strategise on a non-establishment of a causal relationship between Pillar Two and their subsidies. Countries would accordingly re-enable themselves and each other to re-engage into a sustaining of their policies of attracting business activity via fiscal incentives, pressurizing the pursued leveling of the playing field. Such may reinvigorate the fiscal competitive race for investment. An extensive interpretation of the NBR by countries implies a stringent approach towards other countries' top-up tax rules. The consequence of that would be the putting an end to country competition for investment. The trade-off, however, would be the creation of potentials for tax cascading, controversy, and a paralyzation of country governments in their ability to instrumentalise their fiscal system as a policy steering device. Such would encroach on the notion of nation state sovereignty. So, what route would be a beneficial one to take for any relevant country concerned? A lenient approach towards foreign countries' top-up taxation rules to attract company headquarters for instance? Or a stringent approach towards foreign countries to secure potential additional tax revenue collection from overseas investment returns? Indeed, a matter for countries to strategize on. And indeed, it also does not seem too unlikely that the potential for a variety of interpretations and applications may materialize in future by inference.

A paper published by the OECD in 2022 on tax incentives in post-Pillar Two realities fairly submits that governments should reassess and carefully consider their tax incentive regimes.[33] The paper also says that Pillar Two could be an opportunity to reconsider and to proceed to reform any tax incentive regimes utilized. The narrative here seems that Pillar Two is not intended to restrict the ability of jurisdictions to make changes to the design of their corporate tax systems in light of a post-Pillar Two tax architecture, as long as these changes do not result in tax outcomes inconsistent with those provided for under the Pillar Two rules. That brings the current analysis back to where it started. As said, OECD outputs on Pillar Two also note that releases of some further guidance on the identification of benefits related to the QDMTT are under consideration. The OECD has also announced that it will commence a peer review process later this year and assess country Pillar Two implementation the outcomes of which will ultimately be published on the OECD's website 'so the taxpayers and tax administrations can rely on and use them to simplify the operation of the system'.[34] So far however, as said, no further materials have been published or released. That does not seem to be particularly helpful, also considering that Pillar Two is envisaged to become operational as of 2024, already within 4 months.

4 Implications of Falling Foul under the NBR

4.1 A Numerical Example

Moreover, the OECD materials do not say anything on the consequences of when a country at some point disqualifies some other country's domestic top-up tax rules under its interpretation of the NBR. Let us for instance assume a scenario in which the NBR has not been met by a country. An other country has looked into that country's Pillar Two implementation rules, has subjected these to an NBR-assessment, and has arrived at the observation that the assessed country has provided benefits to multinational companies that operate investments in the assessed country in the form of (tax) subsidies related to the assessed country's Pillar Two domestic top-up tax rules. What happens then? Top-up taxation, sure, but at what amount? What about the ETR calculations? Should the subsidy decrease the numerator in the Pillar Two ETR fraction? Should the subsidy increase the denominator perhaps? Is a non-qualifying domestic top-up tax to be regarded as a Covered Tax for Pillar Two purposes? If so, on what basis?

Let us explore some potential implications of falling foul under the NBR by reference to a stylized numerical example.

Box 1. Base Case; Qualifying DMTT

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 Two system. Countries X, A, and B all have implemented Pillar Two rules in their company tax systems. ParentCo X, Sub1 OpCo and Sub2 OpCo all are Constituent Entities (CEs) for Pillar Two purposes. Let us assume for simplicity reasons that unless mentioned otherwise no disparities exist in the perspectives of Countries X, A, and B on the operation of the Pillar Two rules.

? *Country A.* In Country A, the corporate tax base is $1,000. The corporate tax due by Sub1 OpCo is $100. For the sake of simplicity, let us assume that the GloBE-base in Country A is also $1,000. The ETR for Pillar Two purposes (Covered Tax / GloBE base) is 100/1,000*100%=10%. The minimum tax level of 15% is not met. The effective rate is 5 percentage points too low (10% instead of 15%). Additional tax on the relevant GloBE-income will be levied under the Pillar Two top-up taxation system, under either a QDMTT (Country A), IIR (Country X) or UTPR (Country B). Let us assume that Country A has put in place a Pillar Two style QDMTT. Sub1 OpCo is subject to the QDMTT. The ETR in Country A, as mentioned, is 5 percentage points too low (10% instead of 15%). Top-up tax is imposed at the rate set by reference to the difference between the jurisdictional ETR (10%) and the minimum rate (15%), i.e., 5%. Let us assume for the sake of simplicity that the basis against which the top-up tax is assessed is $1,000 (i.e. excluding the SBIE allowance). Sub1 OpCo therefore owes the Country A tax authorities $50 additional tax (5%*1,000=$50).

? *Country B.* In country B, the corporate tax base is $2,000. The corporate tax due by Sub 2 OpCo is $400. For the sake of simplicity, let us assume that the GloBE-base in Country B is also $2,000. The ETR for Pillar Two purposes (Covered Tax / GloBE base) is 400/2,000*100%=20%. The minimum tax level of 15% is met. The effective rate is 5 percentage points above par. No additional tax on the relevant Country B GloBE-income will be levied under the Pillar Two top-up taxation system. Country B has put in place a Pillar Two style Qualified UTPR. Country B proceeds to assess the jurisdictional ETR of Country A. Country B, too, arrives at the observation that Country A's ETR is 10%. The ETR in Country A, as mentioned, is 5 percentage points too low (10% instead of 15%). Country B subjects Sub2 OpCo to UTPR top-up tax. Let us assume for the sake of simplicity that the basis against which the top-up tax is assessed is $1,000 (i.e. excluding the SBIE allowance). Sub2 OpCo will potentially be subject to additional tax under the UTPR at an amount of $50 (5%*1,000=$50). The UTPR however is set at nil. The $50 top-up tax is allocated to Country X, considering that Country X's IIR top-up tax qualifies under the Pillar Two rules and considering that an IIR takes priority over Country B's UTPR under the Pillar Two ordering rules (IIR trumps UTPR).

? *Country X*. In Country X, the corporate tax base is nil, any proceeds from the shareholdings in Sub1 OpCo and Sub2 OpCo are exempt from taxation under the participation exemption regime in Country X's corporate tax system. The corporate tax due by ParentCo is nil. The headline corporate tax rate in Country X is 25%. For the sake of simplicity, let us assume that the GloBE-base in Country X is also nil, as any shareholding proceeds are exempt from the Globe-base under the Pillar Two rules equivalent to the participation exemption regime in the corporate tax system. No additional tax on the relevant Country X GloBE-income will be levied under the Pillar Two top-up taxation system, as the relevant GloBE income is nil. Country X has put in place a Pillar Two style Qualified IIR. Country X proceeds to assess the jurisdictional ETR of Country A. Country X, too, arrives at the observation that Country A's ETR is 10%. The ETR in Country A, as mentioned, is 5 percentage points too low (10% instead of 15%). Country X subjects ParentCo to IIR top-up tax. Let us assume for the sake of simplicity that the basis against which the top-up tax is assessed is $1,000 (i.e. excluding the SBIE allowance). ParentCo will be subject to additional tax under the IIR at an amount of $50 (5%*1,000=$50). The IIR takes priority over Country B's UTPR under the Pillar Two ordering rules. The IIR tax liability will be reduced with an amount of $50 to nil, considering that Country A's domestic top-up tax qualifies under the Pillar Two rules. In such cases the Pillar Two rules prescribe that any IIR liability is reduced with any QDMTT-liability. Pillar 2 prioritizes QDMTT top-up taxation over extraterritorial top-up taxation under the IIR or UTPR (QDMTT trumps IIR).

? *Effect*. Sub1 OpCo is subject to $50 Pillar Two style additional top-up taxation under Country A's QDMTT. Sub2 OpCo is subject to nil Pillar Two style top-up taxation under Country B's UTPR in consideration of Country X's qualifying IIR taking priority. ParentCo is subject to nil Pillar Two style top-up taxation under Country X's IIR in consideration of Country A's qualifying DMTT taking priority, leading to a reduction of Country X's IIR to nil. Notably, under the general Pillar Two framework Country A will also have to assess Country X and Country B under its domestic Pillar Two rules, while Country X will not only have to assess Country A but also Country B under its domestic Pillar Two rules, whereas Country B will not only have to assess Country A but also Country X under its domestic Pillar Two rules. As Countries B and X have above par ETRs (provided that no disparities exist in the interpretation of the Pillar Two rules by the respective countries involved), the assessments will not lead to the recognition of additional tax in the countries involved. For this reason the calculations are not taken-up in the current example. Note that the current example also excludes the operation of any applicable safe harbors. In December 2022 the OECD released the not to be further discussed Transitional Country-by-Country Reporting ('CbCR') Safe Harbour.[35] In July 2023 the OECD released a QDMTT Safe Harbour measure.[36] This measure is briefly discussed below.

Box 2. Disqualifying DMTT

Now let us introduce a subsidy and add it to the base case to explore potential implications.
The fact pattern is identical to that above, with the only difference that Country A now introduces a (tax) subsidy modeled as either a tax incentive, grant, subsidy (except perhaps as a QRTC). By channeling domestic top-up tax revenue back to Sub1 OpCo Country A accordingly seeks to rejoin the fiscal competitive race for investment. Sub1 OpCo receives a grant of $40. The corporate tax due by Sub1 OpCo is $100. The domestic top-up tax due by Sub1 OpCo is $50.
Let us assume that the subsidy provided triggers the disqualification of Country A's domestic top-up tax under the operation of the NBR in the Pillar Two rules in both Countries X and B. When it comes to the impact of the $40 grant on the jurisdictional ETR calculation and subsequent top-up tax implications abroad, the following candidate implications may be recognized:
1. The disqualified DMTT is not considered to constitute a Covered Tax for Pillar Two purposes. The grant is considered to constitute a negative Covered Tax. The grant is not considered to constitute GloBE-income. The ETR for Pillar Two purposes in Country A accordingly is 6% ((100-/-40)/1,000*100%=6%). The top-up taxation consequently due under the IIR (or UTPR) abroad would be $90 (9%*1,000=90).
2. The disqualified DMTT is not considered to constitute a Covered Tax. The grant is not considered to constitute a negative Covered Tax. The grant is considered to constitute GloBE-income. The ETR for Pillar Two purposes in Country A accordingly is 9.6% (100/(1,000+40)*100%=9.6%). The top-up taxation consequently due under the IIR (or UTPR) abroad would be $56.16 (5.4%*1,040=56.16).
3. The disqualified DMTT is considered to constitute a Covered Tax. The grant is considered to constitute a negative Covered Tax. The grant is not considered to constitute GloBE-income. The ETR for Pillar Two purposes in Country A accordingly is 11% (100+50-/-40)/1,000*100%=11%). The top-up taxation consequently due under the IIR (or UTPR) abroad would be $40 (4%*1,000=$40).
4. The disqualified DMTT is considered to constitute a Covered Tax. The grant is considered not to constitute a negative Covered Tax. The grant is considered to constitute GloBE-income. The ETR for Pillar Two purposes in Country A accordingly is 14.4% (100+50)/(1,000+40)*100%). The top-up taxation consequently due under the IIR (or UTPR) abroad would be $6.24 (0.6%*1,040=6.24).
Please note that if Country X were to operate any tax breaks to stimulate ParentCo to engage into setting-up investment activity in the country, the transitional UTPR Safe Harbour would disable Country A and Country B to proceed to top-up tax any subsequent Country X low-taxed investment returns – under the general Pillar Two ETR calculation standards that is – to the 15% minimum level. The reason for that would be that Country X has a 25% headline corporate tax rate in place, thereby meeting the 20% nominal tax rate test under the UTPR Safe Harbour mechanism.

4.2 A Wide Range of Candidate ETRs

The numerical example illustrates that Country A's failure to meet the NBR triggers top-up taxation in all candidate scenarios. The effects vary however and could be moderate, rather detrimental or even devastating, depending on the interpretation of the Pillar Two rules in this regard. As the assessment illustrates top-up taxation quantities would range from $90 (9%*1,000=90) in scenario 1, $56.16 (5.4%*1,040=56.16) in scenario 2, $40 (4%*1,000=$40) in scenario 3, to $6.24 (0.6%*1,040=6.24) in scenario 4. Obviously, scenario 1 would be the worst for both Country A and the multinational enterprise involved, while scenario 4 would perhaps be the best outcome for both Country A and the multinational enterprise concerned. Scenarios 1 and 2 would produce some excess taxation, while scenario 3 would neutralize – or perhaps paralyze depending on the eye of the beholder – Country A's subsidy aspirations, whereas scenario 4 would not, creating an effect similar to that of a QRTC.[37] Note that these calculations are based on the assumption of the absence of any further complicating disparities in Pillar Two rulebooks operations in the countries involved.

Which of the outcomes should be the one to adopt? And what to do for instance if countries were to mutually disagree on the interpretative route to follow? What, for instance, would happen if Country X in the current example were to embrace scenario 4 subjecting ParentCo to $6.24 IIR top-up tax, while Country B for instance would prefer moving towards scenario 1, seeking to subject Sub2 opCo to $90 UTPR top-up tax? Could such an interpretative mismatch for instance initiate a disqualification of Country X's IIR by Country B too? Could such a, say, secondary top-up tax disqualification ensue a triggering of additional top-up tax under the UTPR in Country B, on top that is of the top-up tax already levied by Country X? Could such a sequential disqualification of top-up taxes initiate a negation of Pillar Two ordering rules? What would happen if one jurisdiction would seek to impose its disparate interpretation of its Pillar Two rules on the other? Would such a toppling of top-up taxation responses put the systemic integrity of the Pillar Two system at risk? How to subsequently resolve any potentially ensuing disputes?

We would not know to be honest. Our honest answer is that the matter is not clear, at least, not on the basis of the Pillar Two Model Rules and the commentaries thereon, and not on the basis of the administrative guidance provided so far. The EU Directive on the implementation of Pillar Two in the European Union notably is silent on the matter as well. We only know that the July 2023 batch of OECD Administrative Guidance sets forth that tax credits that do not qualify as QRTCs or MTTCs are treated as reductions to Covered Taxes, and that refunds of Covered Taxes creditable against other Covered Tax liabilities are treated as reductions to Covered Taxes as well.[38] We know that the guidance now also says that tax credits that do not qualify as QRTCs or MTTCs but are nonetheless treated as income for financial accounting purposes rather than as tax reductions need to be subtracted in full from the income calculations for Pillar Two purposes.[39] We however do not know how such, by analogy, would translate into the operation of the NBR and any ensuing implications involving a disqualification of a country's top-up tax because of any benefits provided related thereto. We also would not know on what legal grounds such a top-up tax tidying-up exercise should be based.

Perhaps one may argue that for interpretative purposes one should resort to the underlying principles of 'providing a level playing field among all jurisdictions'.[40] We, however, then stumble on some difficulties in that regard, considering the recent developments in relation to the introduced UTPR safe harbor. The replacement of the detailed Pillar Two ETR calculation for a subject-to-a-statutory-20%-tax-rate-test in the UTPR context (regardless of whether such should be considered normatively good or bad) effectively interferes with the earlier noted efforts in the Pillar Two project towards establishing a global level playing field, at least for headquarters jurisdictions that is. Analytically, the UTPR Safe Harbour may hardly be considered a 'mechanism implemented and administered in a way that is consistent with the outcomes provided for under the GloBE Rules and the Commentary'. In view of this development, now which underlying principle should be called upon to proceed to disqualify those other countries that seek to find some room for maneuver as well to continue competing for investment via their fiscal systems? How to disqualify these countries when some similar objectives now are legitimized and enabled for headquarter jurisdictions to pursue regardless, under a top-up tax safe harbor mechanism specifically designed to cater for achieving that end? We would not be sure.

5 Way Forward?

5.1 No Governance Framework Available

Currently no governance framework has been readily developed or put into place that secures an orderly and coordinated approach of countries in their assessments of each others' Pillar Two top-up taxation rules and the certification thereof. No formal authority or body or procedure has been put into place to this end. Also tax treaties do not offer obvious protection,[41] nor do any of the dispute resolution mechanism frameworks in existing tax treaties or EU law instruments seem applicable. Various high-level alternatives have been floated in search of some enhanced coordination and cooperation and dispute settlement mechanisms, such as a peer group review process amongst others.[42] So far, however, it is still unclear whether and when such a mechanism will see the light of day and if so how such a mechanism would work, operate, and how it would be governed. Absent an umbrella rule coordination framework preventing country divergences it may be fair to anticipate that countries will embark upon their own paths. That may result in countries taking either stringent or extensive interpretations in assessing each other's Pillar Two implementation frameworks, and basing any thereupon decisions under their domestic Pillar Two laws to either or not proceed to collecting top-up tax. Any resulting de-synchronization of Pillar Two rules operation may initiate significant potentials for ensuing tax cascading, legal uncertainties, tax litigation (appeal processes, court proceedings), and controversy. As a corollary, such would also create uncertainties as to whether, and if so how precisely, to provision for any emerging top-up taxation risks in company financial statements.

It should be noted that in July 2023 the IF released a QDMTT Safe Harbour measure.[43] Similar to the UTPR Safe Harbour mentioned above, application of the QDMTT Safe Harbour measure also establishes nil top-up taxation for Pillar Two purposes for those jurisdictions meeting the standards set. Moreover, application of the QDMTT Safe Harbour eliminates the need for multinationals to undertake a second round of calculations of the jurisdictional ETR under the general Pillar Two rules, after completing the QDMTT calculation that is. The QDMTT Safe Harbour however does not provide some equivalent room for maneuver to countries as the UTPR Safe Harbour does in terms of giving some leeway to jurisdictions to continue competing for investment via the tax system. On the contrary. The QDMTT Safe Harbour applies a more stringent standard than the general Pillar Two rules. The QDMTT Safe Harbour requires the QDMTT in a country to follow and adhere to the same computations as required under the general Pillar Two Rules, i.e., including the NBR, except as specifically authorized by Administrative Guidance or the IF. Under the QDMTT Safe Harbour the relevant multinational enterprise involved will need to demonstrate that in addition to the existing QDMTT rules and guidance it meets (i) the QDMTT Accounting Standard; (ii) the Consistency Standard, and (iii) the Administration Standard. These standards amongst others allow countries to devise their ETR calculations under their QDMTT by reference to local financial accounting standards (potentially yielding different ETRs in comparison to ETR calculations under the general Pillar Two Rules which require the calculations to be based, in principle, on the accounting standards in place in the UPE jurisdiction). The assessment of whether a country's QDMTT qualifies for the QDMTT Safe Harbour will be subject to a yet to be devised country peer review process;[44] there too. This begs the question as to how extensive any such envisaged QDMTT Safe Harbour relief will effectively turn out when matters come down to it.

5.2 The Hurdle to Overcome

It may be fair to observe that a governance framework seems to be in need of being developed, and it may also be fair to say that the sooner such will be established the better it would be. The uncertainty, controversy, and tax cascading potentials of a non-coordinated approach towards the NBR all stress the need for some swift action, within the IF for instance in the context of the envisaged peer review framework. In this regard one may think of a subsidies framework providing countries a certain degree of room for maneuver, some safe harbors, a standardization of certified government support instruments for instance, in terms of the types of incentive or subsidy instruments involved, the amounts of monetary support that may be made available, bases for multilateral administrative coordination, the issuance of multilateral tax rulings perhaps and/or perhaps a mutual recognition of unilateral rulings, and perhaps even a forwarding of a range of available underlying policy objectives that may pursued, all in order to define what would be acceptable under the NBR and within what range. Such a framework as well as the governance of any decision-making, the discovery of findings, any evaluations in relation to any certifying proceedings would need to be legitimized, both politically and constitutionally, as extraterritorial top-up taxation effectively entails a fiscal intervention by one country in the economy of another country (that is notably also the reason why Pillar Two may potentially fall foul under the tax treaties). Country representation would constitute an aspect to be properly dealt with as well, and an effective dispute settlement mechanism embedded in the rule of law would need to be catered for. If put into place, such a review framework would guardrail any potential out-of-line behaviors of countries, and such would also streamline and coordinate the ranges of approaches taken by states, as well as the room for discretion, not only in relation to their domestic incentives but also in relation to the assessment of their peers' equivalents. Such would enhance the certainty for countries as to the framework within which countries in a post-Pillar Two era are enabled to establish their fiscal policies. Such would also enhance the certainty for taxpayers, multinational companies, as to the framework within which these are enabled to make use of government issued support of their investments, in a non-controversial way. Such would allow for a striking of a balance between the envisaged level playing field and the pursued instrumentalization of incentives as a fiscal policy tool.

Already a high-level overview of potential benchmark criteria immediately reveals the reasons, at least intuitively, of why such a framework is not there yet. All this would be about, as noted, striking a balance between the envisaged level playing field and the pursued instrumentalization of incentives as a fiscal policy tool. That may be rather hard to come by. What should be the substantive parameters for instance? Should we perhaps revisit pre-Pillar Two traditional tax governance dividing lines for this purpose, identifying harmful tax practices, whereby the NBR would be held to address only those tax measures involving a low-taxation of passive income, or paper profits, a ring-fencing of activity, a lack of transparency, et cetera? That would effectively transform the Pillar Two initiative into a post-BEPS reform addressing only those remaining BEPS issues, while re-enabling countries to continue instrumentalizing their tax systems to mutually compete – using traditional language – in a non-harmful way for real investment via tax credits and other tax incentives. From such a perspective, the relevance of the matter may perhaps also be placed in the context of investment support initiatives that have emerged in various regions and large and influential economies in the world (e.g, US, EU), and for instance also in the context of the conditions developed to base upon the UTPR Safe Harbour mechanism. Should we perhaps alternatively visit any approaches as devised in the EU for instance, under the EU State Aid framework, perhaps in consideration also of the newly operational EU Foreign Subsidies Regulation, as a tool that is to further shape or sharpen the NBR and its operation in the Pillar Two context? Such would further the pursued level playing field, however, at the cost of a trading-off on country autonomous fiscal competences. And there we are, back to where the current analysis started, with the biggest hurdle to overcome: nation state fiscal autonomy.

6 Closing comments

This article elaborates on the No Benefit Requirement, an underexposed element of Pillar Two. If a country were to observe that some other country's Pillar Two top-up tax rules disqualify as such, on the basis that this other country provides benefits to companies in relation to its top-up tax, the first-mentioned country would proceed to top-up taxing those companies on their foreign earnings itself: I'll tax if you don't. One might expect that such a far-reaching fiscal intervention by one sovereign nation in the economy of any of its sovereign peers would only be possible and legitimized on the basis of a principled clear-cut bright-line test, which is founded and legitimized in the rule of law and that is embedded in an institutional framework governed by international public law. That, however, is not the case – at all. Countries committed themselves politically to establishing a global level playing field in company taxation. Countries simultaneously seek to continue their fiscal competition for investment. One however cannot have both. As matters currently stand, the current state of affairs is a vague rule allowing for wide ranging disparate rule-interpretation and operation, having potentially devastating implications for both countries and taxpayers. That will not bring fairness to taxation, that will bring a mess. IF Members, please decide on the route to follow, strike a balance between competition and coordination and overcome political hurdles, walk the talk and bring the said fairness to the corporate tax world. And if the honest answer is that a global level playing field actually is not what we pursue, then the honest answer is that a global level playing field actually is not what we pursue. Then too is a fault confessed half redressed. We will see.

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[1] *See* https://www.reuters.com/markets/asia/no-handouts-big-firms-offset-global-tax-oecd-tells-vietnam-2023-06-07/. Last assessed on August 15, 2023. For some reading and analyses on incentives in relation to Pillar Two, see V. Chand, K. Romanovska, The impact of Pillar II on Corporate Tax Incentives and Incentives post Pillar II – The potential rise of Tax Credits and Subsidies, available on SSRN.

[2] *See* Article 10.1. Pillar Two Model Rules – Defined Terms, "Qualified Domestic Minimum Top-up Tax", "Qualified IIR", "Qualified UTPR": *"provided that such jurisdiction does not provide any benefits that are related to such rules"*. The Pillar Two Model Rules have been published in OECD (2021), *Tax Challenges Arising from the Digitalisation of the Economy – Global Anti-Base Erosion Model Rules (Pillar Two): Inclusive Framework on BEPS,* OECD Publishing, Paris (Pillar Two Model Rules).

[3] *See* OECD (2023), *Tax Challenges Arising from the Digitalisation of the Economy – Administrative Guidance on the Global Anti-Base Erosion Model Rules (Pillar Two), July 2023,* OECD/G20 Inclusive Framework on BEPS, OECD, Paris, Sec. 5.2 Transitional UTPR Safe Harbour, at 89 et seq.

[4] *Ibidem*: *"The UTPR Top-up Tax Amount calculated for the UPE Jurisdiction shall be deemed to be zero for each Fiscal Year during the Transition Period if the UPE Jurisdiction has a corporate income tax that applies at a rate of at least 20%."*

[5] See for some comparison, Maarten de Wilde, "On an animal farm and 'equality, however' according to the Pillar 2 Commentary", *Kluwer International Tax Blog*, 15 March 2022 (kluwertaxblog.com).

[6] *See* Administrative Guidance, *supra note* 6, at 89: *"Transition Period means the Fiscal Years which run no longer than 12 months that begin on or before 31 December 2025 and end before 31 December 2026."* Under the general Pillar Two rules countries UTPR will be introduced as per year-end 2024 while the other top-up taxes will be implemented per year-end 2023.

[7] For some background, see the OECD website: https://www.oecd.org/tax/beps/tax-challenges-arising-from-the-digitalisation-of-the-economy-global-anti-base-erosion-model-rules-pillar-two.htm.

[8] *See* Maarten de Wilde and Ciska Wisman, 'OECD Consultations on the Digital Economy: "Tax Base Reallocation" and "I'll Tax If You Don't"?', in Pasquale Pistone and Dennis Weber (Eds.), *Taxing the Digital Economy; The EU Proposals and Other Insights*, IBFD, Amsterdam, 2019, Ch. 1, at 3-23.

[9] *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 Publishing, Paris.

[10] *See* OECD (2022), *Tax Challenges Arising from the Digitalisation of the Economy – Commentary to the Global Anti-Base Erosion Model Rules (Pillar Two), First Edition: Inclusive Framework on BEPS*, OECD Publishing, Paris.

[11] *See* Council Directive (EU) 2022/2523 of 14 December 2022 on ensuring a global minimum level of taxation for multinational enterprise groups and large-scale domestic groups in the Union.

[12] See 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.

[13] *See* Administrative Guidance, *supra note* 6.

[14] OECD (2021), *Tax Challenges Arising from the Digitalisation of the Economy – Global Anti-Base Erosion Model Rules (Pillar Two): Inclusive Framework on BEPS*, OECD Publishing, Paris, at 7: *"to ensure a level playing field"*.

[15] *See* OECD (1998), Harmful Tax Competition: An Emerging Global Issue, OECD Publishing, Paris.

[16] *See* https://www.oecd.org/ctp/beps-2015-final-reports.htm.

[17] *See*, e.g., OECD (2017), *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris

[18] *See* for some reading and analysis Antti Laukkanen, Pasquale Pistone, Jan de Goede (Eds.), *Special Tax Zones in the Era of International Tax Coordination*, IBFD, Amsterdam, 2019.

[19] See Article 5.3. Pillar Two Model Rules – Substance-based Income Exclusion.

[20] For Pillar Two purposes, of relevance is the determination as to whether any specific incentive in a corporate tax system meets the definition under the Pillar Two Rules of Qualified Refundable

Tax Credit (‘QRTC), i.e., as income tax credits that meet the definition are treated differently for Pillar Two purposes from other income tax credits. A QRTC is defined under the Pillar Two rules (Article 10.1. Pillar Two Model Rules – Defined Terms) as a refundable tax credit paid as cash or available as cash equivalents within 4 years from the date when a constituent entity satisfies the conditions for receiving the credit. A QRTC is a government subsidy provided in cash to the extent that the taxpayer has insufficient tax liability to use the full amount of the credit (refundability). The refundability needs to be likely, that is, in substance rather than in mere form. This means that the refund mechanism should have practical significance to taxpayers (practical significance test), which requires an assessment of the credit regime as a whole, at macro-level, rather than on a taxpayer basis, at micro-level, and by reference to empirical and historical data regarding the whole tax credit regime. The cash payment needs to occur within 4 years from when the group entity involved satisfies the conditions for receiving the credit under the rules in place in the country providing the credit (timing). Creditable or refundable amounts under an imputation credit regime or tax refunds resulting from errors in the computation of tax liability are excluded from the definition (exclusions). A Non-QRTC is defined as a tax credit that is not a QRTC but that is refundable in whole or in part. See further footnote 39 below.

[21] *See* for some reading and analysis OECD (2022), *Tax Incentives and the Global Minimum Corporate Tax: Reconsidering Tax Incentives after the GloBE Rules*, OECD Publishing, Paris. On Marketable Transferable Tax Credits in relation to Pillar Two see Administrative Guidance, *supra note 6*, at 31 et seq.

[22] *See* Article 10.1. Pillar Two Model Rules, Defined Terms, “Qualified Domestic Minimum Top-up Tax”, at 61.

[23] Ibidem.

[24] *See* Administrative Guidance, *supra note* 6.

[25] *See Commentary, supra note 13*, at 213.

[26] *Ibidem*.

[27] *Ibidem*.

[28] *Ibidem*.

[29] *Ibidem*.

[30] *Ibidem*.

[31] *Ibidem*.

[32] *Ibidem*.

[33] *See* OECD (2022), *Tax Incentives and the Global Minimum Corporate Tax: Reconsidering Tax Incentives after the GloBE Rules*, OECD Publishing, Paris.Chapter 6 – Options for policymakers, at 47 et seq.

[34] *See* Stephanie Soong, 'OECD to Start Minimum Top-Up Tax Rule Peer Reviews in 2023', *Tax Notes International*, Vol. 9, 28 February 2023, quoting an OECD official.

[35] *See* OECD (2022), *Safe Harbours and Penalty Relief: Global Anti-Base Erosion Rules (Pillar Two)*, OECD/G20 Inclusive Framework on BEPS, OECD, Paris (Pillar Two Safe Harbour document). The Transitional CbCR Safe Harbour is a temporary measure and will apply to tax years starting on or before 31 December 2026, but not to tax years ending after 30 June 2028. A 'once out, always out' approach will apply, such that multinational groups will no longer be able to invoke the measure in a jurisdiction after a tax year in which they had not invoked the measure in that jurisdiction or in which they did not meet the stipulated conditions. In such scenarios, the Pillar Two system applies in its entirety. Application of the safe harbor measure during the said 3-year transitional period establishes nil top-up taxation for Pillar Two purposes for those jurisdictions where the relevant multinational demonstrates – using simplified calculations based on its qualifying CbCR and qualifying data from its financial statements – that it meets the (i) *de minimis* test; (ii) simplified ETR test, or (iii) routine profits test. Multinationals that pass any of these tests are not required to perform the detailed calculations of the Pillar Two effective tax rate as set out in the Pillar Two Model Rules. The tests involved under the safe harbor regime are in fact 'light' variants of their equivalents in the Pillar Two system, and accordingly provide some temporary administrative simplification and compliance relief for businesses and tax authorities.

[36] *See* OECD (2023), *Tax Challenges Arising from the Digitalisation of the Economy – Administrative Guidance on the Global Anti-Base Erosion Model Rules (Pillar Two), July 2023*, OECD/G20 Inclusive Framework on BEPS, OECD, Paris, Sec. 5.1 QDMTT Safe Harbour, at 77 et seq.

[37] QRTCs generally are accounted for as government grants and are treated for Pillar Two purposes as income in the computation of the Pillar Two ETR (i.e. by taking the QRTCs involved into account in the denominator of the ETR computation). In case the tax incentive involved does not qualify as a QRTC (i.e. 'non-QRTC'), the tax incentive is excluded from income but treated as a reduction in (covered) taxes in the period the tax incentive is claimed (i.e. by taking these non-QRTCs involved into account in the numerator of the ETR computation). See Articles 3.2.4, 4.1.2, 4.1.3 Pillar Two Model Rules. Effectively, this means that QRTCs have a relatively limited impact on the reduction of the Pillar Two ETR vis-a-vis non-qualifying tax credits, i.e. non-QRTCs, as the latter credits reduce tax (numerator ETR fraction) and not income (denominator ETR fraction). As a result, QRTCs result in relatively moderate amounts of potential top-up taxation due, under either a QDMTT in the country providing the tax credit involved or an IIR or UTPR in any other country in which the multinational group operates, in comparison to any other tax credit that is. This accordingly creates a strong incentive for countries that seek to compete for investment by delivering incentives via their tax systems to organize these in their company tax systems by means of a QRTC. For some reading and analysis on QRTCs and Pillar Two, see Peter R. Merrill, Karl Russo, Aaron Junge, Damien Boudreau, and Florian Holle, 'Where Credit Is Due: Treatment of Tax Credits Under Pillar 2', *Tax Notes International*, Vol. 9 20 March 2023.

[38] *See* Administrative Guidance, *supra note* 6, at 35.

[39] *Ibidem*.

[40] S*ee Commentary*, *supra note* 13, at 213

[41] The extraterritoriality of the top-up taxation mechanism renders the Pillar Two top-up tax system, and predominantly the UTPR, to potentially fall foul under the existing double taxation conventions. This matter is increasingly being signaled in both practice and literature and is also creating some legal uncertainty as to the feasibility for countries to effectuate any top-up taxation, and particularly those countries that do not allow for tax treaty overrides under their domestic constitutional systems. See for some reading and analysis, Maarten de Wilde, 'Why Pillar Two Top-Up Taxation Requires Tax Treaty Modification', *Kluwer International Tax Blog*, 12 January 2022 (kluwertaxblog.com).

[42] See e.g., OECD, Public consultation document Pillar Two – Tax Certainty for the GloBE Rules 20 December 2022 – 3 February 2023.

[43] *See* Administrative Guidance, *supra note 6*, Sec. 5.1 QDMTT Safe Harbour, at 77 et seq.

[44] *See* Administrative Guidance, supra note 6, at 88.

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