# KPMG report: New administrative guidance on Pillar Two rules, initial observations and analysis

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# Overview

On December 18, 2023, the Inclusive Framework (IF) released its third tranche of Administrative Guidance on the Global Anti-Base Erosion ("GloBE") Model Rules (December AG). The guidance is principally focused on the application of the Transitional Country-by-Country Reporting (CbCR) Safe Harbor.

The Transitional CbCR Safe Harbor was introduced in guidance released in December 2022, and enables a Multinational Enterprise (MNE) Group to avoid both completing a full GloBE computation and paying a top-up tax for jurisdictions when they are eligible for one of three safe harbor tests: (1) de minimis; (2) simplified effective tax rate (ETR); and (3) routine profits. A KPMG report on this guidance is available here.

The initial guidance on the application of the Transitional CbCR Safe Harbor, *Safe Harbors and Penalty Relief: Global Anti-Base Erosion Rules (Pillar Two)*, included some key requirements MNE Groups must meet in order to be entitled to rely on the Transitional CbCR Safe Harbor. Most notably, there was a requirement for MNE Groups to prepare a Qualified CbC Report based on Qualified Financial Statements (QFS), essentially the accounts used to prepare the Consolidated Financial Statements (CFSs) of the Ultimate Parent Entity (UPE) or local statutory accounts. The initial guidance was relatively brief, and the December AG provides further guidance on how the safe harbors apply.

The December AG has six sections. Sections 1-2 focus on the Transitional CbCR Safe Harbor, while Sections 3-6 focus on various other aspects of the GloBE Rules.

1. **Purchase price accounting adjustments in QFSs** clarifies when purchase pricing accounting adjustments do and do not need to be excluded from a MNE Group's Qualified CbC Report.

2. **Further Guidance on the Transitional CbCR Safe Harbor** addresses a variety of technical issues, including more details on the definition of QFSs, the computation of the Simplified ETR and routine profits test, including in circumstances when an MNE Group is not required to file a CBC Report, and introduces new rules to counteract concerns about hybrid arbitrage arrangements.

3. **Administrative Guidance on application of GloBE Rules** provides more clarity on the definition of revenue for the purpose of the €750m scope threshold, and the treatment of mismatches between the fiscal year of the UPE and Constituent Entities (CEs) and between the fiscal and tax years of CEs.

4. **Further Administrative Guidance on the allocation of Blended Controlled Foreign Company (CFC) Taxes** addresses the application of the temporary allocation rules in various scenarios when a MNE Group is not required to compute the jurisdictional ETR under the full GloBE rules in respect of jurisdictions that are eligible for the Transitional CbCR Safe Harbor under the simplified ETR test.

5. **Transitional Filing Deadlines for MNE Groups with Short Reporting Fiscal Years** provides that groups with short fiscal years will not be required to file a Global Information Return (GIR) until June 30, 2026.

6. **Simplified Calculation Safe Harbor for Non-Material CEs (NMCEs)** provides a safe harbor (similar to the Transitional CbCR Safe Harbor) for NMCEs.

Like the first and second tranches released in February ("February AG") and July 2023 ("July AG"), this guidance is intended to be incorporated in a revised version of the Commentary to the GloBE Model Rules and is intended to provide a consistent application of the rules across jurisdictions. KPMG reports on the February and July AG are available here and here.

## How should businesses respond?

The December AG provides greater clarity on how the IF intend the Transitional CbCR Safe Harbor to apply. Businesses that are seeking to rely on this safe harbor to minimize their Pillar Two compliance need to review their CbCR preparation process to provide that their CbC Report will meet the "Qualified" standard.

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Other issues addressed in the guidance, such as the definition of revenue or allocation of blended CFC taxes (i.e., Global Intangible Low-Taxed Income (GILTI)), can also materially impact the tax implications of Pillar Two for some MNE Groups.

MNE Groups need to review this guidance and determine whether it impacts the disclosures they expect to make in their financial statements from the first quarter of 2024.

The remainder of this document provides a more detailed summary of the December AG.

# Purchase price accounting adjustments in QFSs

In most circumstances, Article 3.1.2 of the GloBE Model Rules requires a MNE Group to remove the effect of purchase price accounting (PPA) adjustments from the entity-level accounts that are used to compute GloBE income.

The initial safe harbor guidance provided three definitions of QFS, including "the accounts used to prepare the Consolidated Financial Statements of the UPE (to mirror the requirement under Article 3.1.2)." This created uncertainty whether MNE Groups were required to remove PPA adjustments from the entity-level accounts they use to prepare their Qualified CbC Report.

The December AG removes the reference to Article 3.1.2 from the definition of QFS and clarifies that there is no general requirement to remove PPA adjustments reflected in the accounts used to prepare the CFSs of the UPE or the separate financial statements of each CE prepared in accordance with an Acceptable Financial Accounting Standard or Authorised Financial Accounting Standard.

However, the December AG requires PPA adjustments to be removed in two scenarios. First, PPA adjustments must be removed if a MNE Group has submitted a CbC Report for a fiscal year (FY) beginning after December 31, 2022 that was based on financial statements without PPA adjustments ("the consistent reporting condition"). This condition is intended to prevent a MNE Group that has submitted a CbC Report that does not include PPA adjustments from amending this approach and including such adjustments in subsequent CbC Reports. Second, if the consistent reporting condition does not require removing all PPA adjustments, a reduction in a CE's income attributable to the impairment of goodwill related to transactions entered into after November 30, 2021 must nevertheless be added back for the routine profits test (in all cases) and for the simplified ETR test (unless there was a corresponding change in deferred taxes) (the "goodwill impairment adjustment").

# Further guidance on the Transitional CbCR Safe Harbor

The additional guidance on the Transitional CbCR Safe Harbor has two parts. The opening sections provide clarifications on how various aspects of the Transitional CbCR Safe Harbor apply. The final section introduces new anti-avoidance provisions that are intended to protect against the potential for hybrid arbitrage arrangements to undermine the intended effect of the safe harbor.

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# Clarifications about the application of the Transitional CbCR Safe Harbor

The December AG addresses a number of issues around the application of the Transitional CbCR Safe Harbor that had previously given rise to uncertainty.

## Tested Jurisdictions

- When an MNE Group has both CEs and a Joint Venture (JV) or JV Group in a jurisdiction the safe harbor test is applied to CEs as a separate "Tested Jurisdiction" from the JV or JV Group. For example, if an MNE Group had a CE and JV in Jurisdiction X, these would be treated as separate Tested Jurisdictions for the purposes of the Transitional CbCR Safe Harbor.

## QFSs

- Consistent source of data for a CE or permanent establishment (PE) (i.e., the CE accounts used to prepare the CFSs of the UPE or local statutory accounts) must be used to apply the safe harbor tests. For example, a group could not use one set of accounts to determine its Profit (or Loss) Before Tax of a CE and another to determine such CE's Simplified Covered Taxes.

- Further, consistent source of data must be used for all entities located in the same Tested Jurisdiction, with exceptions for Non-Material Constituent Entities (NMMCEs) and PEs.

- Qualified CbC Report determination is made on a Tested Jurisdiction-by-Tested Jurisdiction basis, i.e., failing to prepare a Qualified CbC Report for one Tested Jurisdiction does not mean a MNE Group fails the standard in all Tested Jurisdictions.

- Adjustments to QFSs, such transfer pricing adjustments, are not permitted unless such adjustments are specifically required in the Commentary or by the Agreed Administrative Guidance (e.g., the PPA adjustments discussed above).

- An intra-group payment treated as income in the QFSs of the recipient and expense in the QFSs of the payer is included in Total Revenues and PBT for the purpose of the safe harbor computations without further adjustments, irrespective of the treatment of that transaction for tax purposes in the jurisdiction of the recipient or the payer and the treatment of that transaction in the CbC Report.

- MNE Groups that are not required to file a CbC Report (e.g., because they are a purely domestic group) are still eligible to apply the Transitional CBCR Safe Harbor if they complete the relevant section of the GIR using data from QFSs.

- When QFSs are not available for a PE, the MNE Group may use separate financial statements prepared for regulatory, tax reporting or internal management control purposes to determine the portion of a Main Entity's Total Revenue and PBT that is attributable to the PE.

## Simplified ETR computation

- Simplified Covered Taxes include prior year income tax expense (i.e., return to provision adjustments) unless this expense relates to an uncertain tax position (UTP).

- Income tax expense of a PE must be allocated exclusively to the PE jurisdiction, i.e., it cannot also be accounted for in the jurisdiction where the Main Entity is located.

- Parent Entity or Main Entity's Covered Taxes on the income of a PE, CFC or Hybrid Entity do not need to be excluded from the Simplified ETR computation of the Constituent Entity-Owner or Main Entity,

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notwithstanding that this gives rise to the double counting of taxes if the ETR of the PE, CFC or Hybrid Entity jurisdiction must be calculated under the full GloBE rules.

### Routine profits test

- For the purposes of the routine profit test, the Substance-Based Income Exclusion (SBIE) amount is calculated using the same percentages for the payroll and tangible asset carve-out that would be used to compute the SBIE amount under the full GloBE rules, i.e., using the relevant transitional rates for 2024, 2025 and 2026.

**KPMG observation**

The guidance does not address how items held in consolidation (e.g., stock-based compensation) are treated for purposes of the Transitional CbCR Safe Harbor and leaves open the question of when these items may be recognized.

## Treatment of hybrid arbitrage arrangements under the Transitional CbCR Safe Harbor

The December AG notes that the IF has become aware of certain transactions that have the potential to exploit differences between the financial accounting treatment of a transaction as applied to counterparties in the transaction or between the tax and financial accounting treatments of a transaction to enable CEs to qualify for the safe harbor.

To counteract these arrangements, the December AG requires MNE Groups to adjust the Tested Jurisdiction's PBT and income tax expense for three types of Hybrid Arbitrage Arrangement:

1. **Deduction / non-inclusion arrangement** when a CE directly or indirectly provides credit or makes an investment in another CE that results in an expense or loss in the financial statements of a CE when there is no commensurate increase in the revenue or gain in the financial statements of the CE counterparty or the CE counterparty is not reasonably expected over the life of the arrangement to have a commensurate increase in its taxable income (including due to loss carry-forward or an unused interest expense carry-forward for which a valuation adjustment or accounting recognition adjustment has been made).

2. **Duplicate loss arrangement** when an expense or loss is included in the financial statement of a CE and the expense or loss is also included in the financial statement of another CE or the arrangement gives rise to a duplicate amount that is deductible for purposes of determining the taxable income of another CE in another jurisdiction.

3. **Duplicate tax recognition arrangement** when more than one CE includes part or all of the same income tax expense in its Adjusted Covered Taxes or Simplified ETR test, unless the income subject to tax is included in the relevant financial statements of both CEs or the arrangement arises because the Simplified ETR test does not require an adjustment (e.g., for CFC taxes).

The December AG specifies that this guidance applies in respect of arrangements that are entered into after December 15, 2022, unless a jurisdiction faces a constitutional constraint that prohibits it from applying this guidance retrospectively, in which case the guidance will only apply to arrangements entered into after December 18, 2023.

The December AG specifically notes that this guidance is limited to the Transitional CbCR Safe Harbor, but that further guidance will be provided to address hybrid arbitrage arrangements, including those identified above, that may affect the application of the GloBE Rules.

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**KPMG observation**

The principal objective of the rules on hybrid arbitrage arrangements seems to have been to bring in the anti-avoidance rule included in the GloBE Model Rules under Article 3.2.7. However, it is important to note that these rules apply more broadly than 3.2.7. For example, certain duplicate loss arrangements, when an expense is included in the financial statements of a CE in one jurisdiction, but for tax purposes is deductible in another jurisdiction, would not have been covered by 3.2.7.

**KPMG observation**

The December AG states that rules to counteract these hybrid arbitrage arrangements will be introduced in the full GloBE Rules to address comparable hybrid arbitrage arrangements. Businesses need to watch for those rules in future administrative guidance and need to start considering their response to Pillar Two, beyond the Transitional CbCR Safe Harbor.

# Administrative Guidance on application of GloBE Rules

This section of the December AG clarifies various aspects of the full GloBE Rules.

## Consolidated revenue threshold

The GloBE Model Rules and Commentary created uncertainty about how revenue is determined in applying the €750m scope threshold. Specifically, uncertainty existed as to whether revenue is determined by reference to the accounting standard used when preparing the CFSs or the broader definition used for CbCR, which includes items such as extraordinary income and gains from investment activities that accounting standards would not typically treat as revenue.

To address this uncertainty, the December AG clarifies that for the purpose of the GloBE Rules the following principles apply in determining revenue:

- Revenue includes the inflow of economic benefits arising from delivering or producing goods, rendering services, or other activities that constitute the MNE Group's ordinary activities.
- Revenue amounts are determined in line with the relevant accounting standard, which may allow netting for discounts, returns and allowances.
- If different types of revenue are separately presented in the consolidated profit and loss statement of the CFSs they must be aggregated.
- Revenue includes net gains from investments (whether realized or unrealized) reflected in the profit and loss statement of the CFSs and income or gains separately presented as extraordinary or non-recurring items.
- For financial entities, which may not record gross amounts from transactions in their financial statements with respect to certain items, the item(s) considered similar to revenue under the UPE's financial accounting standards must be used in the context of financial activities.

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### KPMG observation

The definition of revenue outlined above excludes income, such as interest income, when this income is ancillary to its ordinary activities (and is recorded below Cost of Goods Sold and Selling, General and Administrative Expenses). An example is specifically cited when a manufacturing company with ancillary interest income would not be required to take this income into account in determining its revenue.

### KPMG observation

For MNE Groups that are close to the scope threshold of €750m, and for whom there is uncertainty about how revenue is determined, this guidance provides some additional clarity. This guidance is likely to be particularly relevant for groups in the financial services sector, for whom "revenue" may not be a frequently used accounting concept.

## Mismatch between fiscal years of UPE and another Constituent Entity

In some scenarios, the financial accounts of a CE used to prepare a MNE Group's CFS are maintained based on a different fiscal period than that of the UPE. For example, a MNE Group may maintain their financial accounts based on a December 31 Fiscal Year and the foreign subsidiary CEs based on a November 30 Fiscal Year.

MNE Groups in this scenario adopt different approaches, some include the income of the subsidiary CE in its CFSs for the fiscal year of the CE (i.e., without accounting for the mismatch in time period), while others segment the income of the subsidiary CE to match the fiscal year of the CFSs (i.e., to align the time periods between the CE and the CFSs).

The December AG clarifies that for purposes of the GloBE Rules the Fiscal Year is generally the accounting period used by the UPE when preparing its CFSs, and when some CE of the MNE group maintain their financial accounts on a different year, the GloBE computations for the UPE's Fiscal year will be based on the same method to address the discrepancy in the fiscal years that is used by the MNE in its CFSs. Hence, in the example outlined above, the first year the MNE Group could be in-scope of the GloBE rules is the fiscal year ended December 31, 2024, and the GloBE computation of a CE with an accounting period ended November 30, 2024 would be based on the accounts used by the group to prepare its CFSs.

## Mismatch between fiscal year and tax year of Constituent Entity

In some instances, the fiscal year end of a CE may not correspond with its taxable year. For example, the fiscal year of a CE may end December 31 and the taxable year may end April 30. In this scenario, the MNE Group may rely on the accounting convention used to prepare its CFSs to determine its Adjusted Covered Taxes. This approach may also be adopted for JVs and JV Groups.

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# Further Administrative Guidance on the allocation of Blended CFC Taxes

The Feb AG introduced an allocation formula to allocate tax incurred under a Blended CFC Tax Regime for fiscal years that begin on or before December 31, 2025, excluding those that end after June 30, 2027. This rule applies to the U.S. GILTI regime.

The Allocation Formula (below) requires MNE Groups to compute their GloBE Jurisdictional ETR, which is then used to determine the Blended CFC Allocation Key. GILTI tax is allocated to jurisdictions that have a GloBE Jurisdictional ETR (computed based on the full GloBE computation (without taking into account the allocation of Blended CFC Taxes)) below 13.125% (the Applicable Rate for the GILTI regime). If an MNE Group qualifies for the Transitional CbCR Safe Harbor in respect of a jurisdiction, the MNE Group's top-up tax is deemed to be zero and the group will not have otherwise been required to calculate a GloBE Jurisdictional ETR for such jurisdiction. It had therefore been unclear whether a MNE Group would have had to compute a GloBE Jurisdictional ETR for these jurisdictions solely for purposes of allocating GILTI tax, undoing the benefits of the safe harbor.

The December AG recognises this and provides that an MNE Group will not be required to compute its Globe Jurisdictional ETR under the full calculation in these circumstances and also resolves ambiguity as to which GloBE Jurisdictional ETR is used in certain fact patterns.

## Temporary Allocation Formula:

$$\textbf{Blended CFC Tax Allocated to an Entity} = \frac{Blended\ CFC\ Allocation\ Key}{Sum\ of\ All\ Blended\ CFC\ Allocation\ Keys} \times Allocable\ Blended\ CFC\ Tax$$

$$\textbf{Blended CFC Allocation Key} = Attributable\ Income\ of\ Entity \times (Applicable\ Rate - GloBE\ Jurisdictional\ ETR)^*$$

*The Blended CFC Allocation Key is 0 for all entities in a jurisdiction when the relevant GloBE Jurisdictional ETR equals or exceeds 13.125%.

## Multiple GloBE Jurisdictional ETRs

In situations in which multiple ETRs are required to be calculated in respect of the same jurisdiction (e.g., when a MNE Group has both investment and non-investment entities in the same jurisdiction), the GloBE Jurisdictional ETR used in the formula is the ETR for the relevant entity or the blended group to which the entity belongs.

## No GloBE Jurisdictional ETR

The December AG provides that the GloBE Jurisdictional ETR does not need to be calculated for certain jurisdictions that would not otherwise be required to undertake the full calculation under the Model Rules and instead provides an alternative rate to use for purposes of allocating GILTI tax. For jurisdictions that qualify for the:

- **Transitional CbCR Safe Harbor** the MNE Group must use the ETR computed using the Simplified ETR test.

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- **Qualified Domestic Minimum Top-up Tax (QDMTT) Safe Harbor** the MNE Group must use the ETR computed for the purposes of the jurisdiction's QDMTT, except than any creditable QDMTT payable is added to the jurisdiction's taxes for the purpose of computing its ETR.

- **Under both the Transitional CbCR Safe Harbor and QDMTT Safe Harbor** when certain entities are not eligible for the safe harbor (e.g., Investment Entities) MNE Groups must compute the GloBE Jurisdictional ETR under the full GloBE Rules for these entities only.

- **For other jurisdictions**, such as those eligible for the de minimis election exclusion, the GloBE Jurisdictional ETR is computed using the Simplified ETR from the Transitional CBCR Safe Harbor.

## Application to non-GloBE Entities

- When a CE pays Allocable Blended CFC Tax for a non-GloBE Entity (i.e., an entity that is not a CE and is also not a JV group member) and this entity is located in a jurisdiction for which an MNE Group has multiple GloBE Jurisdictional ETRs, the MNE Group must use the GloBE Jurisdictional ETR for the blended group of Entities with the largest aggregate amount of Attributable Income (as computed for the purpose of the Blended CFC Tax Regime). Such an instance may arise when a US CE owns a greater than 10% interest in a CFC that is not a CE as the US CE may be subject to GILTI tax in respect of the non-CE CFC.

### KPMG observation

This guidance on the calculation of the Blended CFC Allocation Key provides much needed certainty to U.S. groups that have been assessing how GILTI taxes will be allocated between jurisdictions. The additional details mean that U.S. groups can now much more accurately determine the impact that the allocation of GILTI taxes may have on GloBE computation.

### KPMG observation

The allocation key can result in GILTI taxes being allocated to jurisdictions that have implemented a QDMTT because it is feasible that the jurisdiction's ETR, including creditable taxes imposed under a QDMTT is less than 13.125% because of the SBIE. As well, GILTI taxes can be allocated to jurisdictions qualifying for the routine profits test under the Transitional CbCR Safe Harbor if the Simplified ETR for such jurisdiction is less than 13.125%. To the extent GILTI taxes are allocated to jurisdictions that have implemented a QDMTT or that are eligible for the Transitional CbCR Safe Harbor under the routine profits test, such GILTI taxes are essentially "wasted" in that they will not be taken into account to reduce an MNE Group's top-up tax in respect of another jurisdiction under an IIR or UTPR and will also not reduce top-up tax in respect of the jurisdiction to which they are allocated (since GILTI is not taken into account under a QDMTT and no top-up up tax would have resulted under the Transitional CbCR Safe Harbor in any case).

### KPMG observation

In the longer term, as more jurisdictions introduce QDMTTs, the impact of allocating GILTI taxes may decline, but, for 2024, it could materially reduce a group's top-up tax exposure that would have otherwise been due under the IIR in respect of jurisdictions that have not yet implemented or have delayed their QDMTT.

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# Transitional filing deadlines for MNE Groups with short reporting fiscal years

IF members have agreed that MNE Groups with short reporting fiscal years (i.e., less than twelve months) ending before March 31, 2025 will not be required to file their GIR before June 30, 2026. This aligns with the earliest deadline that MNE Groups with a 12-month fiscal year could face, given that the GloBE Rules only apply to fiscal years beginning on or after December 31, 2023.

# Simplified Calculations Safe Harbor for Non-Material Constituent Entities

MNE Groups may omit subsidiaries from their CFSs if such omissions are not expected to influence the decisions made by primary users of the financial statements. MNE Groups are still expected to apply the GloBE Rules to such entities; however, the IF has recognized that the group may not prepare financial statements used for the preparation of the Group's CFSs.

The GloBE Rules permit a MNE Group to rely on local financial accounting standards when entity-level accounts used to prepare the CFSs are not available. However, the IF has also recognised that such information may not be available or may not be available in a timely manner.

To address concerns about the compliance costs of applying the GloBE Rules to these entities, the IF has developed Simplified Income, Revenue and Tax Calculations for Non-material Constituent Entities (NMCEs and such calculations, NMCE Simplified Calculations). The NMCE Simplified Calculations form part of a permanent safe harbor (referred to as the Simplified Calculations Safe Harbor), which like the Transitional CbCR Safe Harbor, provides that an MNE Group does not need to perform the detailed calculations of GloBE Income or Loss and Adjusted Covered Taxes and may use the alternative GloBE computations for electing NMCEs when the Simplified Calculations Safe Harbor is satisfied.

This guidance is a clarification of the Permanent Safe Harbor that was included in the *Safe Harbors and Penalty Relief: Global Anti-Base Erosion Rules (Pillar Two)* guidance that the OECD released in December 2022.

## Definition of NMCE

An NMCE is defined as an Entity, including a PE of a Main Entity, that is not consolidated in the UPE's CFSs but that meets the definition of a CE for the purposes of the GloBE Rules.

The Simplified NMCE Calculation can only be applied when (i) a MNE Group's CFSs are prepared in accordance with an Acceptable Financial Accounting Standard or an Authorised Financial Accounting Standard adjusted for Material Competitive Distortions and are subject to external audit, and (ii) in the case of an entity with revenue in excess of €50 million, such entity is only an NMCE if the financial accounts for the entity that are used to complete the group's CbC Report are prepared in accordance with an Acceptable or Authorised Financial Account Standard.

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# Application of Simplified Calculations Safe Harbor for NMCEs

The Simplified Calculations Safe Harbor for NMCEs is an annual election that is made for each NMCE individually. When an MNE Group make the election, it will undertake a *Simplified Income Calculation*, *Simplified Revenue Calculation* and *Simplified Tax Calculation* for the NMCEs for which the election is made as follows:

- Simplified Income = Total Revenue as determined under Relevant CbCR Regulations.
- Simplified Revenue = Total Revenue as determined under Relevant CbCR Regulations.
- Simplified Tax Calculation = Income Tax Accrued (Current Year) as determined under Relevant CbCR Regulations (i.e., excluding any deferred tax expenses, adjustments for non-current items and provisions for uncertain tax liabilities).
- Relevant CbC Regulations means the Country-by-Country Reporting regulations of the UPE jurisdiction or of the surrogate parent entity jurisdiction if a Country-by-Country Report is not filed in the UPE Jurisdiction. If the UPE jurisdiction does not have CbC requirements and an MNE Group is not required to file a CbC Report in any jurisdiction, Relevant CbC Regulations mean the OECD BEPS Action 13 Final Report and the OECD Guidance on the Implementation of Country-by-Country Reporting

Having determined the *Simplified Income*, *Simplified Revenue*, and *Simplified Tax Calculation* for the NMCE (or NMCEs) for which the election has been made, the MNE Group aggregates these results with the other CEs in Tested Jurisdiction (if any) and then determines whether one of the three tests that compromise the Simplified Calculations Safe Harbor is met:

1. **De Minimis Test** is met if the Average GloBE Revenue of the Tested Jurisdiction is less than €10 million, and the Average GloBE Income of that jurisdiction is less than €1 million. Average GloBE Revenue and Average GloBE Income will be computed for the current and two preceding fiscal years, e.g., in FY24 the average would be computed for FY22, FY23 and FY24.
2. **ETR Test** is met if the ETR for the Tested Jurisdiction is at least 15%.
3. **Routine Profit Test** is met if the GloBE Income of the Tested Jurisdiction is less than the SBIE amount.

# Example

A MNE Group elects to apply the NMCE Simplified Calculations in respect of a NMCE in Jurisdiction X, in which the MNE Group has one CE (that the UPE consolidates in its CFSs) and one NMCE.

The MNE Group will use the full GloBE Model Rules to determine the Revenue, GloBE Income and Covered Taxes of the CE and Jurisdiction X's SBIE Amount. The MNE Group will determine the equivalent revenue, income, and tax figures for the NMCE using the NMCE Simplified Calculations. The MNE Group will then aggregate the results for the CE and NMCE to determine whether the Simplified Calculations Safe Harbor is satisfied.

If one of the three tests is met the MNE Group's top-up tax for Jurisdiction X will be deemed to be zero. If the MNE Group does not meet one of the three tests it will be required to compute the GloBE Income and Covered Taxes of the NMCE using the full GloBE Model Rules and re-determine whether or not it has a top-up tax liability. Hence, for the MNE Group the Simplified Calculations Safe Harbor and NMCE Simplified Calculations will have no practical effect in Jurisdiction X.

## KPMG observation

For FY24-26, the Simplified Calculation Safe Harbor for NMCEs will only be relevant in jurisdictions when an MNE Group is not eligible for, and does not apply, the Transitional CbCR Safe Harbor. This

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is because when an MNE Group is eligible for and applies the Transitional CbCR Safe Harbor the top-up tax for a jurisdiction will be deemed to be zero, whether or not there are NMCEs located in that jurisdiction.

**KPMG observation**

The design of the Simplified Calculations Safe Harbor and NMCE Simplified Calculations mean that a MNE Group may only elect to apply the NMCE Simplified Calculations if it will meet one of the three safe harbor tests in relevant Tested Jurisdiction. Otherwise, irrespective of making the election it will still need to determine the GloBE Income and Covered Taxes of the NMCE on the basis of the full GloBE Model Rules.

It is feasible that when a MNE Group has two or more NMCEs in a jurisdiction it could determine that it can satisfy the Simplified Calculation Safe Harbor when electing to apply the NMCE Simplified Calculations for some NMCEs but not others. This is permitted by the rules, because a MNE Group elects to apply the NMCE Simplified Calculations on an entity-by-entity basis.

**KPMG observation**

The Simplified Calculations Safe Harbor could be a vehicle for a more radical simplification of Pillar Two, if the IF were able to agree simplified calculations that applied to other types of CEs, beyond NMCEs. However, there is little indication at this stage that this is something the IF is making progress on.

# What to expect in 2024?

As jurisdictions implement the GloBE Model Rules into domestic law it may become more difficult for the IF to issue further Administrative Guidance, or at least the issuance of that guidance may require jurisdictions to amend their domestic law. However, we are still expecting further guidance in 2024 from the IF covering issues such as the cross-border allocation of deferred tax expense, deferred tax liability (DTL) recapture, and post-filing adjustments.

The OECD has also committed to publish a revised version of the Commentary to the GloBE Model Rules incorporating the changes made in the various versions of Administrative Guidance in 2024. This will make it considerably easier to follow guidance, which is currently split over six separate documents.

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# Contact us

**For more information, contact a KPMG tax professional in Washington National Tax:**


**Danielle Rolfes**
**E:** drolfes@kpmg.com

**Kevin Brogan**
**E:** kevinbrogan@kpmg.com

**Marcus Heyland**
**E:** mheyland@kpmg.com

**Quyen Huynh**
**E:** qhuynh1@kpmg.com

**Alistair Pepper**
**E:** alistairpepper@kpmg.com

**John DerOhanesian**
**E:** jderohanesian@kpmg.com

**Daren Gottlieb**
**E:** darengottlieb@kpmg.com


**www.kpmg.com**

**kpmg.com/socialmedia**

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