Joint ventures and Pillar Two

October 2025

As the Pillar Two rules come to be implemented in ever more jurisdictions, and businesses get to grips with the practical issues arising, an increasing number of interpretative challenges have been identified for the application of the rules to joint ventures (JVs). JVs can be particularly prolific for MNEs in certain sectors, e.g., energy and natural resources.

The Pillar Two JV concept, first set out in the 2021 Model Rules, might be viewed as a narrowed version of the original idea, in the 2020 Pillar Two Blueprint, to subject associates (in which an MNE had a 20 percent and above holding) to Pillar Two tax. The Pillar Two JV concept is quite particular and can differ from the JV concept under accounting standards. A Pillar Two JV will exist where an MNE has an investment in an entity which is equity method accounted, in the consolidated financial statements (CFS) of the MNE, and where the MNE ownership interest (OI) percentage in the entity is 50 percent or above (subject to certain exclusions). This definition can include entities which the accountants do not treat as JVs (e.g., associates) but can also exclude entities which the accountants might treat as JVs (where the holding percentage is less than 50 percent but there is significant influence).[1]

For this reason, as well as others, businesses can in practice be 'caught out' by the Pillar Two JV rules. At first glance, an MNE may consider themselves to have no Pillar Two JVs only to discover, on deeper analysis, that they actually do. An unusual approach is taken to calculating the OI percentage, which equally weights MNE equity rights to profits, capital and reserves – MNEs can miss the fact that a Pillar Two JV exists if they simply look at equity holding percentages. The fact that non-JV associates (from an accounting perspective) can also be treated as Pillar Two JVs has been seen in practice to contribute to outcomes where one MNE treats an entity as a Pillar Two JV, while a second MNE consolidates the same entity. This leads to unusual outcomes which may not have been entirely anticipated by the Inclusive Framework at rule design stage.

The purpose of this article is to explore one important theme in the application of the Pillar Two JV concept. This is namely the manner in which the Pillar Two rules "mix-and-match" the characterizations of a Pillar Two JV entity, for different applications of the various Pillar Two rules. In some circumstances the Pillar Two rules treat a Pillar Two JV entity as a 'normal' Constituent Entity (CE), while in other instances the rules will treat the entity as being the Ultimate Parent Entity (UPE) of a separate MNE group. In still further instances the rules will treat the entity as not being a CE at all, but rather as an 'inert' equity investment holding of the MNE group. For the purposes of simplicity, in this article we refer to this as the Pillar Two rules ascribing one of three different "Personalities" to a Pillar Two JV entity in different circumstances.

The article seeks, in particular, to highlight the instances in which it is not entirely clear which "Personality" the rules require to be used for a given application of the rules. It will also highlight the tensions that may arise from 'switching' between "Personalities" for the application of two or more related rule provisions, where it might make more intuitive sense for a single, consistent "Personality" to be used.

1 Where an entity qualifies as a JV or JV subsidiary for GloBE purposes, this will be referred to as a Pillar Two JV in this article. We will distinguish between Pillar Two JVs that are treated as a CE of the main group, or a separate group, for certain parts of the Pillar Two rules, and 'normal CEs' that are consolidated on a line-by-line basis.

Issues further arise or are even aggravated where two JV owners, in the same Pillar Two JV, are in different positions. This is the case, for example, where the owners are subject to different levels of taxation, where their countries of residence apply or interpret certain aspects of the GloBE rules differently, or where the Pillar Two JV is recognized differently in their accounts.

The outstanding uncertainty in how elements of the Pillar Two JV rules operate makes applying these rules difficult, but we've consistently heard that the biggest challenge is collecting the data necessary to apply the rules, which companies tax departments were unlikely to have access to prior to Pillar Two. Moreover, because Pillar Two JVs can be small, the cost of collecting this data can be significant when compared to the potential top-up tax liability, raising the question whether the Inclusive Framework should consider further simplification efforts, such as excluding Pillar Two JVs below a certain revenue threshold or permitting groups to use a simplified calculation similar to that provided for Non-Material Constituent Entities. However, at the time of writing, there is no indication that Inclusive Framework members are inclined to pursue this path, and so groups need to dive into the complexity of the Pillar Two JVs rules. This article explores that complexity and identifies areas where countries may apply the rules differently.

Note, however, that the issues highlighted in this article are not the only source of difficulty with respect to the handling of JVs for Pillar Two purposes. We plan to return, in later articles, to other ambiguities and practical issues that may add further complexity with respect to the treatment of Pillar Two JVs and other forms of joint operations, e.g., where ownership interest percentages are pushed over or below the 50 percent line midway through a fiscal year or where entities are consolidated under a proportional consolidation method.

Rule application to Pillar Two JVs

The Pillar Two Model Rules apply to entities and permanent establishments (PEs), that qualify as CEs and that are part of an MNE group with a consolidated group revenue that exceeds EUR 750 million in at least two of the last four consecutive fiscal years.

The term "Constituent Entity" includes any entity that is included in a Group and that is not excluded from the scope of the Model Rules, e.g., government entities that do not carry on a trade, international organizations and non-profit organizations, pension funds as well as investment funds and real estate investment vehicles that qualify as the UPE of an MNE group.

The term "Group" means a collection of enterprises related through ownership or control such that the assets, liabilities, income, expenses and cash flows of those entities (1) are included in the Consolidated Financial Statement (CFS) of the UPE; or (2) are excluded from the CFS of the UPE solely on size or materiality grounds, or on the grounds that the entity is held for sale.

Under the core rules above, entities that are accounted for under the equity method would not qualify as a CE and, thus, would be fully excluded from the scope of Pillar Two absent a special rule for such entities.

However, Article 6.4 of the GloBE Model Rules establishes special rules for entities that qualify as JVs for GloBE purposes thereby bringing such JVs into scope of the GloBE Rules, along with their JV subsidiaries. JVs within the meaning of the GloBE Rules are equity method accounted entities in which the UPE holds directly or indirectly 50 percent or more of the Ownership Interests and that do not meet any of the exclusion criteria.[2]

Importantly, not all equity accounted operations will be impacted by Pillar Two. Due to the applicable 50 percent ownership threshold, it is important to note that entities that are considered as JVs for accounting purposes will not be brought into scope of Pillar Two where the UPE holds less than 50 percent of its Ownership Interests. Similarly, an entity commonly referred to as an "associate" under accounting rules (e.g. IAS 28) and reported under the equity method typically would not meet the GloBE definition of a JV if the UPE does not reach the 50 percent ownership threshold.

2 A Joint Venture does not include (1) an Ultimate Parent Entity of an MNE Group that is subject to the GloBE Rules; (2) an Excluded Entity as defined by Article 1.5.1, (3) an Entity whose Ownership Interest held by the MNE Group are held directly through an Excluded Entity referred in Article 1.5.1 and the Entity operates exclusively or almost exclusively to hold assets or invest funds for the benefit of its investors; carries out activities that are ancillary to those carried out by the Excluded Entity; or substantially all of its income is excluded from the computation of GloBE Income or Loss in accordance with Articles 3.2.1(b) and (c), (4) an Entity that is held by an MNE Group composed exclusively of Excluded Entities; or (5) a JV Subsidiary.

Are Pillar Two Joint Ventures subject to the same rules as normal CEs?

The treatment of Pillar Two JVs for GloBE purposes is clarified in different places in the Model Rules and related Commentary and varies depending on which area of the rules is in question.

This has the result that there is no single, consistent framing of what a Pillar Two JV 'is' for the purposes of the rules. The characterization of a Pillar Two JV, for each individual application of the rules, ends up being 'influenced' by the broader characterization of entities in the specific part of the Rules/Commentary for which guidance on a particular application of the rules is set out.

As noted in the introduction, this leads us to identify three different "Personalities" for a Pillar Two JV entity with respect to the different parts of the Model Rules/Commentary and these can be clustered as follows:

Personality 1: JV treated as the UPE/CE of a separate group	Personality 2: JV treated as a (lower-tier) CE of the main group	Personality 3: JV not treated as a CE
Consolidation election (Article 3.2.8)	Application of arm's length principle between JVs and regular CEs (Article 3.2.3)	Scope revenue threshold testing (Article 1.1)
Separate blending (Article 6.4)	Allocation of cross-border covered taxes between JVs and regular CEs (Article 4.3)	JV not required to apply IIR/UTPR (Article 2)
Treatment of flow-through JVs (Article 3.5/Article 7.1)		Not required to submit GIR (Article 8.1)
		Exclusion for initial phase of international activity (Article 9.3)

The next section of this article will explore examples of circumstances in which these "Personalities" are relevant.

Personality 1: JV treated as the UPE / CE of a separate group

The general principle is outlined in Article 6.4 of the Model Rules. It generally requires MNE Groups to apply Chapters 3 to 7, and Article 8.2 for purposes of computing any Top-Up Tax of the Pillar Two JV and its JV Subsidiaries as if they were CEs of a separate MNE Group and as if the Pillar Two JV was the Ultimate Parent Entity of that Group. Accordingly, the JV Group's ETR needs to be calculated separately from the rest of the main MNE Group without blending the GloBE income and Covered Taxes with other normal CEs.

The concept of the Pillar Two JV being treated as a deemed CE of a separate group is confirmed in several parts of the Commentary:

One example is **Article 3.2.8**, which provides an election that permits consolidating intra-group transactions in the same jurisdiction where the local CEs are included in a tax consolidation group. The aim is to align the GloBE rules with local tax regimes that disregard domestic intra-group transactions for tax purposes. The Commentary to Article 3.2.8 clarifies that the election is limited to transactions between CEs (other than Investment Entities, Minority-Owned Constituent Entities (MOCEs), and JVs treated as CEs under Article 6.4) located in the same jurisdiction.[3] As such, transactions between normal CEs of the main group and Pillar Two JVs cannot be consolidated for GloBE purposes given that they are part of different local blending groups.

Another example is the treatment of flow-through Pillar Two JVs. The Commentary to the transitional Country-by-Country Reporting Safe Harbour (TSH) rules notes that Pillar Two JVs that qualify as Tax Transparent Entities are to be treated as UPEs of a separate group and are subject to the rules for flow-through UPEs, namely **Article 7.1**.[4] The aim of that provision is to align the GloBE rules with local tax regimes that provide for a single-level taxation approach such that tax is levied at the owner rather than the entity level. Without Article 7.1, approaches to single-level taxation would result in outcomes inconsistent with the policy objectives of Pillar Two, where GloBE income remains at the level of a Tax Transparent UPE, whilst no tax expense is recognized at the level of the Tax Transparent UPE. In that case, the ETR of the UPE itself would be nil, exposing the UPE to a top-up tax charge even though the burden of taxation is borne by the UPE's owners. For this reason, Article 7.1 allows the GloBE income of a flow-through UPE to be reduced by the amount of income that is attributable to the UPE owners provided that the income at the level of those owners is subject to tax at a nominal rate of at least 15 percent (or provided certain other conditions are met). The TSH guidance clarifies that this approach is also available for a flow-through Pillar Two JV such that its GloBE income is to be reduced where the JV owners meet the conditions of Article 7.1. The application of this rule and potential unintended consequences will be examined later in this paper.

3 Commentary to 3.2.8, para. 135.
4 Commentary to Transitional Country-by-Country Reporting Safe Harbour, para. 34.

Personality 2: JV treated as a (lower-tier) CE of the main group

Whilst deemed UPE / CE of a separate group is the dominant personality, there are some instances where the Pillar Two JVs are treated as lower-tier CEs of the main group.

One example is the application of **Article 3.2.3.** That provision generally requires MNE Groups to apply the arm's length principle to cross-border, intra-group transactions in order to protect the integrity of jurisdictional blending. The provision requires intra-group transactions to be recognized at arm's length for GloBE purposes and to be accounted for in the determination of GloBE Income in both the initiating and counterparty jurisdictions, unless the transaction is carried out within one jurisdiction or the exception for Undertaxed Jurisdictions applies.[5] The Commentary to Article 3.2.3 clarifies that the arm's length principle also applies to transactions between Pillar Two JVs and normal CEs of the main group thereby deeming the Pillar Two JV as a CE that is part of the main group.[6]

Similarly, the Commentary to Article 6.4 clarifies that certain cross-border tax expenses should be allocated between Pillar Two JVs and normal CEs in accordance with **Article 4.3.** As a starting point, the amount of Covered Taxes allocated to each CE of a jurisdiction is the amount of Covered Taxes accrued in the financial accounts of that CE. However, Article 4.3.2 requires certain Covered Taxes to be reallocated from one CE to another. For example, Covered Taxes on distributions from a CE (e.g., withholding taxes on dividends distributed) during the Fiscal Year which are accrued in the financial accounts of the CE's direct CE-owners should be allocated to the distributing CE. Furthermore, where CE-owners are subject to a CFC tax regime and Covered Taxes are included in the accounts of direct or indirect CE-owners under a CFC tax regime on their share of the CFC income, that amount of Covered Taxes should be allocated to the CE (i.e., the CFC) – subject to certain exceptions. In this context, the Commentary notes that the computation of the jurisdictional ETR for the Pillar Two JV should consider Covered Taxes recorded in the financial accounts of the normal CEs of the main Group that relate to the GloBE income or loss of the Pillar Two JV in accordance with Article 4.3. As such, the Commentary treats the Pillar Two JV as a lower-tier CE of the main group by allowing downward adjustments from normal CEs to Pillar Two JVs, which would not be possible if the Pillar Two JV would be regarded as being part of a separate MNE Group.

5 No adjustment under Article 3.2.3 is to be made where the transfer pricing adjustment increases or decreases the MNE Group's taxable income in a jurisdiction that has a nominal tax rate below the Minimum Rate or that was a Low-Tax Jurisdiction with respect to the MNE Group in each of the two Fiscal Years preceding the unilateral transfer pricing adjustment (an Undertaxed Jurisdiction).

6 However, it should be noted in this context that the exception for same-country transactions does not appear to apply to transactions between JVs and other CEs. Although the wording of the Commentary to Article 3.2.3 (para. 108) is not entirely clear, transactions between Pillar Two JVs and other normal CEs that are located in the same jurisdiction should, therefore, be recorded in accordance with the arm's length principle similar to cross-border transactions. Following the reasoning of the Commentary with respect to MOCEs, this is necessary because the ETR and Top-up Tax computations are calculated separately for Pillar Two JVs and normal CEs. Thus, the income and expense of the parties to the transaction will not be eliminated in the jurisdictional blending computation and failure to reflect transactions based on the arm's length principle would run the risk of distorting the ETR and Top-up Tax calculations.

Personality 3: JV not treated as a CE

Finally, a number of areas in the Model Rules and Commentary rely on a third concept whereby Pillar Two JVs are not regarded as a CE at all, but rather as an 'inert' equity investment holding.

One example is the **Commentary to Article 3.2.1,** which clarifies that entities that are JVs and associates for accounting purposes are not CEs under the definition in Article 1.3 because they are not controlled by the MNE Group.[7] Consequently, for purposes of testing the revenue threshold of EUR 750 million, revenues of the Pillar Two JV should be disregarded. Similarly, the location of the Pillar Two JV should be disregarded in determining whether the group qualifies as a MNE Group.[8] Pillar Two JVs are, however, brought into the scope of the rules where the revenue of normal CEs of the main group exceeds the revenue threshold in at least two of the last four consecutive fiscal years.

Even where a Pillar Two JV is generally regarded as a CE of the main group under Article 6.4, it cannot collect IIR Top-up Tax with respect to lower-tier low-taxed Pillar Two JV Subsidiaries. In other words, it is not treated as a Partially-owned Parent Entity (POPE)[9] for the purposes of applying the Top-up Tax charging rules under **Chapter 2 of the Model Rules**. Instead, normal CEs of the main group that hold directly or indirectly Ownership Interests in the Pillar Two JV are required to apply the IIR with respect to their allocable share in the Pillar Two JV. Article 6.4 further provides that where the top-up tax attributable to the Pillar Two JV has not been brought into charge under a qualified IIR, such liability shall be added to the total UTPR top-up tax amount of the rest of the main group.

With respect to the administration of the GloBE rules, the Commentary to **Article 8.1** clarifies that a Pillar Two JV is not required to submit a GIR for the main group because it is not a CE of that group.[10]

Lastly, according to the Commentary to **Article 9.3,** tangible assets and the location of Pillar Two JVs are to be disregarded when applying the threshold test for the exclusion of the initial phase of international activity.[11] This provision provides for UTPR relief where an MNE Group has CEs in no more than six jurisdictions and where the sum of the net book values of tangible assets of all CEs located in all jurisdictions other than the reference jurisdiction does not exceed EUR 50 million. The QDMTT Commentary further allows jurisdictions to exclude qualifying groups from the application of local QDMTT.[12]

7 Commentary to Article 3.2.1(c), para. 50.

8 According to Article 1.2.1, an MNE Group means any Group that includes at least one Entity or Permanent Establishment that is not located in the jurisdiction of the Ultimate Parent Entity.

9 Defined as a CE (other than a UPE, PE or Investment Entity) that owns (directly or indirectly) an Ownership Interest in another Constituent Entity of the same MNE Group and has more than 20 percent of the Ownership Interests in its profits held directly or indirectly by persons that are not CEs of the MNE Group.

10 Commentary to 8.1.1, para. 8.

11 Commentary to 9.3, para.21.

12 Commentary to Article 10, QDMTT, para. 118.51. Jurisdictions have three options how to apply the exclusion for QDMTT purposes. Option one allows the jurisdiction not to adopt Article 9.3 in their QDMTT legislation. Option two allows the jurisdiction to introduce Article 9.3 in their QDMTT legislation but limited to the cases where none of the Ownership Interests in the CEs located in the QDMTT jurisdiction are held by a Parent Entity subject to a QIIR. Option three allows the jurisdiction to adopt Article 9.3 in their QDMTT legislation without the limitations in option two.

What are some of the issues to consider when dealing with Pillar Two Joint Ventures for GloBE purposes?

In the following section, we discuss several cases to demonstrate the complexity of dealing with Pillar Two JVs for GloBE purposes, considering the varied application of the JV personality concepts, for different rule provisions. These issues are reinforced where both JV owners are in scope of Pillar Two but are in different positions. These are necessarily just a small selection of the interpretative ambiguities so far identified with the Pillar Two JV concept.

Issue 1:

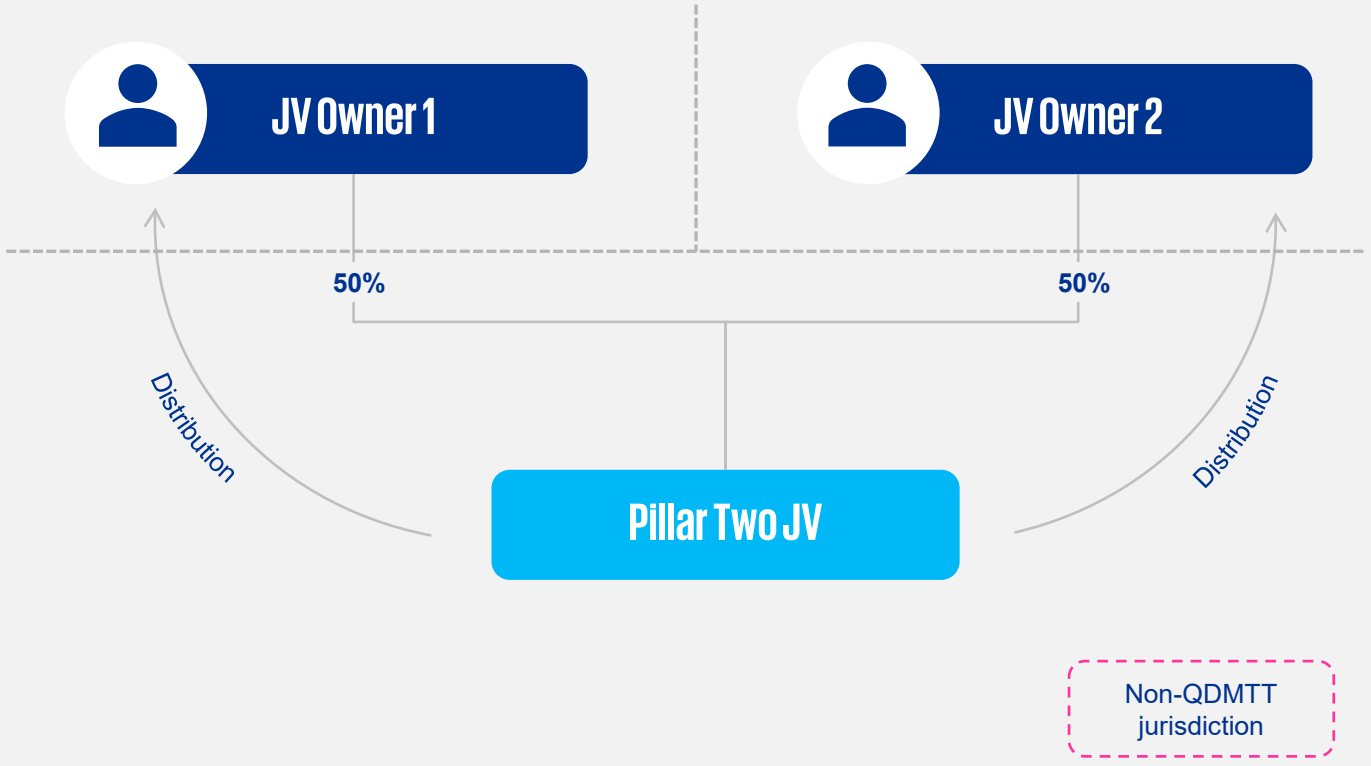
Allocation of cross-border taxes between Pillar Two JVs and normal CEs

As outlined above, the Commentary to Article 6.4.1(a) seems to indicate that Pillar Two JVs need to be treated in the same way as normal CEs as regards downward allocation of cross-border taxes (Personality 2), which differs from the general GloBE principle requiring Pillar Two JVs to be considered as a separate MNE Group.

However, it appears that several Pillar Two implementing jurisdictions take different approaches with respect to allocation of cross-border taxes between Pillar Two JVs and normal CEs.

From the perspective of some jurisdictions, the withholding taxes recorded at owner level are to be allocated to the Pillar Two JV (Personality 2). By contrast, from the perspective of other jurisdictions, the tax recorded at owner level is not to be allocated to the Pillar Two JV (Personality 1). The tax thus remains at the level of JV owner 1.

Example 1



	JV owner 1	JV owner 2	Pillar Two JV
Operating Income	100	100	100
Dividend Income	50	50	0
GloBE Income	**100**	**100**	**100**
Tax expense on operating income (i.e., other than distributed profits)	20	20	10
Tax expense on distributions from JV	5	5	

Assume that Pillar Two JV (located in a non-QDMTT jurisdiction) distributes dividends in the amount of 50 to each of its 50%-owners. JV owner 1 and JV owner 2 form part of separate MNE Groups in scope of Pillar Two and both consider the dividends as Excluded Dividends for GloBE purposes.

When Pillar Two JV distributes the profits to the owners, taxes are accrued in the accounts of JV owner 1 (5) and JV owner 2 (5).

From the perspective of the jurisdiction in which JV owner 1 is located, the taxes are to be allocated to Pillar Two JV. As a result, Pillar Two JV would have an ETR of 20% ((10+5+5) / 100) and would not trigger any IIR top-up tax liability at the level of JV owner 1.

KPMG comment

This could require alignment and information exchange between the JV owners to enable JV owner 1 to take into consideration the taxes paid at the level of JV owner 2. Such coordination may not always be readily feasible in practice.

From the perspective of the jurisdiction in which JV owner 2 is located, the tax on the distribution is not to be allocated to the Pillar Two JV. The tax thus remains at the level of JV owner 1 (and may need to be excluded from the amount of Covered Taxes where it constitutes an excluded dividend). As a result, from the perspective of the jurisdiction of JV owner 2, Pillar Two JV would have an ETR of 10% (10 / 100) and would trigger IIR top-up tax liability of 2.5 (50% x (15%-10%) x 100).

KPMG comment

We understand that, for example, Canada has clarified that Covered Taxes are allowed to be allocated to the Pillar Two JV even though the Pillar Two JV is not considered as a member of the MNE group for other purposes. A similar approach seems to apply in Singapore. On the other hand, we understand that, for example, the Australian Pillar Two law deems JVs to be CEs for certain purposes but not in relation to the section on the adjustment of Covered Taxes. Consequently, cross-border taxes may not be allocated to the Pillar Two JV in Australia given that the Pillar Two JV is not considered as CE of the same group. Our understanding is that similar approaches are taken by the Netherlands and the United Kingdom. As such, taxpayers may want to closely monitor whether and how further jurisdiction may set out their own local interpretations in this context.

KPMG comment

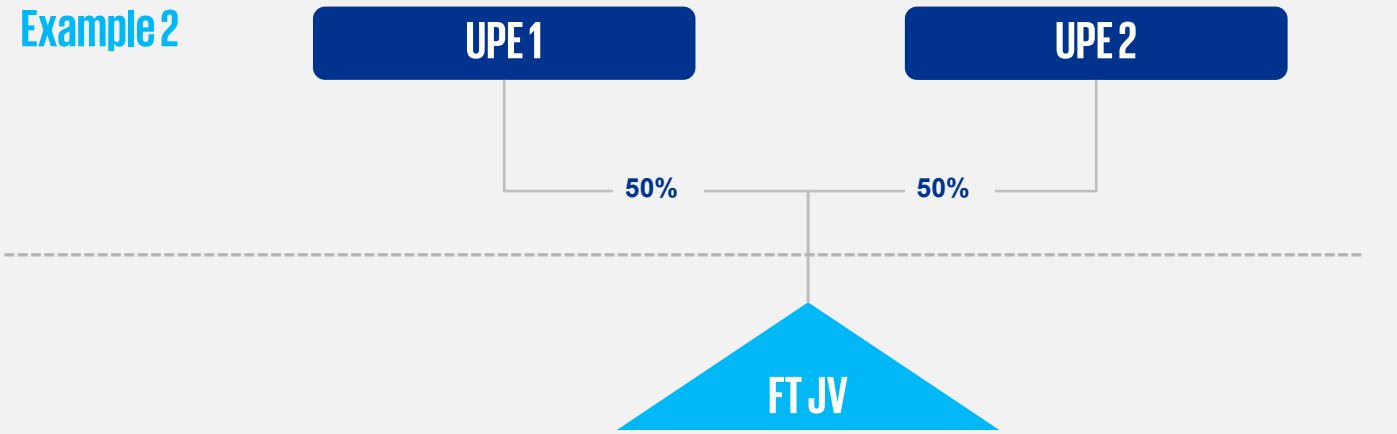
A similar issue may arise where the Pillar Two JV is located in a QDMTT jurisdiction and withholding tax on the dividend distribution is accrued in the accounts of the JV owner(s). Per the OECD QDMTT guidance, such withholding taxes are to be allocated to the distributing Constituent Entity under QDMTT. Conceivably, there is a risk that differences between QDMTT implementing jurisdictions may emerge as to how this allocation rule is applied in the context of Pillar Two JVs. Such differences may further complicate the completion of the GloBE Information Return with respect to QDMTT jurisdictions.

Issue 2:

Treatment of flow-through Pillar Two JVs

As outlined above, the Commentary to the TSH suggests treating flow-through Pillar Two JVs as flow-through UPEs of a separate group, i.e., in line with the general principle (Personality 1), and to reduce the GloBE income at the level of the JV where the owners meet the conditions under Article 7.1. Consequently, the Commentary appears to not allow the allocation of GloBE income from flow-through Pillar Two JVs to its owners pursuant to Article 3.5.1(c).

Example 2



	UPE 1	UPE2
GloBE Income (Attribute to JV owners)	100	100
Tax at Minimum rate	15	15
Nominal ratein JV owner jurisdiction	10%	20%
Reasonable expected tax liability by JV owner	10	20
GloBE income reduction Article 7.1.1(a)(i)	**No**	**Yes**

In this scenario, following the Commentary to the TSH, the GloBE income of in total 200 at the level of FT JV would only be reduced to 100. GloBE income of 100 attributable to UPE 1 would not be reduced and would remain at the level of FT JV with no corresponding Covered Taxes. Accordingly, Top-up Tax in the amount of 15 would be triggered at the level of FT JV.

On the other hand, one could argue that the Commentary to Article 6.4.1(a), allowing for an allocation of taxes from normal CEs to Pillar Two JVs (Personality 2), might open up the possibility of treating Pillar Two JVs as CEs of the main group with respect to other areas of the GloBE framework, including attributing flow-through Pillar Two JV income and losses to normal CEs in line with Article 3.5.1(b).

Such interpretation might be argued to offer a more reasonable outcome where the Pillar Two JV income is subject to tax in one JV owner's (UPE 1) hands at a tax rate lower than the minimum rate (i.e., UPE 1 does not meet the 7.1 conditions) and in the other JV owner's (UPE 2) hands at a sufficiently high tax rate to meet the 7.1 conditions.

KPMG comment

There is a question whether Top-up Tax of 15, per the example, would be exclusively attributed to the low-taxed JV owner (UPE 1), on the basis that the inclusion ratio of UPE 2 would be reduced to zero. Alternatively, both JV owners could face a Top-up Tax liability (i.e., EUR 7.5 each) on the basis that the inclusion ratio relies on the pure quantum (i.e., 50 percent each). If the latter were to apply, there may be additional 'second-order tax implications' in cases where compensation payments are made by UPE 1 for the additional tax borne by UPE 2. In this context, questions would arise as to whether such payment might be taxable (under corporate income tax rules) or trigger withholding tax liability.

By contrast, if one would apply Article 3.5.1(b), the ETR at the level of the JV owners would reflect income recognized at the level of the Pillar Two JV and the Covered Taxes paid at the level of the owner. At the level of the flow-through JV, no income and no taxes would be recognized for Pillar Two purposes. Consequently, Top-up Tax in the amount of 5 ((15% - 10%) x 100) would be triggered (i.e., not 15). In addition, the Top-up Tax would arise only at the level of the JV owner (UPE 1) that is subject to a tax rate lower than the minimum rate and would not impact the high-taxed JV owner (UPE 2).

KPMG comment

In consequence, following the same approach as for the allocation of cross-border taxes (i.e., treating Pillar Two JVs as CEs of the main group) would provide for an economically more sensible outcome. There are indications that some Pillar Two implementing jurisdictions might be in favor of attributing income and losses from flow-through Pillar Two JVs to normal CEs (i.e., applying Article 3.5.1(b) to flow-through Pillar Two JVs), albeit such approach would not be consistent with the general GloBE principle of requiring separate calculations for Pillar Two JVs. As such, it is advisable for taxpayers in scope of Pillar Two to keep monitoring potential differences in local implementation of the rules and accompanying local guidance with respect to the treatment flow-through Pillar Two JVs.

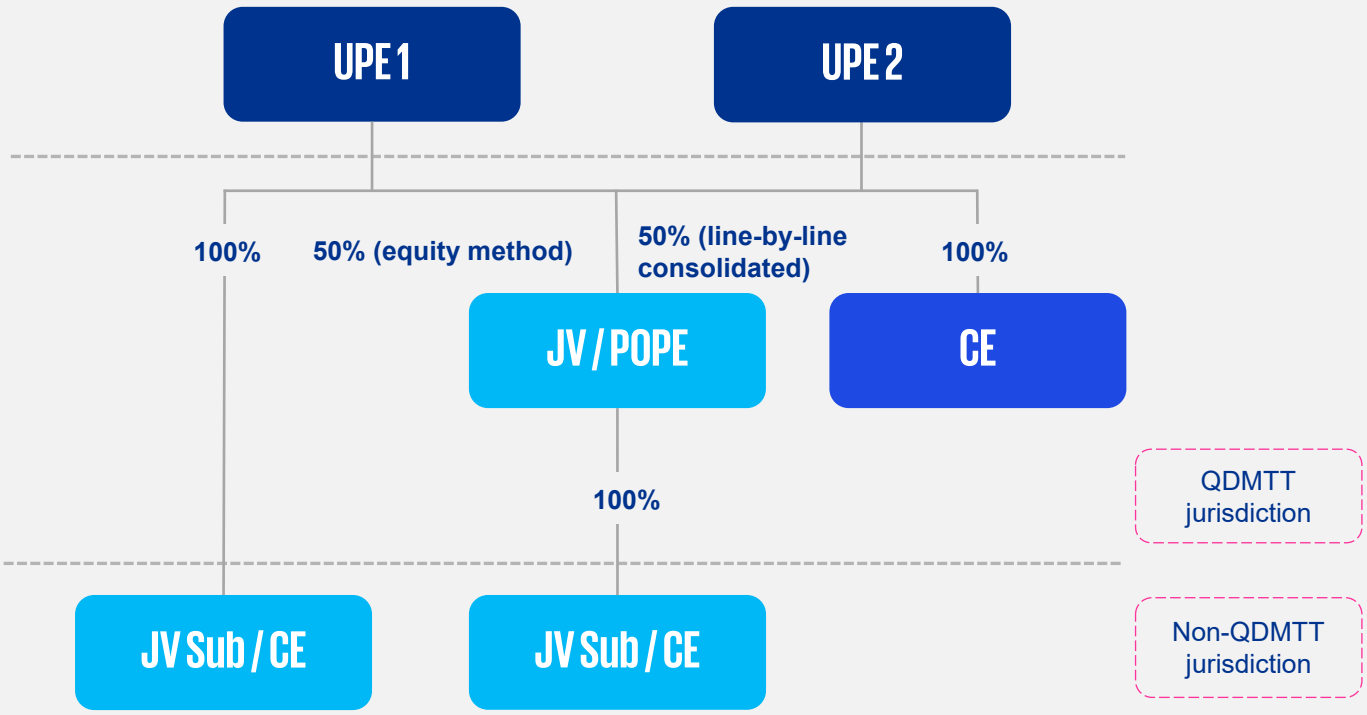
Issue 3:

Different consolidation approaches by JV owners

As already indicated in Examples 1 and 2, issues may arise where both JV owners are in scope of Pillar Two but are in different positions.

This is also true in a situation where one group (UPE 1 / Group 1) recognizes a 50%-owned entity under the equity method whilst the other group (UPE 2 / Group 2) recognizes the other 50% share in the entity on a line-by-line basis. This situation appears to arise in practice more frequently than initially expected, potentially due to different consolidation determinations under the same GAAP or different consolidation criteria under different GAAPs.

Example 3



In this scenario, UPE 1 would treat the equity accounted entity as a Pillar Two JV and its subsidiary as a JV Subsidiary for GloBE purposes. By contrast, UPE 2 would consider the entity as a POPE (and, therefore, as a normal CE) and its subsidiary also as a normal CE.

This gives rise to a number of questions, including whether the entities can be blended with other CEs located in the same jurisdiction. Whilst in the view of UPE 1, this would not be possible due to the blending restrictions provided under Article 6.4, Group 2 would blend the income and taxes of the entities with other CEs located in the same jurisdiction. Similarly, UPE 1 and UPE 2 would potentially take different approaches with respect to the rules discussed above (i.e., allocation of cross-border taxes, flow-through entities, consolidation election, application of the arm's length principle, etc.). For IIR purposes, the question also arises whether Top-up Tax would need to be levied at the level of UPE 1 or JV/POPE.

One way of solving this issue is to assume that one qualification takes precedence over the other. For example, the Pillar Two JV qualification could take precedence such that both UPE 1 and UPE 2 would treat the entities as Pillar Two JV and Pillar Two JV Subsidiary, respectively. However, this would require alignment and information exchange between the JV owners, which may not always be feasible in practice.

Alternatively, both groups need to run separate calculations for Income Inclusion Rule (IIR) and Domestic Minimum Top-up Tax (DMTT) purposes in accordance with their own qualification. However, this approach automatically leads to the issue of potential double taxation, for example, where QDMTT with respect to JV/POPE is calculated separately for purposes of Group 1 and Group 2 (with a deemed ownership interest of 100 percent for each calculation). Similarly, double taxation may arise where IIR top-up tax with respect to JV Sub/CE would be levied both at the level of UPE 1 (allocable share 50 percent) and JV/POPE (allocable share 100 percent).

KPMG comment

We understand that, for example, Ireland and the UK have clarified in their respective Pillar Two guidance manuals that the ETR and top-up amounts of the Pillar Two JV group will be calculated separately for each JV owner. As noted above, the approach of having separate calculations for each JV owner requires a proper mechanism to avoid double taxation. It may also require a mechanism to reconcile differences in cases where a QDMTT jurisdiction receives two GIRs (from each JV owner) with different calculations, for example, due to different accounting treatments at the level of the JV owners.

KPMG comment

Whilst the Irish and UK guidance appear to remain silent on this, we note that the Pillar Two legislation in Hong Kong (SAR) China provides relief from double taxation including in situations where an entity is a Pillar Two JV of MNE Group 1 and a normal CE of MNE Group 2. More specifically, according to the legislation in Hong Kong (SAR), China, double tax relief may be provided by the Commissioner in a manner that is reasonable in the respective circumstances. Notably, no specific solutions are provided at this stage by the Hong Kong authorities, which may be to give them latitude to deal with potentially complex cases. At the same time, it indicates that the issue has been brought to the attention of Inclusive Framework members. As such, it is advisable for taxpayers in scope of Pillar Two to keep monitoring local implementation of the rules and accompanying local guidance, which may offer clarifications on how to appropriately limit the risk of double taxation in these scenarios.

What else to consider / outlook?

The article aimed at highlighting some of the challenges in applying the Model Rules / Commentary in respect of Pillar Two JVs as well as local differences in application and interpretation that have already started to emerge as a result. It is important to note that the article has examined just a small selection of the interpretative ambiguities so far identified with the Pillar Two JV concept and that there are likely additional sources of difficulty with respect to the handling of JVs for Pillar Two purposes. We also expect that further countries will clarify their positions over the coming months and potentially provide for additional 'twists' in the context of the treatment of Pillar Two JVs. As such, in-scope groups will want to carefully monitor approaches taken by GloBE implementing jurisdictions in this respect and seek advice from local Pillar Two experts where necessary.

Please also note that there are a number of other technical or practical challenges that may add further complexity with respect to the identification and treatment of Pillar Two JVs. One example is the determination of ownership interest (OI) percentages. Where OI percentages change midway through a fiscal year (e.g., issuance/transfer of shares) such that they are pushed over or below the 50 percent line, there is a question whether the OI percentages need to be recalculated on the occurrence of the 'change event'. This means that an entity could be a Pillar Two JV for part of a year, and then not a Pillar Two JV for the rest of the year. Alternatively, the OI percentages are calculated only on an annual basis such that an entity is either a Pillar Two JV for a full year or not at all. We plan to explore in later articles the ambiguities around OI determinations with respect to the different parts of the Model Rules/Commentary in more detail.

Finally, one should also consider the ongoing work at the level of the Inclusive Framework on a "side-by-side" (SbS) system between the U.S. international tax system and Pillar Two as this may impact and change the way Pillar Two JVs are treated for GloBE purposes. As at the date of this article, it is our understanding that possible technical solutions are being worked out by the Inclusive Framework to exclude groups from IIR and UTPR where the UPE is located in a jurisdiction that operates an eligible SbS regime (for more details, see a report prepared by KPMG International). One key issue to resolve in this context will be the treatment of entities that are partly held by groups eligible for the SbS system (e.g., Pillar Two JVs, Minority-owned Constituent Entities, Partially owned Parent Entities). Negotiations on the SbS system are set to continue for the remainder of 2025, and likely beyond, so developments should be monitored closely.

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