# Inclusive Framework BEPS Agreement

**Update on Pillar One and Pillar Two of BEPS 2.0**

Policy Perspectives Update – the Hong Kong SAR

# Potential deferred implementation of BEPS Pillar One and Pillar Two – Updates from the OECD and the EU

The OECD/G20 Inclusive Framework on BEPS (IF) has been working on the Pillar One and Pillar Two proposals of BEPS 2.0 in parallel. While the detailed Model Rules and Commentary of the GloBE Rules under Pillar Two have been published by the OECD, the work on Pillar One is progressing at a slower pace than originally proposed by the OECD. The OECD recently indicated that the implementation of Pillar One would likely be deferred until 2024 at the earliest. On the other hand, the European Union (EU) has proposed to defer the implementation of Pillar Two in the EU until 31 December 2023 in general and up to 31 December 2029 in certain cases.

## Update on Pillar One and Pillar Two implementation

### Status of Pillar One – Update from the OECD

Pillar One concerns the reallocation of taxing rights over a portion of the profits of the largest and most profitable MNE groups to the market jurisdictions. The OECD originally aimed to introduce Pillar One via a Multilateral Convention (MLC) that was scheduled to be available for consultation in the summer of 2022, followed by implementation of Pillar One in 2023.

However, the OECD Secretary-General indicated at the World Economic Forum held in Switzerland on 24 May 2022 that the implementation of Pillar One would likely be deferred until 2024 at the earliest. The OECD now aims to reach an agreement on the key elements of Pillar One at the G20 Finance Ministers' meeting in July this year, followed by a draft MLC being finalised by the end of 2022.

It remains to be seen if this has any impact on the Digital Services Tax (DST) stand still and roll back agreed by the IF members in the October 2021 Statement, especially given a number of jurisdictions (e.g. India, Denmark, Canada, New Zealand) have said they may push ahead with DST if there were further delays in Pillar One implementation.

### Status of Pillar Two – Update from the EU

Pillar Two seeks to introduce a global minimum tax of 15% applicable to MNE groups with annual consolidated revenue of EUR750 million or more. Based on the OECD's timeline, the Income Inclusion Rule (IIR) would be effective in 2023 whereas the Undertaxed Payment Rule (UTPR) would be effective in 2024.

On 22 December 2021, the EU issued a proposed Minimum Tax Directive to incorporate the Pillar Two rules into the EU law. The Pillar Two rules in the EU generally model the GloBE Model Rules issued by the OECD in December last year, but with a wider scope that includes large-scale domestic groups as well (with specific transition rules for the first five years in which these groups come within the scope of the Directive). However, the EU Member States did not reach a unanimous agreement on the Directive and also a Revised Proposal on the Directive subsequently issued on 12 March 2022.

The EU then issued a revised compromise text for the Minimum Tax Directive on 28 March 2022, which proposed the following deferral on the global minimum tax implementation timeline:

- the IIR to apply for fiscal years beginning on or after **31 December 2023**; and
- an option for EU Member States to defer the application of the IIR and the UTPR up to **31 December 2029**, if **no more than 12** Ultimate Parent Entities of in-scope MNE groups are located in those EU Member States.

The EU Member States again failed to reach a unanimous agreement on the revised compromise text in the meeting held on 5 April 2022 due to concerns expressed by Poland in respect of the missing legal binding linkage on the implementation of both Pillar One and Pillar Two. The EU now aims to reach an agreement on the Minimum Tax Directive in the next meeting scheduled on 17 June 2022.

## KPMG observations

The likely deferral of Pillar One implementation does not necessarily mean the implementation of Pillar Two will be delayed as well. The OECD Secretary-General noted that it is now up to individual jurisdictions to implement the Pillar Two Model Rules into their legislation. Even with the proposed deferred timeline of Pillar Two implementation in the EU, some countries like Australia, Canada, Japan and the UK are understood to have an interest in continued adherence to the 2023 implementation timeline of Pillar Two. That said, the final implementation timetables and effective dates of the Pillar Two domestic legislation of the adopting jurisdictions remain to be seen.

As for the Hong Kong SAR (Hong Kong), the government announced in the 2022/23 Budget delivered in February this year that it plans to submit a legislative proposal to the Legislative Council in the second half of this year to implement the global minimum tax in accordance with the international consensus. The government will also consider introducing a domestic minimum top-up tax for MNE groups that fall within the scope of Pillar Two from year of assessment 2024/25. We trust in coming to the final decision on the effective dates of the global minimum tax and domestic minimum tax in Hong Kong, the government will consult the stakeholders, monitor the ongoing global developments in this area and take into account the likely Pillar Two implementation timelines in other jurisdictions.

Although there are still some uncertainties as to the implementation timetables of Pillar One and Pillar Two in both Hong Kong and other jurisdictions, in-scope MNE groups with business operations in Hong Kong should start preparing for the future changes to the Hong Kong tax system resulting from the BEPS 2.0 project and closely monitor the developments in this area. Hong Kong businesses with offshore claims on passive income such as dividends, interest and royalties also need to get prepared for the upcoming changes to the offshore regime for passive income in Hong Kong as Hong Kong will need to effect such changes by the end of this year to get off from the EU grey list for tax purposes.

# Contacts

## Global Tax Policy Leadership Group

**David Linke**
**Global Head of Tax & Legal Services**
**E:** David.Linke@kpmg.co.uk

**Grant Wardell-Johnson**
**Global Tax Policy Leader and Chair**
**E**: Grant.WardellJohnson@kpmg.co.uk

**Manal Corwin**
**Americas Regional Tax Policy Leader**
**E**: mcorwin@kpmg.com

**Vinod Kalloe**
**EMA Regional Tax Policy Leader**
**E**: kalloe.vinod@kpmg.com

**Conrad Turley**
**Asia Pacific Regional Tax Policy Leader**
**E**: conrad.turley@kpmg.com

**Chris Morgan**
**Responsible Tax Project Leader**
**E**: christopher.morgan@kpmg.co.uk

## Regional contacts

**John Timpany**
**Head of Tax, Hong Kong SAR**
**E**: john.timpany@kpmg.com

**Ivor Morris**
**Hong Kong SAR BEPS 2.0 Project Leader**
**E**: ivor.morris@kpmg.com

**Anita Tsang**
**Director, Tax Policy and Knowledge Management**
**E**: anita.tsang@kpmg.com

**kpmg.com/cn/socialmedia**