



# TaxNewsFlash

Canada

## Multinationals — Act Now to Meet Pillar Two Obligations

August 16, 2023

No. 2023-31

Large multinationals should prepare now for upcoming tax obligations and financial statement disclosures with the release of Canada's draft legislation to implement global minimum tax rules. This highly anticipated legislation, which was released on August 4, 2023, is based on Pillar Two of the Organization for Economic Cooperation and Development's (OECD) two-pillar solution to address the tax challenges from digitalization of the economy. Finance's complex draft legislation, which is intended to ensure that multinationals (MNEs) pay a minimum 15% rate of tax in each jurisdiction, will apply to fiscal years beginning on or after December 31, 2023. Note that these rules affect not only MNEs headquartered in Canada, but also Canadian entities of foreign-based MNEs, as the rules contain a domestic minimum top-up tax.

With the release of these proposals under the new *Global Minimum Tax Act*, Canada joins many other jurisdictions that are currently working to implement Pillar Two in their domestic tax law to be effective as early as 2024. Although these rules are subject to public consultation and are not yet enacted, MNEs should still act quickly to determine how they are affected by these rules. In particular, affected MNEs should consider the impact on their financial statements, review their eligibility for any simplifying measures including the transitional country-by-country report (CbCR) safe harbours, and, where no safe harbours apply, perform detailed calculations to assess potential exposure to additional taxes. Additionally, MNEs should ensure appropriate systems are in place for the significant data collection process required to meet their upcoming filing and payment obligations. KPMG has developed global technology modeling, data gap analysis, and compliance tools to help MNEs efficiently analyze their structures and prepare for the new Pillar Two regime.

## Background

Generally, the OECD/G20 Inclusive Framework contemplates tax proposals under two specific “pillars”. Pillar Two focuses on ensuring large MNEs pay a minimum rate of tax. As part of this pillar, the OECD/G20 Inclusive Framework released the “global anti-base erosion” (GloBE) model rules in 2021 that would apply to MNEs with consolidated revenue equal to or greater than €750 million in at least two of the last four years. Since the release of the GloBE model rules, the OECD/G20 Inclusive Framework has also released additional guidance and launched several public consultations on various aspects of the rules and their implementation.

To enact the Pillar Two rules in Canada, Finance released proposed legislation for the new *Global Minimum Tax Act* (GMTA) on August 4, 2023. Canada’s approach to implementing Pillar Two generally aligns with the OECD’s approach and includes an Income Inclusion Rule (IIR) and a domestic top-up tax that are intended to apply to fiscal years of a qualifying MNE group that begin on or after December 31, 2023, which is consistent with most other countries. Although Finance’s draft legislation does not include the Undertaxed Profits Rule (UTPR), there is a placeholder for these rules included in the GMTA. Finance previously noted that the UTPR rules are intended to apply for fiscal years of MNEs that begin on or after December 31, 2024 (i.e., one year later than the IIR and the domestic top-up tax). Note that, according to the draft legislation, the GMTA should generally be interpreted consistently with the OECD’s GloBE model rules, commentary and related administrative guidance, which the OECD may publish from time to time. Finance is accepting comments on these rules until September 29, 2023.

For details of the OECD’s releases on Pillar Two, see *TaxNewsFlash-Canada* 2023-28, “[OECD Provides Pillar One and Pillar Two Update](#)”, *TaxNewsFlash-Canada* 2023-05, “[OECD Offers More Guidance On Pillar Two Tax Rules](#)”, *TaxNewsFlash-Canada* 2022-56, “[OECD Asks for More Feedback on Pillar One and Two Specifics](#)”, *TaxNewsFlash-Canada* 2022-12, “[OECD Offers Guidance on Global Minimum Tax Rules](#)” and *TaxNewsFlash-Canada* 2021-63, “[OECD Releases Model Global Minimum Tax Rules](#)”.

## Which MNE groups are affected?

Canada’s Pillar Two rules will affect MNE groups that report revenue equal to or greater than €750 million (pro-rated for short fiscal years) in at least two of the four immediately preceding fiscal years, as reported in the consolidated financial statements of the MNE group’s ultimate parent entity (UPE). To be considered an MNE group, a group must have at least one entity or permanent establishment that is not located in the jurisdiction in which the UPE of the group is located.

The following entities are generally excluded under these rules:

- Governmental entities

- International organizations
- Non-profit organizations
- Pension funds
- Real estate investment vehicles or investment funds that are ultimate parent entities.

In addition, an entity may be excluded from these rules if it is owned by one or more of these entities (other than a pension fund that is a pension services entity) and it meets certain ownership and activity or financial accounting income tests.

### **New tax obligations**

Under these rules, affected MNE groups will be required to file a GloBE Information Return and generally make any required payments within 15 months after the last day of the fiscal year. As a result, most affected MNEs will not have to file under these rules until 2026. Under the proposed Canadian rules, the filing obligation for a fiscal year must generally be made with the Minister of National Revenue by the Canadian UPE of the MNE group, the designated filing entity of the MNE group that is located in Canada, or each constituent entity of the MNE group that is located in Canada, depending on the circumstances.

Note that, as a transitional measure, in the first fiscal year that MNE groups are subject to these rules, they are allowed to meet their filing and payment obligations under these rules within 18 months after the last day of the fiscal year.

### **Penalties**

MNE groups that do not comply with these rules may be subject to significant penalties. In particular, where an MNE group fails to file a GloBE Information Return as required, each constituent entity of the MNE that is located in Canada is jointly and severally liable to a penalty equal to \$25,000 per month (up to a maximum of 40 months). This penalty may also apply where an MNE group fails to notify the CRA that the GloBE Information Return will be filed by a qualifying foreign filing entity by the due date for the fiscal year. The proposals also include additional late-filing penalties equal to 5% of amount of unpaid tax at the time the return was required to be filed plus 1% of that tax for each additional month (up to 12 months) the return is late, increased in certain cases of repeated failure to file.

The proposals provide some penalty relief in certain cases for fiscal years beginning before January 1, 2027 and ending before July 1, 2028. To be eligible, the entity must have used reasonable measures to ensure the correct application of the GloBE model rules in completing the GloBE Information Return.

## Prepare now for upcoming obligations

Now that Finance has released its Pillar Two proposals, MNEs should take important steps to prepare to meet new obligations outlined in these rules.

### *Financial reporting disclosures*

With the recent amendments to IAS 12, affected MNEs should start to consider the quantitative and qualitative information that may need to be disclosed in the consolidated financial statements or separate financial statements of each group, especially those jurisdictions within the group that have already enacted or substantively enacted Pillar Two legislation. In determining which disclosures to provide, affected MNEs should begin to collect the appropriate information and assess their potential exposure under the GloBE rules. This determination includes an analysis of both the consolidated financial statements of the UPE, and the separate financial statements of each group entity.

### *Assess availability of transitional CbCR Safe Harbours*

MNE groups should also act fast to determine whether they qualify for the transitional safe harbour rules in each jurisdiction in which they operate. These jurisdictional safe harbours allow taxpayers to simplify certain calculations and to not be subject to GloBE top-up taxes for the first three years that the rules apply (i.e., for fiscal years beginning before January 1, 2027 and ending before July 1, 2028). To qualify for the safe harbours, MNE groups must ensure their CbCR is prepared in accordance with the OECD guidelines using qualified financial statements. Where their CbCR meets these requirements, MNE groups will be entitled to use, on a jurisdiction-by-jurisdiction basis, the simplified tests available under these rules (i.e., a de minimis test, a simplified effective tax rate (ETR) test or a routine profits test). For jurisdictions where the CbCR transitional safe harbours do not apply, a detailed computation and assessment of the potential tax exposure under the GloBE rules should be undertaken.

### *Assess any potential data gaps*

Meeting these new Pillar Two obligations will require MNE groups to collect and file a significant amount of information, particularly for large MNEs with a global footprint and a large number of constituent entities. Affected MNE groups should ensure that they have the appropriate systems in place now to capture the substantial information that will be required to be reported in the GloBE Information Return and calculate any taxes owing including under the domestic minimum top-up tax. The OECD's release of the standard template for the GloBE Information Return comprises 28 pages and potentially hundreds of data points required under the GloBE rules, many of which must be reported on a jurisdiction-by-jurisdiction or constituent entity-by-constituent entity basis. Affected entities should be prepared to address the potential systems issues in collating this data and work quickly to identify and resolve data gaps with the necessary solutions and automation.

## We can help

Your KPMG adviser can help you assess the effect of Pillar Two proposals on your business, including preparation to meet the transitional CbCR safe harbour requirements, which can simplify the required calculations in the first three years and identifying the information needed to compute the Pillar Two tax liability.

### *Enabled by technology*

In addition, KPMG's cross-functional team can use internally developed global technology tools to help review an MNE's group structure and perform a detailed assessment to help determine potential GloBE tax liabilities, identify potential elections and help develop a more comprehensive plan for how to manage these complex obligations going forward.

In particular, we can use these tools to help MNEs:

- Perform robust Pillar Two modeling to highlight potential outcomes under various scenarios
- Review the group structure to understand how the rules may apply
- Provide data and systems support to identify and produce required information in a standard and adaptable form
- Enable scenario planning to assist affected MNEs manage the effects of Pillar Two efficiently
- Assist with restructuring such as legal entity simplification, as required
- Provide a coordinated approach to address systems and data related issues, including planning based on certain accounting treatments.

For more information, contact your KPMG adviser, or one of the following:

Penny Woolford  
National Leader International Corporate Tax  
T: 416-777-8906  
E: [pennywoolford@kpmg.ca](mailto:pennywoolford@kpmg.ca)

Sharon Szeto  
GTA International Corporate Tax  
T: 416-777-3231  
E: [sszeto@kpmg.ca](mailto:sszeto@kpmg.ca)

Brian Ernewein  
National Tax  
T: 416-228-6575  
E: [bernewein@kpmg.ca](mailto:bernewein@kpmg.ca)

Julie Bouthillier  
Montreal International Corporate Tax  
T: 514-840-2114  
E: [jbouthillier@kpmg.ca](mailto:jbouthillier@kpmg.ca)

David Francescucci  
National Leader Transformative Tax Advisory  
and Value Chain Management  
T: 514-840-2395  
E: [dfrancescucci@kpmg.ca](mailto:dfrancescucci@kpmg.ca)

Susie Cooke  
National Leader Tax Transformation  
T: 416-468-7327  
E: [susiecooke@kpmg.ca](mailto:susiecooke@kpmg.ca)

Demet Tepe  
National Leader Transfer Pricing  
T: 514-840-5767  
E: [dtepe@kpmg.ca](mailto:dtepe@kpmg.ca)

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