

OECD releases third administrative guidance on Pillar Two and confirms delay of the Pillar One timeline

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Authors: [Patrick Marley](#), [Oleg Chayka](#), [Ilana Ludwin](#)

On December 18, 2023, the OECD released the third set of [Administrative Guidance on Pillar Two](#) [PDF] (third administrative guidance) that was approved by the OECD/G20 Inclusive Framework on BEPS (Inclusive Framework) on December 15, 2023.

Pillar Two is part of the [OECD's two-pillar initiative](#) and involves an introduction of a 15% global minimum tax on undertaxed income of large multinational enterprise (MNE) groups. The OECD released the global anti-base erosion (GloBE) model rules on [December 20, 2021](#), and the GloBE commentary and examples on March 14, 2022. The OECD has since published other documents relating to Pillar Two, including two sets of administrative guidance that were released on [February 2, 2023](#), and July 17, 2023.

Notwithstanding the administrative guidance released to date, many uncertainties and ambiguities remain with respect to the interpretation and application of the GloBE model rules. Unfortunately, the OECD does not appear to be able to respond in a timely manner to these interpretive issues. The domestic tax systems of most countries employ thousands of people to audit and administer tax laws in a manner consistent with domestic law. However, a fundamental flaw with Pillar Two is that the rules are intended to be administered on a consistent basis globally without having set up the infrastructure required to make that a reality. Each country must feed their interpretive questions to the OECD, which then must try to form a consensus on how to respond to these questions among the more than 140 countries that are members of the Inclusive Framework. It is simply not feasible for the system to operate quickly — even if the OECD were to be staffed to levels comparable to those of any country's domestic tax administration.

Canada and many other members of the Inclusive Framework have committed to introduce a global minimum tax under Pillar Two. On [August 4, 2023](#), the Department of Finance released a draft of the *Global Minimum Tax Act* (Canada) (GMTA) that proposes to initially implement in Canada two global minimum tax measures — namely, the income inclusion rule and a domestic minimum top-up tax. The GMTA is proposed to apply to fiscal years of qualifying MNE groups beginning on or after December 31, 2023. The Department of Finance has received numerous submissions on the GMTA, including a [submission from Osler](#). It is expected that the Canadian government will release revisions to the GMTA in the first half of 2024. While the GMTA is not expected to be enacted into law in Canada until some time in 2024, it is proposed to have retroactive effect to taxation years beginning on or after December 31, 2023.

The third administrative guidance addresses purchase price accounting adjustments, the transitional CbCR Safe Harbour, consolidated revenue threshold, fiscal year mismatches, allocation of blended controlled foreign corporation (CFC) taxes, transitional filing deadlines for MNEs with short fiscal years and revisions to the Simplified Calculations Safe Harbour rules for non-material entities. It also includes a number of examples to demonstrate the operation of the guidance.

The content of the third administrative guidance will be incorporated into the revised GloBE commentary, which is now set to be released at some point in 2024.

The OECD also published a brief statement on [December 18, 2023 \[PDF\]](#) regarding Pillar One, including its intention to finalise the multilateral convention (MLC) by March 31, 2024, so that the MLC signing ceremony can be held by the end of June 2024. Although the OECD continues to make plans for Pillar One signing ceremonies, there remain significant uncertainties as to whether Pillar One will ever reach the finish line. As a result, Canada has been [moving ahead](#) with its proposal to introduce a digital services tax to backstop a failure to reach an adequate global agreement on Pillar One.

Pillar Two: third administrative guidance

Purchase price account adjustments

The third administrative guidance clarifies that constituent entities may use financial accounts that reflect the effect of purchase price accounting (PPA) adjustments in the computation of profit or loss before tax for transitional CbCR Safe Harbour purposes if both of the following requirements are met:

- The MNE group does not file a CbC Report for a fiscal year beginning after December 31, 2022, that is based on the constituent entity's reporting package or separate financial statements without the PPA adjustments. (This requirement does not apply to constituent entities that are required by law or regulation to revise the reporting package or separate financial statements and to reflect therein PPA adjustments.)
- A goodwill impairment adjustment is added back for purposes of applying the routine profits test and, subject to some specific rules, the simplified effective tax rate (ETR) test to the extent it reduces income and relates to transactions entered into after November 30, 2021.

The relevant changes implementing this approach are set to be made to the transitional CbCR Safe Harbour rules in the Safe Harbours and Penalty Relief document that was released by the OECD in December 2022 (2022 SH document). The latter document will eventually be incorporated into the revised GloBE commentary.

Transitional CbCR Safe Harbour

The transitional CbCR Safe Harbour enables qualifying MNE groups to apply simplified safe harbour tests based on information contained in the Qualified CbC Reports and Qualified Financial Statements, as explained in the 2022 SH document.

The third administrative guidance clarifies the design and operation of the transitional CbCR Safe Harbour rules in respect of joint ventures, use of qualified financial statements, simplified ETR calculations, application of the routine profits test and treatment of hybrid

arbitrage arrangements.

In particular, it provides that, for transitional CbCR Safe Harbour purposes, separate tested jurisdictions will exist and include only constituent entities of the MNE group, joint ventures and joint venture groups even if those constituent entities, joint ventures and joint venture groups are located in the same jurisdiction.

If a qualifying MNE group is not required to prepare and file a CbC Report, it can still qualify for the transitional CbCR Safe Harbour if it fills in section 2.2.1.3(a) of the GloBE Information Return using information from qualified financial statements as if the MNE group were required to prepare and file a CbC Report.

Where an MNE group calculates the substance-based income exclusion (SBIE) amount for transitional CbCR Safe Harbour purposes, it must use the same SBIE rates prescribed to be used under the GloBE model rules, including the increased transitional SBIE rates.

Additional guidance is also intended to prevent the transitional CbCR Safe Harbour where it would otherwise be available as a result of one or more hybrid arbitrage arrangements (such as deduction/non-inclusion arrangements, duplicate loss arrangements or duplicate tax recognition arrangements).

Consolidated revenue threshold

To determine whether the €750-million consolidated revenue threshold is met by an MNE group, the revenue amounts can be netted to account for discounts, returns and allowances as long as such netting is both in line with the relevant accounting standard and done before deducting the cost of sales and other operating expenses.

The third administrative guidance clarifies that revenue includes the net realized or unrealized gains from investments that are recorded in the profit and loss statement of the consolidated financial statements as well as income or gains that are presented separately as extraordinary or non-recurring items. If an MNE group presents its gross gains and losses from investments separately rather than as a net amount, the gross losses can only reduce the group's revenues by up to the amount of the gross gains from investments that are included in the group's revenues.

Fiscal year mismatches

Generally, the accounting period used by the ultimate parent entity (UPE) to prepare the consolidated financial statements is the fiscal year for the GloBE purposes. Should some constituent entities use accounting periods that are different from the UPE's accounting period, the unadjusted or adjusted financial results of the constituent entity's fiscal year that are included in the group's consolidated financial statements, as the case may be, should be used for GloBE computations.

If the financial accounts are prepared for an accounting year that is different from the UPE's fiscal year but are not included in the consolidated financial statements due to entity materiality or joint venture considerations, the GloBE computations for the relevant constituent entity, joint venture or joint venture group, as the case may be, should be prepared with reference to the accounting period that ends during the UPE's fiscal year.

Finally, where a constituent entity has different year ends for financial and tax purposes, the adjusted covered taxes should be determined with reference to the methodology used in the

consolidated financial statements (or other applicable financial statements).

Allocation of blended CFC taxes

The first administrative guidance introduced a simplified methodology for allocating U.S. global intangible low-taxed income (GILTI) and similar taxes under blended CFC tax regimes to constituent entities that are located in low-tax jurisdictions where the GloBE jurisdictional ETR is below 15%. The simplified methodology involves determination of a special blended CFC allocation key and is applicable to fiscal years that end on or before June 30, 2027.

The third administrative guidance includes further guidance on

- GloBE jurisdictional ETR that should be used to compute the blended CFC allocation key when multiple GloBE jurisdictional ETRs are computed for the same jurisdiction
- computation of the GloBE jurisdictional ETR for purposes of determining the blended CFC allocation key of an entity located in a jurisdiction for which the MNE group is not otherwise required to compute an ETR by virtue of, for example, application of a safe harbour or the *de minimis* exclusion
- computation of the GloBE jurisdictional ETR for purposes of determining the blended CFC allocation key of non-GloBE entities in situations where there are multiple ETRs computed for the relevant entities in the jurisdiction

Transitional filing deadlines for MNEs with short reporting years

MNE groups that happen to have short reporting years ending before March 31, 2025, will not be required to file their GloBE Information Returns or notifications before June 30, 2026. Effectively, this means that any such short reporting years are treated in the same manner as a normal reporting year that ends on December 31, 2024, and that benefits from the transitional 18-month filing deadline for the first fiscal year that an MNE group becomes in scope of the GloBE rules in 2024.

Simplified Calculations Safe Harbour for non-material entities

The 2022 SH document contained, among other things, the Simplified Calculations Safe Harbour rules for non-material constituent entities (NMCEs) and related simplified CbC-based income, revenue and tax calculations. NMCEs are entities, including permanent establishments, that are not consolidated in the UPE's consolidated financial statements due to their size or materiality but are nonetheless constituent entities for GloBE purposes. A permanent establishment is an NMCE if its main entity is an NMCE.

The third administrative guidance revises the Simplified Calculations Safe Harbour rules for NMCEs so that these rules can be coherently incorporated in the revised GloBE Commentary. It clarifies that the Simplified Calculations Safe Harbour for NMCEs is subject to an annual election that is made for each NMCE rather than for the jurisdiction and provides an example illustrating the operation of the Simplified Calculations Safe Harbour rules for NMCEs.

Pillar One: OECD's statement on timing

On December 18, 2023, the OECD published a brief statement that reiterates the commitment of the Inclusive Framework members to achieve a consensus-based solution for

Pillar One and to finalize the multilateral convention (MLC) by March 31, 2024, so that a MLC signing ceremony can be held by the end of June 2024.

The OECD's statement has two main implications. First, it acknowledges that the MLC will not be finalized and signed by the end of 2023 as per the OECD's announcement made in [July 2023](#). Second, it demonstrates that the OECD is not yet ready to acknowledge the significant possibility that Pillar One will never be finalized. In particular, by its design, Pillar One cannot come into effect without having been adopted by the United States — and it continues to appear very unlikely that the U.S. will enact Pillar One into their domestic law in the near term or at all.

Canada has already [rejected](#) the July 2023 DST moratorium and recently released a revised version of the [Digital Services Tax Act \(DSTA\)](#) in an implementation bill in Parliament. The DSTA delegates to the Governor in Council the right to determine the day on which the DSTA comes into force, provided that the date is not earlier than January 1, 2024. It remains open to the Canadian government to delay the effective date for the DSTA, and strong opposition from the U.S. to the Canadian DST makes such a delay a possibility.

Further reading

For further details on the OECD's two-pillar approach and Canada's commitment to the pillars, please see the Osler updates on

- [October 14, 2020](#) (blueprint reports on international tax Reform – Pillar One and Pillar Two)
- [December 14, 2020](#) (Osler submission on the OECD Pillar One and Pillar Two blueprints)
- [October 12, 2021](#) (statement on the Two-Pillar Solution)
- [December 21, 2021](#) (draft DST legislation)
- [December 23, 2021](#) (GloBE Model Rules)
- [December 22, 2022](#) (transitional and permanent safe Harbours, temporary penalty relief and two consultation papers on the GloBE Information Returns and certainty for the GloBE matters)
- [February 7, 2023](#) (administrative guidance)
- [March 28, 2023](#) (Budget 2023 update on Pillar One and Pillar Two)
- [July 14, 2023](#) (subject-to-tax-rule and Canada's position on DST moratorium extension)
- [August 10, 2023](#) (draft *Global Minimum Tax Act* (Canada) and revised DST legislation)
- [October 2, 2023](#) (Osler submission on *Global Minimum Tax Act* (Canada))
- [November 21, 2023](#) (update on the Canada's plans to introduce a digital services tax in Fall Economic Statement 2023)
- [December 4, 2023](#) (Bill C-59 that includes a revised version of the DSTA and related regulations)