Where stands Pillar Two?

- **Background**

As a reminder, the OECD/G20 Inclusive Framework on BEPS brings together over 125 countries and jurisdictions that collaborate to implement measures from the BEPS Project.

On 8 October 2021, international tax reform took a further step forward thanks to a declaration by the members of the OECD's Inclusive Framework that wishes to implement a solution based on Pillar One and Pillar Two measures. These two pillars aim to reform international tax rules and ensure that multinational enterprises pay a fair share of taxes wherever they operate.

Pillar One aims to achieve a fairer distribution of profits and taxing rights between countries for large multinational enterprises (MNEs), which are the winners of globalization.

Pillar Two seeks to frame corporate income tax competition by introducing a global minimum tax that countries can apply to protect their tax base. Such measure does not end tax competition but seeks to limit it according to multilaterally agreed rules.

Following this latest breakthrough in the OECD/G20 tax reform project, the European Union, wishing to be among the first jurisdictions to implement this landmark global agreement, proposed on 22 December 2021, a directive guaranteeing a minimum effective tax rate for the global activities of large multinational groups.

The proposed directive allows an EU Member State in which the effective tax rate of an international group company is below 15% to remedy this under-taxation by levying an additional tax. In the system devised by the Inclusive Framework, such possibility is primarily given to the State of the parent company. The particularity of the directive proposal seemed thus to rely in giving the State of the subsidiary the possibility of levying this additional tax, but such a possibility is already provided for by the OECD's Inclusive framework.

The specificity of the proposed directive consists in the compulsory extension of the minimum taxation system to purely national groups. A parent company established in a Member State and having a subsidiary in the same State with an effective tax rate of less than 15% will thus have to pay an additional tax. The European Commission has argued that this identical treatment of purely domestic groups and groups with foreign subsidiaries and permanent establishments is necessary to respect the freedom of establishment.

The transposition date initially foreseen by the proposed directive was 31 December 2022 for application from 1 January 2023. However, the rule on under-taxed payments would only apply from 2024.

- **In mid-March, significant concessions had already been made**

During the ECOFIN meeting of 15 March 2022, it was agreed to postpone the deadline for transposition of the Directive to 31 December 2023. The new rules would apply to financial years beginning on or after 31 December 2023, with the exception of those concerning the undertaxed payment rule (UTPR) which would apply to financial years beginning on or after 31 December 2024. This is one year later than originally planned. These changes were supported by several Member States.

The compromise of the meeting of 15 March 2022 also envisages a mechanism that would allow Member States with no more than 10 ultimate parent entities falling within the scope of the directive located on their territory to opt for the application of the GloBe rules (OECD, income inclusion rule and undertaxed payment rule) only to financial years beginning on or after 1 January 2026 or 2028. This means an additional 3 or 5 years.

In practice, this would give companies additional time to put in place the procedures and mechanisms necessary to comply with these new obligations.

- **Debates in the European Parliament - 4 April 2022**

Debates in the European Parliament have highlighted the urgency of adopting the Minimum Tax Directive.

- **ECOFIN meeting - 5 April 2022**

On 5 April 2022, the ECOFIN Council met to adopt a general approach on the proposal for a directive implementing Pillar Two.

Twenty-six Member States were in favour of adoption, but Poland, which had welcomed the OECD's Inclusive framework, was against it. Poland, through its representative, believes "*that both pillars should be dealt with in a package. We must maintain our objective of full integration of these two pillars in order to meet the tax challenges arising from the digitalisation of our economies. We do not support a separate treatment of these two pillars within the European Union*".

Although Poland's reason is relevant because in the OECD’s draft Pillar One and Pillar Two are closely linked, the Polish veto of the draft directive is seen in Brussels as a means of pressure to release the 36 billion in grants and loans earmarked for Poland under the European recovery plan. These funds have been blocked by the Commission since last year due to Warsaw's failure to ensure the independence of its judiciary.

Prior to this meeting, Member States with no more than 10 ultimate parent entities (UPEs) falling within the scope of this directive on their territory were given an additional 3 or 5 years. At the ECOFIN Council of 5 April 2022, it was decided that an additional period would be granted to Member States with no more than 12 UPEs on their territory and the transitional period would be set at 6 years.

However, the OECD text, which was transcribed by the European Commission, raised technical problems, as the French Minister pointed out, such as the link between Pillar One and Pillar Two.

At the ECOFIN meetings of 3 May and 24 May 2022, the directive was not discussed, it was removed from the agenda for lack of progress.
The European Commission approved Poland's €35.4 billion recovery plan on 1 June 2022, allowing Poland to lift its veto at the ECOFIN meeting on 17 June.

But at that meeting it was Hungary, the only member state whose recovery plan was not approved, that vetoed the plan.

Today, the European Commission's directive has not yet been adopted, as decisions on tax matters must be taken unanimously. Bruno Le Maire hopes that the directive can still be adopted before the end of the EU Presidency on 30 June. He also spoke in favor of giving up the unanimity rule in tax matters and switching to qualified majority voting.

It should be noted that outside the European Union, Pillar Two has not progressed, and the draft multilateral instrument (MLI) will not be published in July as initially planned.

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