KPMG

# Navigating BEPS 2.0

## Key considerations for Chief Financial Officers (CFO)

### As your tax department grapples with BEPS, what should you know as a CFO?

As of today, 137 out of 141 member jurisdictions of the OECD/G20 Inclusive Framework (IF) on base erosion and profit shifting (BEPS) — representing more than 90 percent of global GDP — have now signed up to the BEPS 2.0 initiative. These 137 jurisdictions have approved an eight-page statement released on 8 October 2021, by the IF, finalizing key aspects of a two-pillar framework for reforming the international tax system, and several update releases have been issued since that time. Pillar One deals with the reallocation of certain profits from the most profitable multinational enterprises to market jurisdictions, and Pillar Two deals with a global minimum tax.

Together, when implemented, the two pillars would reflect one of the most significant reforms to the international tax system in over 100 years. The political agreement reached allows for jurisdictions to implement the global minimum tax with a start date of 2023, however it is generally thought that jurisdictions would not be prepared to implement the global minimum tax until 2024. Even with a potential start date of 2024, there is a limited period of time to prepare for the changes given the complexity of the rules and financial accounting and tax data needed. Known colloquially as BEPS 2.0, this package follows on from the OECD's 2015 BEPS program of international tax reform to deal with profit shifting, cross border tax arbitrage and tax transparency.

Many authorities believed that the BEPS 1.0 program did not adequately address the challenges of the digitalization of the economy and started to impose unilateral tax measures to deal with the issue. The purpose of the BEPS 2.0 project is to move towards a consensus position to help avoid misaligned unilateral efforts and double taxation. In addition, through the global minimum tax rules, it also seeks to address some of the perceived gaps in the way BEPS 1.0 deals with base erosion and stop the "race to the bottom" on company tax rate competition globally.

## Pillar Two checklist for Chief Financial Officers

**01** Determine which entities in the group structure are in-scope of the rules

**02** Perform impact assessment to determine whether a top up tax obligation will arise and which elections to make

**03** Manage internal and external stakeholders, including market disclosure obligations

**04** Assess resource needs to determine impact and ongoing compliance needs and set up a project team

**05** Assess new complex data needs and any systems changes needed for reporting

**06** Review governance and controls to help manage the risks associated with complex rules

**07** Determine if material financial statement impacts and disclosures are needed

**08** Review restructuring, supply chain, IP location, financing (including transition rules that may need to be monitored now)

**09** Monitor country reactions and participate in local policy/guidance development

## How KPMG professionals can help

- **Impact assessment and ongoing compliance**

  KPMG firms can help organizations understand appropriate responses to BEPS 2.0, including structuring considerations, leveraging bespoke technology tools and identify any data or related systems changes needed.

- **Accounting and assurance support**

  KPMG firms can help organizations navigate the significant accounting interactions with the Pillar Two rules in terms of calculating effective tax rates and the flow on accounting implications of any top up tax.

- **Legal entity simplification**

  KPMG firms can help organizations with restructuring to potentially simplify reporting, provide cost savings and help reduce tax risk for the corporate group, if the group structure and value chain are no longer appropriate.

- **Communication with stakeholders**

  KPMG firms can support organizations in establishing expected BEPS 2.0 impacts and assist with engaging C-suite/audit committees. Other tax and legal support including international and transfer pricing issues, DST taxes as well as IP and R&D considerations can all be provided.

# As CFO, what should you consider?

The Pillar Two "top up tax" calculation initially keys off financial accounts, but there are numerous adjustments that may be required. There are also elections available that may require a more granular level of breakdown and tracking than required for financial statements. The accounting impact and treatment of any "top up tax" payable should also be considered. More broadly, both the Pillar One and Pillar Two rules are complicated and the organization may need additional resources or system changes for future compliance. While immediately affecting Heads of Tax, the OECD's BEPS developments, including the Pillar Two "top up tax" will likely have significant impact on your finance function. Considerations for your CFO are included below.

| | **Pillar One —** Reallocation of taxing rights to market jurisdictions | **Pillar Two —** Global minimum tax |
|---|---|---|
| **What is it?** | Pillar One seeks to reallocate taxing rights for 25 percent of residual profits to market/end-user jurisdictions, for over 100 multinational groups globally (global revenue of EUR 20bn or more is required). This threshold may drop to EUR 10bn by 2030. | Pillar Two rules subject thousands of multinational groups around the world to a global minimum tax of 15 percent (groups with global revenue of EUR 750m or more are in scope). |
| **Why does it matter?** | The main Pillar One rules (reallocation of taxing rights) are relevant only to a limited number of multinationals around the world. However, there are also transfer pricing changes expected to apply to all multinational groups, which would set a globally agreed, standardized arm's length remuneration return for certain routine market/distribution activities in a market/end-user country. | Large multinational groups will now be subject to a minimum tax rate of 15 percent in the jurisdictions in which they operate. This means tax incentives claimed/low tax income in offshore locations and certain exempt income may no longer be of benefit to the group from 2023. Even if there is no "top up tax" payable for the group, there is still a significant compliance burden expected to demonstrate that all jurisdictional effective tax rates (as calculated under complicated rules with multiple data sources needed) are at 15 percent or above. These changes are attracting media attention, and potentially require significant changes to meet new compliance obligations, so organizations have to be ready to respond on the impact. |
| **Who does if effect?** | Multinational groups with revenue of EUR 20bn or more and profitability above 10 percent (measured as profit before tax divided by revenue). Over 100 groups globally are likely in scope. This threshold may drop to EUR 10bn by 2030. There are carve outs for financial services and extractive industries. | Multinational groups with annual consolidated revenues of EUR 750m or more in two of the last four years, but jurisdictions may choose to apply a lower threshold. |
| **What is required?** | For in-scope entities, excess profit above 10 percent is considered to be residual profit. Of this residual profit, 25 percent will be reallocated and taxed in those market/end-user jurisdictions (even where the group does not currently have any taxable presence). The allocation is expected to be based on certain nexus and formulae, with de-minimis carve outs for smaller operations. | Parent companies headquartered in jurisdictions adopting the rules will typically bear the obligation to calculate and pay any "top up tax" for offshore jurisdictions with a tax rate below 15 percent. For foreign owned inbound groups in participating jurisdictions, there may be "top up tax" obligations where the foreign parent jurisdiction does not apply the rules or where specified intra-group payments are taxed at a rate below the minimum. Some relief is given for low taxed entities with "substance" (based on tangible assets and payroll). |
| **When does it take effect?** | The OECD recently indicated a 2024 start date for the reallocation of taxing rights part of the measures once a critical number of jurisdictions are able to ratify the Pillar One Multilateral Convention. The Pillar One rules will require a certain number of jurisdictions to sign up to a Multilateral Convention. Removal of unilateral Digital Services Taxes are dependent on this. The transfer pricing changes are expected to be released at the end of 2022, but are likely to have a later start date. | While jurisdictions may implement the Pillar Two rules for 2023, it is generally thought that most jurisdictions would implement for 2024. The draft EU Directive and the proposed legislation from the UK and Korea would introduce Pillar Two from 2024.<br>Importantly, there are several factors that could impact this timeline and the course of implementation more generally, including (i) the impact of the Inflation Reduction Act, which did not bring the US into conformity with Pillar Two; and, as a result, could reduce other jurisdictions' willingness to proceed; (ii) ongoing leadership changes in key jurisdictions, including Italy and the UK, which could affect the consensus; and (iii) a rapidly evolving global economic landscape. |

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