



Two-Pillar Solution: addressing the tax challenges arising from the digitalisation of the economy

Impact Analysis

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Manager
Media and Speeches Unit
The Treasury
Langton Crescent
Parkes ACT 2600
Email: media@treasury.gov.au

Contents

Executive Summary3

Introduction5

Background Information.....5

Problem and consequences from inaction9

Why is government action needed?12

Options13

Impacts21

Consultation31

Recommended option.....38

Implementation38

Document Status45

References.....46

Appendix A: Additional information on OECD consultations48

Executive Summary

The Government, as part of its election commitment platform, has announced a multinational tax avoidance package to ensure multinationals pay their fair share of tax in Australia. This includes a commitment to support the OECD/G20 Two-Pillar Solution to address the tax challenges arising from the digitalisation of the economy.

This Impact Analysis recommends that Australia should proceed with the Government's election commitment to implement the Two-Pillar Solution, starting with the Pillar Two global minimum tax including a Domestic Minimum Tax. These reforms would improve the economic and revenue outcomes of Australia's tax system at the expense of new compliance costs for large multinational businesses.

The Two-Pillar Solution aims to address challenges that governments and multinational businesses are facing with current international corporate tax settings. It has become harder for governments around the world to raise corporate income taxation revenue from large multinationals. This arguably stems from outdated international conventions for corporate income taxation. These conventions were established a century ago and so did not account for today's levels of digitalisation and globalisation. These problems require coordinated government action and cannot be addressed by market forces.

By using digital technologies, large multinationals increasingly have the ability to operate at 'scale without mass' in countries where they earn significant revenues without needing a traditional physical presence. These 'market countries' then have limited ability to collect corporate income tax since this type of tax is generally collected in the countries where a business' employees and assets are based. Under the current system large multinationals have been also able to utilise legal tax planning strategies to shift taxable profits from higher taxing countries to low- or no-tax jurisdictions.


The emergence of 'scale without mass' digital businesses has led to several countries introducing new Digital Services Taxes, which tax revenues, unlike corporate income taxation which is based on profit (revenue minus expenses). In response, the US has expressed their willingness to take retaliatory trade action against countries that impose Digital Services Taxes on US digital companies, which it views as discriminatory. The OECD has warned of the risks for the global economy if a proliferation of Digital Services Taxes leads to 'tit for tat' trade retaliations.

Another response to globalisation and digitalisation has been a 'race to the bottom' for corporate income tax rates where countries have lowered their corporate income tax rates to attract or retain local investments from multinationals. This kind of tax competition erodes the ability of all countries to raise revenue from taxing the profits of multinationals (known as 'base erosion'). It can also give large multinationals a tax advantage over domestic businesses in relatively high tax countries.

In response to these issues, countries from around the world have been negotiating a package of corporate income taxation reforms through the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting. The package is known as the Two-Pillar Solution. Key design parameters for the Two-Pillar Solution were announced in October 2021.

As its name suggests, the Two-Pillar Solution is made up of a Pillar One and Pillar Two.

Pillar One is about ensuring more of the profits of the largest and most profitable multinationals are taxed where the products or services are consumed. While Pillar One is primarily an attempt to address the problem of 'scale without mass', it is also about stabilising the international tax system, to avoid escalating trade tariffs by limiting the spread of Digital Services Taxes.



Pillar Two seeks to establish a global minimum tax on large multinationals. While it is primarily seeking to address the ‘race to the bottom’, it also helps to create a more level playing field between large multinationals and domestic businesses, which do not access the same profit shifting strategies.

Going forward, the options for Australia are to continue towards implementing Pillar One and Pillar Two, or not implement them. The baseline assumption is that the rest of the world will continue to work towards implementing Pillar One and Two, with or without Australia.

Should Australia implement Pillar One we will be allocated new corporate taxing rights on very large and profitable multinationals.

Pillar One also includes a proposal for simplified transfer pricing rules, which aim to provide an agreed methodology for the pricing and calculation of profits from international trade on a commercial arm’s length basis for cross-border transactions between related parties. While negotiations are ongoing, depending on the final model adopted the simplified transfer pricing rules may reduce the amount of profits to be taxed by Australia for some large multinationals. Overall, successful global implementation of Pillar One will also benefit our economy, in that it helps to avert a potential global escalation of trade tariffs.

Should Australia implement Pillar Two and a qualifying domestic minimum tax, it will have new taxing rights on large multinationals where their current taxation arrangements are below the 15 per cent minimum effective tax rates. Implementation is estimated to increase receipts by \$370 million and increase payments by \$111 million over the five years from 2022-23. Successful global implementation of Pillar Two will also be beneficial for our economy, in that it decreases the taxation differential between Australia and other countries, therefore reducing the influence that taxation has on foreign investment decisions. It will also support Australian domestic businesses, by decreasing some of the tax advantages that are available to large multinationals.

Accordingly, the best option for Australia is to proceed towards implementing the Two-Pillar Solution.

Implementation of Pillar Two will primarily involve Australia passing domestic laws that mirror agreed international model rules to bring about global minimum taxation for large multinationals effectively from 2024. With the international model rules agreed, the Government can now progress this legislation.

Implementation of Pillar One will primarily involve Australia signing a new multilateral treaty, which is expected to be ready for signature in 2023, which will be activated once a critical mass of countries has ratified. This is expected to occur in 2024 and will require a Government decision when the treaty is finalised. The full revenue and other implications of Pillar One cannot be determined at this point.

Introduction

The Government as part of its election commitment platform, announced a multinational tax avoidance package to ensure multinationals pay their fair share of tax in Australia. This included a commitment to support the OECD's Two-Pillar Solution. The Two-Pillar Solution is made up of Pillar One, which is about ensuring more of the profits of the largest multinationals are taxed where the products or services are consumed; and Pillar Two, which seeks to establish a global minimum tax on large multinationals.

This document examines the impacts and manner of implementation of the Government's election commitment.

Background Information

Corporate Income Taxation

Corporate income taxation generally refers to taxes on business profits (revenues minus expenses). In contrast to personal income taxes, corporate income tax is collected from businesses, rather than from the individuals who own them. This type of taxation is a common feature of most countries' tax systems.

As with any tax, there are different perspectives on the role of corporate income taxation. One view justifying why we have corporate income taxation is that it exists as an integrity measure for the personal income taxation system, which can have difficulty in adequately taxing wealthier individuals, who may be able to use company structures to reduce their personal income tax. In this way, having a corporate income tax can result in more revenue being collected more fairly across a population of business owners and non-business owners. However, the purpose of corporate income taxation is more complex when it comes to businesses operating across multiple countries, as they have access to multiple strategies to shift profits to low tax jurisdictions. Over time, the ability to profit shift can lead to an erosion of a jurisdiction's tax base, as more and more taxable business entities or activities relocate to jurisdictions with low- or no-taxation. This can occur even when legal profit shifting strategies are used.

OECD and G20 negotiations

Following the financial crisis in 2008, the OECD and G20 countries prioritised addressing global tax issues, the most pressing of which was corporate taxation. This included an [Action Plan to address Base Erosion and Profit Shifting \(BEPS\)](#), which led to the formation of the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting in 2016. Under the Inclusive Framework more than 130 countries and jurisdictions are collaborating with the aim of minimising tax avoidance strategies that exploit gaps and mismatches in tax rules to avoid paying tax. Much of the original BEPS Action Plan has now been implemented, however, the work on the tax challenges from digitalisation (Action One) continues to be progressed (and expanded on) as part of the proposed OECD/G20 Inclusive Framework Two-Pillar Solution.

Multilateral action to address digitalisation

While the existing BEPS multilateral measures are important as integrity measures, they do not fully address the core tax challenges relating to digitalisation, the ‘race to the bottom’, and ‘scale without mass’ (explained in the problem section).

The original motivation for the Two-Pillar Solution to reform the international corporate tax system was the emergence of highly digitalised multinationals – which exacerbated some of the longer-standing challenges associated with taxing corporate profits in a globalised economy, such as profit shifting. Concerns have also been growing about the use of low- or no-tax jurisdictions, sometimes referred to as ‘tax havens’, and the tax planning opportunities they present to some multinationals.

While one of the original focus areas of the OECD/G20 Two-Pillar project was the emergence of specific multinational digital business models, it has since broadened in scope to potentially affect all large multinationals.

Through the [OECD’s public consultation process in 2020](#),¹ economic analysis was released predicting that the continued build-up of these pressures and the proliferation of unilateral actions, such as Digital Services Taxes, could harm global economic growth.² The OECD argued that a better alternative is the Two-Pillar Solution being negotiated through the Inclusive Framework.

OECD Inclusive Framework members released a [statement](#) on 1 July 2021,³ which was updated on 8 October 2021, and was accompanied by a [detailed implementation plan](#).⁴

The OECD Inclusive Framework approach to addressing the tax challenges of international corporate taxation has focused on two separate policy streams, known as the Two Pillars.

- Pillar One primarily seeks to relocate some of the profits from the largest and most profitable multinationals to countries where the goods and services are actually consumed.
- Pillar Two primarily seeks to set an effective global minimum corporate tax rate of at least 15 per cent.

In designing a solution, the OECD is trying to develop a consensus that will be acceptable for all OECD Inclusive Framework members. This is a challenging project due to competing interests between more than 130 countries.

¹ Organisation for Economic Co-operation and Development (2020), Public Consultation Document – Reports on the Pillar One and Pillar Two Blueprints 12 October 2020 – 14 December 2020

² Organisation for Economic Co-operation and Development (2020), Tax Challenges Arising from Digitalisation – Economic Impact Assessment

³ Organisation for Economic Co-operation and Development (2021), Statement on a Two-Pillar Solution to Address the Tax Challenges Arising From the Digitalisation of the Economy, 1 July 2021

Organisation for Economic Co-operation and Development (2021), Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy, 8 October 2021

Domestic actions by Australia

The Australian Government is committed to closing loopholes exploited by multinationals and to improving transparency of their business arrangements.

The Government has committed to ongoing engagement on the multilateral Two-Pillar Solution and to implement a multinational tax avoidance package. As part of this commitment, the Government is progressing a set of measures which targets the deliberate activities of multinationals to minimise tax. These measures also enhance public reporting (transparency) initiatives to maintain public trust in the tax system.

The Government's commitments in this area of taxation build on Australia's response over the last decade to address tax planning and profit shifting arrangements. Australia's response has been substantially increased by the Australian Taxation Office's (ATO) enforcement mechanisms, including penalty type regimes to urge multinationals to better align their profit reporting system to reflect the actual location of their economic activities. However, given the global nature of these issues, efforts by one country in isolation to address profit shifting will have a limited effect.

Australia has long been a strong and active supporter of the BEPS Project. Australia has been vigilant in implementing the BEPS recommendations, including ensuring our transfer pricing laws remain world's best practice; implementing full Country-by-Country reporting (CbCR); adopting a range of integrity rules in our tax treaties through the Multilateral Instrument; and introducing new rules to prevent tax avoidance through hybrid mismatches.

Following the United Kingdom's lead, in 2015, Australia introduced domestic measures targeting international tax avoidance. These measures including implementing the Multinational Anti-avoidance Law (MAAL) and Diverted Profits Tax (DPT), doubling penalties for multinationals that seek to avoid tax, imposing tax conditions on foreign investors, strengthening thin capitalisation laws, establishing the Tax Avoidance Taskforce and establishing a domestic Voluntary Tax Transparency Code. In addition, Australia has enhanced whistle-blower protections for individuals to report tax misconduct to the ATO.

The MAAL seeks to address artificial arrangements designed to avoid a taxable presence in Australia. This is an integrity measure that allows the cancellation of certain tax benefits received by significant⁵ global entities and their related parties. The Government's implementation of the MAAL encouraged many large businesses to restructure their operations to be compliant with the law. These restructures have resulted in more than \$8 billion additional taxable sales being booked in Australia.⁶

Australia extended the GST to imported digital products and services (1 July 2017), low value imported goods (1 July 2018), and to offshore sellers of hotel bookings (1 July 2019). These are not considered to be Digital Services Taxes. This is because the GST is a consumption tax with a broad base that taxes value-add amounts and does not discriminate against non-residents.

⁵ Significant in this context means a global parent entity with an annual global income of A\$1 billion or more with related parties. Per Australian Taxation Office (2021), Significant global entities – penalties.

⁶ Australian Taxation Office (2020), Tax Avoidance Taskforce highlights 2019-20

The DPT is an integrity mechanism that aims to ensure that tax paid by significant global entities reflects their activities in Australia and prevents the diversion of profits offshore. It allows the Commissioner of Taxation to assess a taxpayer's diverted profits, with respect to economic substance and contrived arrangements. The tax is imposed at the rate of 40 per cent on the assessed diverted profits. The rate of 40 per cent is effectively an additional penalty rate of 10 per cent on top of Australia's headline corporate income tax rate.

Australia has also implemented several budget measures that provide additional funding to the ATO to conduct more compliance activities covering multinationals.⁷

Historical conventions of the international corporate income tax system

A business that has a presence across multiple jurisdictions is known as a multinational. Determining income tax liability for a multinational is much more complicated compared to individuals or local businesses. This is because it involves assessing the income of legally separate, but related (through ownership or other interests), parties that operate under different rules in separate legal jurisdictions, with each jurisdiction having their own accounting, taxation, and transparency rules, as well as treaties between countries that can further impact the applicable taxation rules.

A framework has been established, through tax treaties and transfer pricing guidelines, to allocate corporate taxing rights among the countries where the value is added (i.e., where the profits were generated) in the supply chain.

The international corporate taxation system has been designed on a principle that profits are taxed based on concepts of permanent (physical) presence of a business where it operates. Arguably, such a notion has reduced relevance in a digital economy, which has led to views that existing conventions are "outdated".

This concept of value creation considers where and how a business is funding, developing, producing, and selling its products, rather than simply where its goods or services are finally consumed. Much of this practice traces back to 1923, when the Financial Committee of the League of Nations commissioned a report into double taxation to resolve disputes.

Currently, the international taxation system is structured in three parts: the 'source' country where the production of economic activity occurs; the 'residence' country where the ownership of the firm resides; and the 'consumer' country where the products (goods or services) are ultimately consumed. Traditionally, taxation on the consumption of products is addressed in 'consumer' countries through consumption taxes like a Value Added Tax (VAT) or Goods and Services Tax (GST) and the taxation of profits (i.e., taxable income) is shared between the 'source' and 'residence' countries.

More recently, with the digitalisation of the economy and growing amount of value being derived from intellectual property, exactly where the value is added in a true economic sense (as opposed to legal concepts) has become harder to establish. Old conventions are becoming challenged, and many countries are now starting to impose new taxes on corporate revenues, not just profits.

⁷ [Australian Government, Budget 2022-23 Budget Paper No. 2](#)

Problem and consequences from inaction

The ‘race to the bottom’ to reduce corporate tax rates

In recent decades, there have been concerns with a potential ‘race to the bottom’ in corporate tax rates, where countries compete with each other in order to attract investment of global capital – and possibly also headquarters of multinational firms. This ‘race to the bottom’ reduces the tax paid on the economic activity of multinational firms.

Multinationals care about after-tax returns, so if a country has a higher tax rate, this will be one of the factors in their decision making on where business activity will be undertaken. When countries are incentivised to lower taxes to attract and retain international investment from multinationals, it ultimately erodes the ability for all countries to generate corporate income tax revenue.

If globalisation and digitalisation trends continue, more and more of Australia’s consumption will be derived from large multinationals, who will increasingly centralise their profitable activities in low- or no-tax jurisdictions – outside of Australia in countries where the corporate tax rate is lower than the corporate tax rate in Australia. In this way, the continued ‘race to the bottom’ could further erode Australia’s ability to raise revenue from corporate income taxation.

Multinationals’ ability to have ‘scale without mass’

While globalisation and digitalisation of the economy have been greatly beneficial in growing the economy and improving living conditions through access to opportunities and consumption of a broad set of goods and services, it has also made profit shifting strategies much easier for multinationals to implement in scale and scope.

The ability to derive significant profits from a country without having the traditional physical presence (mass) presents challenges to governments seeking to raise revenue. For example, businesses can more easily relocate their profits to preferred jurisdictions via licensing agreements and intellectual property arrangements to minimise taxation. They can also contract directly with customers from a foreign country. This enables businesses to engage in cross-border sales with little physical presence in a jurisdiction.



New value creation through network effect from customers



In the context of the Two-Pillar negotiations some countries have raised whether digitalisation means that customers themselves are now adding value, through their participation - and the subsequent collection of their data – and whether this value add is appropriately taxed. Questions about who owns data or data rights are not fully resolved and will continue to be public policy issues that will be debated into the future.

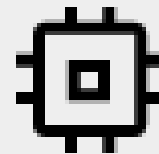
Currently, the international corporate taxation system has been designed on a principle that profits are taxed based on concepts of permanent (physical) presence of a business where it operates. Arguably, such a notion has reduced relevance in a digital economy.

However, in a digital economy, the existing boundary issues over which country a product's value was added in, or where in the supply chain the profit was generated, has been amplified. This is because it can be very hard to clearly identify the internal economy of a large vertically integrated and geographically dispersed digital business, such as determining the fair value of intellectual property licenses, meaning that digital businesses are even better placed to exploit profit shifting strategies, compared to the traditional trade of tangible goods.

A growth in the ability for multinationals to have 'scale without mass' will further erode Australia's ability to raise revenue from corporate income taxation.

Economic benefits of globalisation and the digital economy

When considering the tax challenges that digitalisation and multinationals create for the corporate income taxation system, it is important to keep in mind the significant economic benefits that they also bring.



In general, countries that allow international trade and multinational businesses enjoy access to better and cheaper products and more lucrative investment, employment and business opportunities. These benefits have driven significant globalisation over time. The relatively recent emergence of the digital economy has continued this trend, with highly digitalised businesses now operating around the world.

For example, advertising through services owned by multinationals such as Alphabet (Google) and Meta (Facebook) gives small businesses in Australia a significantly cheaper and more effective way to target their advertising than traditional mediums. This results in less costs being passed on to end-consumers, while also supporting increased competition, which also generally results in lower prices to win over customers.

Online marketplaces that act as intermediaries between sellers and buyers lower traditional search costs and facilitate greater competition between manufacturers, accommodation providers, transport providers and in trade services. Digital content providers support competition with traditional media and entertainment channels as well as the traditional telecommunications market.

Digital Services Taxes and trade considerations

The 'race to the bottom' and 'scale without mass' challenges both act to erode the ability of governments to raise revenue from corporate income tax. In response, governments around the world will continue to consider new options to raise revenue.

Digital Services Taxes are intended to address the challenges of 'scale without mass' concerns by local businesses that there is an uneven playing field with large multinationals, and observations around high levels of user participation. Most of these Digital Services Taxes are, in practice, a revenue tax on the domestic operations of large digital businesses' advertising sales. Digital Services Taxes are considered by the OECD Inclusive Framework to be unilateral actions (actions taken individually by jurisdictions).

The introduction of Digital Services Taxes globally has led the OECD to highlight the risk that the proliferation of Digital Services Taxes and other similar measures could lead to escalating trade tariffs.

The United States Trade Representative has made determinations in its assessment of a number of these taxes that they are discriminatory against US businesses. The US has further threatened retaliatory tariffs on imports for a number of countries which are considering or have implemented Digital Services Taxes, including France, the United Kingdom, Spain, Italy, Canada and Austria. The United States' tariffs were then suspended to allow the OECD multilateral negotiations to continue efforts to finalise the Two-Pillar Solution.

These threats include imposing levies of 100 per cent on US\$2.4 billion worth of French goods if France decides to maintain its Digital Services Tax.

Around 42 countries have announced or passed legislation in relation to Digital Services Taxes, with varying scopes, thresholds and rates. The US Trade Representative has initiated investigations into the planned digital tax regimes of at least ten jurisdictions. The pace of these announcements has escalated as political demand for action is growing, which is an indication of the complexity that will arise for businesses in the absence of a global deal.

OECD modelling on the impacts from a proliferation of Digital Services Taxes and other similar measures

The OECD in their blueprint analysis undertook economic modelling of the world implementing the Two-Pillar Solution, which they called a 'consensus' scenario, and of the world without the Two-Pillar Solution, called the 'no consensus' scenario. In the no consensus scenario, the world economy is damaged from increasing tax and trade retaliations involving Digital Services Taxes and trade tariffs.


As the behavioural decisions of countries is highly uncertain, the OECD modelled a narrow Digital Services Tax scenario, and a scenario where Digital Services Taxes are implemented more broadly. The magnitude of these adverse effects would notably depend on the number of jurisdictions introducing Digital Services Taxes, the design and rate of these Digital Services Taxes, and the scale of the tariff retaliation and potential subsequent tariff counterretaliation by jurisdictions targeted by tariffs. Under stylised scenarios with 'narrow' Digital Services Tax implementation (i.e. only focusing on jurisdictions currently under section 301 investigation by the United States), it is estimated that the negative effect on global GDP could reach -0.1 per cent to -0.2 per cent. In scenarios with broader Digital Services Tax implementation, the negative effect on global GDP could reach -0.4 per cent to -1.2 per cent.⁸ The OECD has also argued that the continued proliferation of Digital Services Taxes will increase compliance costs on businesses, given each country will take slightly different approaches to their adoption.

Equity and Level playing field concerns

Without action there may be a reduction in the ability for small domestic businesses to compete equally with large multinationals, because multinationals can use profit shifting strategies to lower tax burdens and overall costs.

One of the key objectives of a well-designed tax system is to achieve a certain level of horizontal and vertical equity. Simplistically, vertical equity means that those earning higher income should pay

⁸ Organisation for Economic Co-operation and Development (2020), Tax Challenges Arising from Digitalisation – Economic Impact Assessment



proportionally more tax than those on lower incomes. Horizontal equity means those earning the same income should pay the same level of tax.

A lack of horizontal equity creates an uneven playing field in a competitive market. Simply, businesses that have the ability to pay less tax on their income can undercut other business. Over time, this lowers competition, which may be bad for economic efficiency and consumer outcomes.

In relation to corporate taxation, multinationals generally have unfair advantages over solely domestic based Australian businesses, as multinationals typically have access to additional tax minimisation strategies that are enabled from cross-border transactions with related parties. Multinationals can also take advantage of other deliberate tax concessions, such as lower tax rates specified in tax treaties and more generous capital gains taxation exemptions, which are generally designed to attract foreign investment.

Why is government action needed?

Government action is needed to implement an election commitment to support the OECD/G20 Two-Pillar Solution to address the tax challenges arising from the digitalisation of the economy.

At the global level, Government action is needed as the market acting alone will not solve the challenges in the international tax system. In fact, the market-based tax minimisation incentives for multinationals are likely to lead to the problems of the 'race to the bottom' and 'scale without mass' only becoming larger. The market can also not effectively coordinate agreement on the design of a new tax system given the vested interests of incumbent multinationals in maintaining the status quo.

The success of the Two-Pillar Solution can be judged to the extent it addresses the following objectives:

- Ensuring multinationals pay a fairer share of tax globally and are appropriately taxed in proportion to their economic activity;
- Equity and level playing field concerns;
- Sustainability of the corporate tax base;
- Economic efficiency;
- Promoting the stability of and consistency in the international tax system;
- Facilitation of international trade;
- Providing acceptable levels of business certainty;
- Avoiding excessive overlap in the allocation of taxing rights between jurisdictions; and
- Facilitation of foreign investment.

Options

The options focus on whether or not to implement the Government’s election commitment to implement the Two-Pillar Solution. The Two-Pillar Solution is a multilateral agreement brokered through the OECD/G20 to address the tax challenges arising from the digitalisation of the economy.

With so much momentum to date around the Two-Pillar Solution, and more than 130 countries committing to key design principles in July and October 2021, the assumption at this stage is that the Two-Pillar Solution will likely be implemented by other countries, with or without Australia.

Government decisions on different aspects of the Two-Pillar Solution are needed at different times based on specific implementation mechanisms and timeframes. On this basis, the options below separate Pillar One from Pillar Two, although the Government’s election commitment and the Inclusive Framework statement view both Pillars (and their constituent elements) as a package.

Option 1: Australia to implement Pillar One

Pillar One Summary	
What does it do?	Reallocates corporate income taxation rights towards countries where the end consumers are located.
What do multinationals do differently?	Multinationals will need to complete a new global tax return, and more closely track the location of their customers.
Who is in scope?	Multinationals who have greater than EUR20 billion revenue per annum and also have a profit to revenue ratio exceeding 10 per cent.
Major exemptions?	Extractive Industries, Regulated Financial Services and Government enterprises.

Pillar One Cameo

Megacorporation has customers in nearly every country in the world, has large revenues and is highly profitable. To minimise global taxation, Megacorporation has consolidated the majority of their intellectual property and intangible assets in a low-tax jurisdiction (also known as an investment hub). The legal entity operating in the investment hub uses a profit shifting strategy of charging high fees to Megacorporation's subsidiaries operating in higher taxing countries, generally where customers are located.

Once in scope of Pillar One, Megacorporation will need to file a new type of global tax return. The new global tax return will then be used to assign a portion of Megacorporation's profits to be taxed in the countries according to where revenue was derived (where consumers are located). This is opposed to the existing corporate tax system, that generally allocates taxing rights based on where profits are legally reported within Megacorporation's businesses.

For a country that has consumers (also known as a 'market jurisdiction') they may have additional taxation rights allocated to them (known as Amount A). Investment hubs will have reduced taxing rights, as they will be expected to relieve double taxation. From Megacorporation's point of view, they pay slightly more tax overall, as some of the taxing rights on their profits are shifted from low-tax jurisdictions to generally higher taxed market jurisdictions.

Megacorporation will not have to pay any Digital Services Taxes, as to receive the new Amount A taxing right, countries must remove and commit not to introduce a Digital Services Tax. In addition, Megacorporation also benefits from improved Tax Certainty processes, by streamlining the resolution of some of their tax disputes with individual countries.

PILLAR ONE BUILDING BLOCKS

The implementation plan agreed by the OECD Inclusive Framework in October 2021 includes reference to several building blocks for Pillar One.

Scope refers to which multinationals the new taxing right applies. This is set at global turnover above EUR20 billion and profit to revenue ratio above 10 per cent (with profit above this level referred to as 'residual profit'). Extractive and Regulated Financial Services are excluded.

Nexus refers to the revenue threshold before a country is eligible to receive the new taxing right. This is set at EUR1 million for most countries but lower for smaller economies.

Quantum refers to the size of the new taxing right. Which is 25 per cent of the profit above the 10 per cent profit to revenue ratio. As the Quantum is a percentage of a percentage, this means that only a minority of the total taxing rights are being redistributed.

Revenue Sourcing refers to the mechanism to determine how much profit countries are allocated under the new taxing right. This is determined based on the end market jurisdictions where goods and services are consumed.

Tax base refers to rules for how global profit is calculated. It has been agreed this will be based on the existing global financial accounting reports produced by multinationals, with a limited number of adjustments.

Under this option, Australia would enter into a Multilateral Convention (treaty), along with all other major countries, so as to create a global redistribution of corporate income taxing rights.

The Multilateral Convention aims for a fairer distribution of taxing rights among jurisdictions over the largest and most profitable multinational enterprises. More specifically, it:

- Seeks to redesign the international income tax system to adapt to new business models and taxation challenges, by making changes to the outdated profit allocation rules; and
- Attempts to expand the taxing rights of market jurisdictions (where the consumer is located).

The existing design will remain and be supplemented with a new reallocation of taxing rights over multinationals' profits, reallocating from investment hubs to market jurisdictions.

This will help to address the problem of 'scale without mass', where a company can make profits while paying little to no income tax in the jurisdiction where the good or service is consumed.

Key elements of Pillar One include:

- Reallocation of certain taxing rights over large and highly profitable multinationals to market jurisdictions where their users and customers are located (Amount A).
- Streamlined application of transfer pricing rules (based on the arm's length principle) to in-country baseline marketing and distribution activities (Amount B).

Reallocation of taxing rights (Amount A)

This would involve large and highly profitable multinationals being required to undertake a number of formulaic steps, the key ones being to determine whether they are in scope for Amount A, determining the tax base, assessing the quantum of re-allocations and attributing revenue to markets.

The amount of taxing rights to be redistributed under Pillar One is known as 'Amount A'. This redistribution would only apply where a multinational has global revenues exceeding EUR20 billion per annum and a profit before-tax to revenue ratio exceeding 10 per cent. The OECD has estimated that around 100 multinationals would be in the scope of Pillar One initially.

There is an exclusion for Extractives and Regulated Financial Services from the scope of Amount A. These exclusions reflect the policy goals of retaining source country taxing rights over economic rents from location-specific non-renewable extractive resources and returns by financial firms subject to regulated capital adequacy requirements (or similar internationally recognised regulatory regimes).

Amount A is equal to 25 per cent of the multinational's global residual profits. For the purpose of Amount A, global residual profit is defined as all profit above a 10 per cent profit to revenue ratio. For example, if a company had a total profit of \$15, and total revenue of \$100, then residual profit would be \$5, and the size of Amount A would be \$1.25. The multinational would then allocate these Amount A profits among market jurisdictions based on the proportion of their revenue sourced from each jurisdiction. The market jurisdiction would then apply their domestic corporate tax system to tax the allocated residual profits, while another 'relieving jurisdiction' would be required to effectively relinquish their taxing rights over these profits (also referred to as elimination of double taxation). Pillar One would also include a 'Marketing and Distribution Profits Safe Harbour' to cap the amount of profit reallocated to a market jurisdiction that is already able to tax the multinational's residual profits.

As a condition of joining Pillar One, countries need to remove all Digital Services Taxes and commit to not introducing similar measures in the future. This would help stabilise the international tax rules and reduce the risk of trade disputes.

Streamlined application of the arm's length principle (Amount B)

Amount B aims to simplify and streamline the process of applying transfer pricing rules under the arm's length principle for "baseline marketing and distribution activities", with a particular focus on the needs of low-capacity jurisdictions (relating to the capacity to administer complex taxation law). Baseline marketing and distribution activities essentially amounts to the downstream advertising, transport and retailing of the goods or services that typically occur near customers. Amount B is not limited to the multinationals in scope of Amount A. The details of Amount B are still being negotiated.

PILLAR ONE BUILDING BLOCKS

Segmentation refers to situations where the multinational may be split up for the purposes of calculating the profitability. To be used in situations where a large multinational has business groups of varying profitability.

Marketing Distribution Profits Safe Harbour is the mechanism that will cap an allocation of new taxing rights, where a country is already taxing 'residual profits'.

Elimination of Double Taxation is the mechanism for deciding which countries give up taxing rights to be reallocated to other countries. This has been determined to be the countries that capture the most 'residual profit'.

Tax Certainty refers to a new dispute resolution and prevention mechanism.

Administration refers to the filing of the global tax return. Which can be a single entity within the multinational group.

Unilateral Measure refers to Digital Services Taxes and other similar measures. It has been determined countries will need to remove Digital Services Taxes to receive the new taxing right.

Implementation is the legal enforcement mechanism. Which has been determined as a Multilateral Convention.

Option 2: Australia to implement Pillar Two

Pillar Two Summary	
What does it do?	Primarily allows countries which implement Pillar Two to apply a top-up tax on multinationals where they are taxed below the global minimum rate.
What do multinationals do differently?	Complete a new global information return, as well as other reporting requirements to meet the new rules and possibly pay top-up taxes.
Who is in scope?	Multinationals who have global revenue of at least EUR750 million.
Major exemptions?	International shipping, Government enterprises and pension funds.

Pillar Two Cameo

Megacorporation operates in nearly every country in the world, has large revenues and is highly profitable. To minimise global taxation Megacorporation has consolidated the majority of their intellectual property and intangible assets in a low-tax jurisdiction. The legal entity operating in the low-tax jurisdiction then charges fees to Megacorporation’s subsidiaries in other higher taxing countries.

Once in scope of Pillar Two, Megacorporation will need to file a new type of global information return. The new global information return would indicate whether they are paying tax above or below the global minimum rate of 15 per cent in each jurisdiction in which it operates. If they are being taxed below the global minimum, they will be required to pay top-up taxes in up to the point where they are paying the minimum global tax rate in each jurisdiction.

For high taxing countries there may be situations where they can increase their taxation revenue through the collection of top-up taxes. However, low-tax jurisdictions may respond by increasing their tax rates, as companies operating in their country will be charged top-up taxes by other countries anyway, so they may as well tax them instead.

Megacorporation will pay an overall higher amount of taxation where it does not pay the minimum rate in jurisdictions. Additionally, as Pillar Two has in effect put a floor on tax competition, it will partly reduce the financial benefits for Megacorporation to undertake profit shifting activity.

Pillar Two Key elements

The implementation plan agreed by the OECD Inclusive Framework in October 2021 included the overall design for Pillar Two.

Global anti-Base Erosion Model Rules, which include:

(i) an **Income Inclusion Rule**, which imposes top-up tax on a parent entity in respect of the low taxed income of a constituent entity in another jurisdiction; and

(ii) an **Undertaxed Payment Rule**, which denies deductions or requires an equivalent adjustment to the extent the low-tax income of a constituent entity in another jurisdiction is not subject to tax under an IIR.

The GloBE Model Rules will operate to calculate the **effective tax rate** on a jurisdictional basis using a common definition of covered taxes and a tax base determined by reference to financial accounting income.

The **minimum tax rate** used for purposes of the IIR and UTPR will be 15% and the GloBE Model Rules will operate to impose a top-up tax where the effective tax rate falls below this rate.

Separately, Pillar Two also has a treaty-based rule (**the Subject to Tax Rule**) that allows source jurisdictions to impose limited source taxation on certain related party payments subject to tax below a minimum rate.

Under this option, Australia along with other major countries would implement domestic legislation that brings about a common approach to under taxation.

Pillar Two is intended to address the 'race to the bottom' where countries are competing with each other to attract mobile capital through offering lower corporate tax rates. Pillar Two does not explicitly mandate that any country increase their corporate tax rate, rather it creates incentives for countries to do so on their own accord. It does this by granting countries the right to tax the profits of entities within a large multinational group where the group operates in a particular jurisdiction and the effective tax rate of that jurisdiction falls below the globally agreed minimum tax rate.


The Global anti-Base Erosion Rules (GloBE) Model Rules will determine whether an entity is undertaxed in a jurisdiction by calculating their effective tax rate. To make compliance simpler, safe harbours and carve-outs from the GloBE Model Rules will be provided, including for substantive tangible assets and payroll and for entities with minimal financial presence.

The stated objective for Pillar Two is that it seeks to ensure that all large and internationally operating businesses pay at least a minimum level of tax globally. More specifically, Pillar Two seeks to put a floor on tax competition on corporate income tax through the introduction of a global minimum corporate tax rate. Pillar Two sets multilaterally agreed limitations on tax competition.

The October Statement⁹ set this minimum rate at 15 per cent. This is an effective tax rate, which would take into account incentives provided to multinationals that lower their effective tax rates below a jurisdiction's headline tax rate. For example, a country with a headline tax rate of 20 per cent that provides tax concessions could have an effective tax rate lower than 15 per cent for some multinationals.

The GloBE Model Rules will apply to multinational groups with consolidated revenues of at least EUR750 million. It will not apply to entities that

⁹ Organisation for Economic Co-operation and Development (2021), Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy, 8 October 2021



already pay low- or no-tax for public policy reasons (e.g. government organisations, certain investment funds, pension funds and non-profit organisations). Income from international shipping operations and some related activities will also be excluded.

Implementation of Pillar Two would require domestic legislation to implement the GloBE Model Rules. It would also involve a treaty to implement a Subject to Tax Rule (STTR).

Global anti-Base Erosion (GloBE) Model Rules

The GloBE Model Rules consist of two interlocking rules: the Income Inclusion Rule (IIR) and the Undertaxed Payments Rule (UTPR). These rules are designed to collect a top-up tax on profits undertaxed in jurisdictions in which a multinational operates. These rules are discussed in more detail below.

The OECD Inclusive Framework has released the GloBE Model Rules, Commentary and Examples to inform the design of domestic legislation. An Implementation Framework, addressing high priority implementation and administration issues has also been released. Administrative guidance on issues not critical for domestic implementation will continue to be published by the Inclusive Framework in an ongoing manner.

The GloBE Model Rules also allow, but do not require, a jurisdiction which implements the rules to claim primary rights over the collection of any top-up tax on undertaxed profits in that jurisdiction. This can be achieved by that jurisdiction implementing a Domestic Minimum Tax to prevent local under-taxation.

Income Inclusion Rule (IIR)

The IIR would allow jurisdictions to apply a top-up tax on a resident multinational ‘parent’ company, where the group’s income in another jurisdiction is being taxed below the global minimum rate of 15 per cent. For example, if a multinational had its headquarters in Australia, but its foreign subsidiaries in a particular jurisdiction were paying an effective tax rate of 10 per cent, Australia may be able to apply a top-up tax on the Australian parent company equivalent to 5 per cent of the foreign subsidiaries’ profits.¹⁰

Undertaxed Payments Rule (UTPR)

The UTPR would allow jurisdictions to apply a top-up tax on a resident subsidiary member of a multinational group if the group’s income in another jurisdiction is being taxed below the global minimum rate of 15 per cent and where no IIR applies. For example, if a multinational subsidiary in Australia had a foreign related entity paying less than the global minimum rate on its profits,¹¹ and there was no foreign jurisdiction applying the IIR in relation to those profits, then Australia may be able to apply the UTPR to the Australian subsidiary in respect of the under-taxation in the related entity’s jurisdiction. Top-up tax would be allocated using substance-based allocation factors among countries in which the multinational group operates and that have implemented the UTPR. Broadly, a country with proportionately more tangible assets and employees will receive a larger allocation of the UTPR top-up tax.

¹⁰ Subject to any exclusions and reductions.

¹¹ Subject to any exclusions and reductions.

Should Australia implement a Domestic Minimum Tax?

A sub-option in implementing Pillar Two is whether or not to introduce a Domestic Minimum Tax.

The GloBE Model Rules allow, but do not require, a jurisdiction which implements the GloBE Model Rules to adopt a Domestic Minimum Tax, giving the jurisdiction the first claim to additional taxing rights on any low-taxed domestic income.

Should Australia not introduce a Domestic Minimum Tax, then other countries could potentially gain corporate taxing rights over Australia's undertaxed profits. This would happen in certain situations where Australia's tax system taxes at an effective rate of at least 15 per cent, possibly due to tax concessions and incentives built into the system. As such there is a strong financial incentive for Australia to have a Domestic Minimum Tax since it would allow Australia to collect tax that would otherwise be collected by other jurisdictions.

It will be important that the Domestic Minimum Tax is implemented in a way that is consistent with the outcomes under the GloBE Model Rules, known as a Qualified Domestic Minimum Tax. Designing a Domestic Minimum Tax on a different basis could mean that it is non-qualified. Adopting a Qualified Domestic Minimum Tax will help lower compliance costs as well as reduce the risk other countries could take taxing rights from Australia.

Subject to Tax Rule (STTR)

The STTR is primarily intended to overcome concerns faced by developing countries that have entered into bilateral tax treaties, which have reduced their taxing rights on certain related-party income. The STTR allows those developing countries to regain such taxing rights by allowing them to tax up to the STTR minimum rate of 9 per cent, when such income is taxed below that rate.

If an Inclusive Framework member country is taxing certain income below this STTR minimum rate,¹² it is obligated to include an STTR into its bilateral tax treaty when requested to do so by the developing country treaty partner. If an STTR is included in an existing bilateral tax treaty then, broadly, the payer jurisdiction may additionally tax certain related-party payments on its gross amount where the payee jurisdiction has taxed the payment below the STTR minimum rate. This taxing right will be limited to the difference between the STTR minimum rate and the tax rate on the payment.

Option 3: Australia to not implement Pillar One

Under this option, Australia would not implement Pillar One. It is currently assumed that the remaining OECD Inclusive Framework members would continue to work towards implementation of Pillar One.

Option 4: Australia to not implement Pillar Two

Under this option, Australia would not implement Pillar Two. It is currently assumed that the remaining OECD Inclusive Framework members would continue to work towards implementation of Pillar Two.

¹² Calculated on an adjusted nominal basis.

Impacts

Impact on Australia from implementing Pillar One

Pillar One revenue impacts

With a number of detailed design elements yet to be settled, it is too early to formalise a revenue impact estimate for Australia regarding Pillar One at this stage.¹³ Australia remains actively involved in the OECD negotiations.

Because there will be a net transfer of taxing rights from lower tax jurisdictions to higher tax jurisdictions, global tax paid is expected to increase. The OECD has estimated that the average percentage revenue gains from Pillar One may be greater for low-income countries than the gains for middle- and high-income countries.

At this stage, the extent to which Australia would benefit from the estimated reallocation remains dependent on factors still under negotiation, such as the Marketing and Distribution Profits Safe Harbour and Elimination of Double Taxation mechanisms. There are also theoretical impacts to revenue from positions that could be overturned through arbitration under the new Tax Certainty process of issues related to Amount A. In addition, there could also be revenue impacts from Amount B (transfer pricing simplification) to the extent negotiated changes become mandatory.

Pillar One economic impact

Benefits


Ordinarily, higher taxation on its own can be expected to decrease economic output. However, the OECD analysis indicates that if Pillar One can help avoid the current proliferation of uncoordinated unilateral tax measures (e.g. Digital Services Taxes) as well as prevent damaging tax and trade disputes, it will have a net positive impact on the global economy.¹⁴ The OECD has estimated that the negative economic implications of a protracted tax and trade related conflict would reduce global GDP from somewhere between 0.1 per cent to 1.2 per cent.¹⁵

The OECD estimates indicate that Pillar One may reallocate about US\$200 billion of taxing rights towards market jurisdictions (where the consumers are located).

Pillar One will affect jurisdictions differently, particularly depending on whether they are investment hubs or market jurisdictions. In general, investment hubs (jurisdictions where lower corporate income tax rates attract high levels of business investment, resulting in high residual profits) will be negatively affected, as their high residual profits relevant to their local consumer base will result in reallocations

¹⁴The OECD estimates are subject to a number of data and modelling caveats, and should be interpreted as illustrating the broad order of magnitude.

¹⁵ OECD (2020), Tax Challenges Arising from Digitalisation – Economic Impact Assessment, retrieved from www.oecd.org



of taxing rights to market jurisdictions through Pillar One's Amount A. Market jurisdictions (including many jurisdictions that have higher corporate income tax rates, lower residual profits, but many end-consumers) stand to benefit from the reforms, as these jurisdictions will receive the aforementioned re-allocated Pillar One Amount A taxing rights. In broad terms, Australia is a market jurisdiction for these purposes.

Costs

The OECD has estimated that the direct negative investment impacts from higher taxation resulting from Pillar One and Pillar Two would lead to a reduction of global GDP of less than 0.1 per cent.¹⁶ The OECD believes this cost is small and would be more than offset by other factors, such as greater investment certainty and reduced compliance costs from avoiding the proliferation of unilateral taxes.

Pillar One also works towards creating a more even playing field between the world's largest and most profitable multinationals and local businesses. A more even playing field within and between countries should, over the long-term, lead to some economic efficiency improvements, from better competition and from operational decisions being based more on economic (rather than taxation) rationales.

Pillar One impact on Australian business

Treasury estimates that no Australian headquartered multinationals currently fall in scope of Amount A. However, as a result of future changing economic conditions, profitability and revenue levels, some Australian multinationals may eventually meet the EUR20 billion revenue and 10 per cent profitability thresholds. Also, a revised EUR10 billion revenue threshold is expected to take effect if the seven-year review (around 2030) finds that Amount A has been successfully implemented. The OECD has estimated that at these thresholds, there would be about 100 multinationals globally currently in scope of Pillar One (Amount A).

Some out-of-scope multinationals may face increased compliance burdens, as they may be required to check how close they are to revenue and profitability thresholds.

For in-scope (non-Australian) multinationals, Pillar One (Amount A) is expected to have limited impact on business operations. Since Amount A reallocates taxing rights over multinational profits between countries based on the location of consumers, there is limited ability or incentive for multinationals to change their operations, especially in market jurisdictions like Australia.


Importantly the design of Pillar One reflects Australia's national interests, in that extractive activities and regulated financial services industries are excluded. These entities represent a significant component of Australia's existing corporate tax base.

Additionally, Australian subsidiaries of in-scope multinationals could be impacted to some extent by certain elements of Amount A, in particular the Elimination of Double Taxation (EODT) and the Marketing and Distribution Profits Safe Harbour (MDSH) mechanisms.

Pillar One impact on Australian consumers and employment

Pillar One is likely have little to no impact on Australians' consumer experience or employment levels. This is because Pillar One involves coordinated action to address tax distortions without discouraging economic activity in market countries. This coordination includes a mechanism to avoid double tax by

¹⁶ OECD (2020), Tax Challenges Arising from Digitalisation – Economic Impact Assessment, retrieved from www.oecd.org



reducing tax liabilities in jurisdictions with current residual profits by an amount equal to the profits allocated to market jurisdictions. This is what makes Pillar One a reallocation of taxable profits.

Overall, Pillar One should not restrict service delivery or availability to the Australian market. Since multinationals will still want to earn profits from market jurisdictions, an increase in the share of their global profits that are taxed locally should not materially impact their activities. This is particularly likely given that Pillar One (Amount A) only affects the residual profits of in-scope multinationals. These residual profits are expected to be above the level of return multinationals require to carry on their global business. In theory, these profits can be taxed at a higher rate without affecting supply.

There is a possibility that increased global tax expenses of multinationals will affect the way that these multinationals carry on their business or price their products. However, this is a far less likely outcome for Amount A's profit reallocation system compared with other designs, such as Digital Services Taxes.

Pillar One compliance costs

The OECD considers the global compliance costs from Pillar One will be relatively minor compared to the revenues of in-scope multinationals, with most of the additional activities required under Pillar One expected to leverage existing activities that a multinational group would already undertake. For example, existing tax returns, financial reports and consolidated accounting statements, as well as multilateral obligations like Country-by-Country Reporting, would be utilised for Pillar One calculations. In practice, it is likely that the vast majority of the increase in compliance costs and burdens from Pillar One will be imposed by other countries, primarily investment hub and headquarter countries.

Nonetheless, it is likely that Australian entities will see increases in compliance costs due to the need to determine if they are within scope. While no Australian headquartered multinationals are likely to be in scope of Pillar One in the near term, some stakeholders have raised concerns that the calculations needed to rely on the extraction exclusion will still add compliance costs.

Multinationals will need to invest in recruitment and training of staff to ensure that they understand the rules and are compliant where they are in scope. There is a potential that Australian subsidiary entities will be responsible for some aspects of this compliance if they are required to report to their foreign parent entities.

For Pillar One, there will be a requirement of additional record keeping systems and procedures to ensure relevant calculations can be made, but also, that it can be determined an entity is compliant with the reforms. The use of the global consolidated financial statements provides a simple starting point, however more detailed information will need to be gathered to comply with novel rules, such as in relation to revenue sourcing. Owing to the nature of the Amount A calculations, multinationals will only be aware of the Amount A liability after the relevant period, meaning there will likely be necessary adjustments to closing procedures for year-end to account for Amount A outcomes.

Additionally, Pillar One will introduce a high level of complexity in its early years. This is due to the international nature of the work requiring many stakeholders working together to understand, and comply with, the rules. The compliance complexity of Pillar One is potentially offset by the tax certainty framework and Amount B, which are intended to provide certainty to taxpayers, and simplify the transfer pricing processes respectively.

Concerns about complexity and compliance challenges have consistently been raised during public consultation. Recruitment, training, and external advisory will likely contribute to significant costs upfront.

More broadly, the OECD has argued that Pillar One could result in lower overall compliance costs on large multinationals over the long-term, compared to the alternative of a proliferation of Digital Services Taxes with inconsistent implementation.

Finally, Pillar One includes new tax certainty provisions that could reduce tax disputes over time internationally, potentially reducing costs for business and tax administrations.

Tax Certainty

A central element of Pillar One, Amount A, is a new Tax Certainty Framework that aims to reduce compliance costs for large multinationals. It seeks to provide certainty over all aspects of Amount A, including the elimination of double taxation. This eliminates the risk of uncoordinated compliance activity in potentially every jurisdiction where a multinational Group has revenues, as well as a complex and time-consuming process to eliminate the resulting double taxation. The tax certainty process includes:

- A Scope Certainty Review, to provide an out-of-scope Group with certainty that it is not in scope of the rules for Amount A for a Period, removing the risk of unilateral compliance actions;
- An Advance Certainty Review, to provide certainty over a Group's methodology for applying specific aspects of the new rules that are specific to Amount A, which will apply for a number of future Periods; and
- A Comprehensive Certainty Review to provide an in-scope Group with binding multilateral certainty over its application of all aspects of the new rules for a Period that has ended, building on the outcomes of any advance certainty applicable for the Period.

Regulatory obligations on in-scope Pillar One companies

Under Pillar One, the ultimate parent entity of a multinational group will carry the primary obligation for compliance with the new rules. Some subsidiaries within the multinational Group – especially those entities entitled to double tax relief – will also have administrative obligations with respect to Pillar One.

While it is estimated that no Australian headquartered company will be in scope initially, Australia will still need legislative changes to implement Pillar One. This might include legislation to enable the Australian Government to collect the Pillar One taxation payments from foreign companies, who are not necessarily captured by our existing tax system. Tax certainty processes may also require Australia to collect and exchange taxpayer information with other tax administrations.

While the precise requirements on Australian businesses will depend on their role within an in-scope group, the likely steps for a multinational to comply with Amount A of Pillar One are outlined below.

Step One: Determine whether a multinational is in scope

Multinationals would need to check whether they are in scope, with global revenues exceeding EUR20 billion per annum and profitability to revenue ratios exceeding 10 per cent (regardless of whether they are 'digital' businesses or not). The scope excludes Extractives and certain Regulated Financial Services businesses.

Step Two: Determine the tax base

In-scope multinationals would then determine their total global profit, by consolidating all the financial accounts of foreign subsidiaries, with certain adjustments.

Step Three: Determine the quantum

In-scope multinationals would then identify their global profits in excess of the 10 per cent profitability threshold (known as ‘residual profits’) and identify 25 per cent of these residual profits, being their ‘Amount A’.

Step Four: Attribute revenue sourcing

The taxing right for the Amount A profit would then be allocated by the multinational proportionally to the jurisdictions where the goods and services were consumed (the ‘market jurisdictions’), providing sales meet the nexus test of EUR1 million within the jurisdiction, with a lower threshold for developing countries. The market jurisdictions would then apply their domestic corporate tax rate to the share of the Amount A profit allocated to them, receiving taxation revenue on this basis. The allocation to each jurisdiction is subject to a Marketing and Distribution Profits Safe Harbour, which may limit some of the reallocation of taxing rights where the multinational already has a profitable taxable presence within a jurisdiction.

Step Five: Eliminate double taxation

Double taxation of profit allocated to market jurisdictions will be relieved by jurisdictions with the highest amount of residual profits, according to tiers which are currently being negotiated. Negotiations will examine the form of tax relief, which could be in the form of either a tax exemption or tax credit.

Compliance costs on out-of-scope businesses

As noted above, even if a multinational ends up not being in scope of Pillar One, it may still create a compliance burden for them to check how close they are to revenue and profitability thresholds. To make this easier, it is likely global accounting firms will create guidance and tools (like a smart spreadsheet or software package) in order to help advise multinationals as to whether they are in scope. Further, it is expected that the tax certainty process would help reduce some of the costs associated with determining scope. It is presumed that large multinationals would already have global accounting firms contractually engaged, and that they would extend their existing contractual services to receive top-up specialist advice on Pillar One scope. The multinationals’ employees will also need to take time to gather data for the purposes of determining scope, as well as briefing their Boards on the Pillar One design and scope matters.

While no Australian multinationals are expected to be in scope of Pillar One at this stage, top Australian-incorporated multinationals will likely want to seek assurances that they are out of scope, as well as get a general understanding of the Pillar One regime. This may involve:

- Upfront costs to receive external specialist advice to understand Pillar One rules;
- Upfront costs to make system changes to gather data in-line with Pillar One rules; and
- Ongoing costs to calculate their global revenue and profit ratios in-line with Pillar One rules.

While not factored into Australian compliance cost calculations, foreign-headquartered multinationals operating in Australia can expect lower compliance costs from some aspects of Pillar One including:

- Reduction in costs from the tax certainty provisions under Pillar One, which have the potential to reduce the costs associated with resolving tax disputes; and
- Potential transfer pricing simplification under Amount B.

Using the Office of Impact Analysis' Regulatory Burden Framework, the average annual regulatory burden is estimated to be \$0.7 million. For clarity this regulatory cost reflects only the cost to a small number of Australian businesses in confirming they are not in scope of Amount A. The expected decreased costs from foreign-headquartered multinationals not needing to comply with a theoretical Australian Digital Services Tax (as such a tax is banned under Pillar One), reduced tax disputes with the ATO from new tax certainty processes, and simplified transfer pricing under Amount B have not been quantified. The remaining regulatory burden imposed on foreign-headquartered multinationals that are in scope of Pillar One is presumed to be imposed by their home country (not Australia) and would be unchanged regardless of whether Australia implements Pillar One.

Impact on Australia from implementing Pillar Two

Pillar Two revenue impacts

Implementing Pillar Two and a qualifying domestic minimum tax is estimated to increase receipts by \$370 million and increase payments by \$111 million over the five years from 2022-23. The actual revenue gain outcome will be dependent on the response of other jurisdictions in implementing the Pillar Two rules, their own domestic minimum taxes, and behavioural responses by multinational groups.

Overall, the OECD has estimated that Pillar Two would increase global tax revenues.¹⁷ These tax revenue increases will come through the adoption of a global minimum tax by a critical mass of jurisdictions. Countries that implement the GloBE Model Rules will increase tax revenue via the global minimum tax if there are entities in the MNE group operating in low tax jurisdictions. However, these low tax jurisdictions may increase their revenue by choosing to increase their corporate tax rates or implement domestic minimum taxes. While the OECD had estimated that the average percentage revenue gains from Pillar Two may be greater for high-income jurisdictions than the gains for middle- and low-income jurisdictions, that estimate was based on earlier design assumptions.¹⁸

From an economic perspective, implementing Pillar Two will help strengthen Australia's corporate tax base. A smaller differential between the headline tax rates of Australia and other countries may help make Australia more attractive for new business and investment. Also, multinationals that have already invested in Australia may have less incentive to relocate or to shift profits to other countries due to this decreased differential. However, if low-tax jurisdictions increase their tax rates, the amount of low-tax income subject to Australian Pillar Two top-up tax may be reduced.

¹⁷ Organisation for Economic Co-operation and Development (2021), Brochure: Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy, 8 October 2021

¹⁸ Organisation for Economic Co-operation and Development (2020), Tax Challenges Arising from Digitalisation – Economic Impact Assessment

A domestic minimum tax implemented alongside Pillar Two (Sub-option 2(a)) may increase revenue for Australia. However, as Australia has a headline corporate tax rate above the minimum rate, it is expected that few companies will have an effective tax rate under the minimum and would therefore be required to pay top-up tax.

The OECD estimates that in 2018 about US\$1,717 billion of corporate profits were low-taxed, which will continue to increase over time without Pillar Two.

Pillar Two economic impact

Pillar Two Economic Benefits

While work to model the economic impacts of Pillar Two are ongoing, in a qualitative sense it should have a slight positive impact, primarily from making Australia a relatively more attractive place for mobile capital investments. This is because Australia's headline corporate tax rate is relatively higher than other countries, which to some extent reduces foreign investment, particularly for tax sensitive mobile capital. Accordingly, if Pillar Two brings about an effective global minimum tax rate, there should be reduced tax competition between jurisdictions, which will make investing in higher taxing jurisdictions like Australia relatively more attractive as compared to the status quo.

Another economic benefit will come from reducing the financial incentives for Australian companies to offshore their economic activity for tax purposes. For example, at the moment Australian companies can get a financial benefit from offshoring their global marketing services to low-tax jurisdictions.

Should Pillar Two bring about overall higher global tax rates on large multinationals, it may have slight competition benefits for small Australian business, by way of reducing some of the tax advantages some large multinationals have.

Note it is not possible to model the quantitative economic impacts on Australia's economy for Pillar Two, primarily because of uncertainty around behavioural responses of low-tax jurisdictions, and the resultant behavioural change in multinational profit shifting incentives and strategies.

Pillar Two Economic Costs

The most significant negative economic impact from Pillar Two on the Australian economy is an increase in compliance costs, which arise from the need to calculate effective global income and tax paid over a four-year period. This is different to the current system, where companies generally just need to calculate profit year to year in each country.

Under Pillar Two, the financial incentives for multinationals to use profit shifting strategies will be reduced, given there will be an effective minimum tax rate. Given overall more tax is paid, over the long-term, the amount of global investment can be expected to be slightly lower. This also flows through to slightly lower investment returns for shareholders over the long term. It is important to note, however, that investment impacts are unavoidable and inherent to all forms of taxation.

The OECD estimates that Pillar Two is expected to increase total global taxation revenue to a greater extent than Pillar One (since Pillar One is more a reallocation of taxing rights, while Pillar Two provides for new top-up taxes that will incentivise some countries to increase their tax rates). Increased corporate income tax is associated with a reduction in return to investors. A lower return to investors can make it harder for new investment projects to get started.

Pillar Two consumer impact and employment

It is expected that if choosing to implement Pillar Two along with many other jurisdictions, there will be no material direct impact on Australian consumer experiences. While some multinationals subject to Pillar Two top-up taxes might cease activities that are only worthwhile for them in a low or no tax environment, this should have minimal impact on Australia. In general, multinationals operating in Australia are not contingent on low or no tax arrangements that will be affected by Pillar Two. Additionally, multinationals will still wish to earn profits from the Australian market, and as such, it is not expected that there will be any restrictions by multinationals to Australian product delivery.

Since Australia already has a corporate income tax rate above the minimum 15 per cent rate, it is unlikely that any Australian based new investment projects (and their associated employment benefits) will be negatively affected by Pillar Two. Given that MNEs will have less incentive to shift their profits to lower-tax jurisdictions when they can only offer a tax rate as low as 15 per cent, Australia will become relatively more attractive for new investment compared to now.

Pillar Two compliance costs

The compliance costs of Pillar Two on in-scope business are expected to be significant. Concerns about complexity and compliance challenges have consistently been raised during public consultation. Significant increases in the upfront compliance costs of large multinationals' time and investment are expected, in relation to, but not limited to, training, business operation planning, and software and/or hardware to support compliance. Costs of advisory services are also expected to increase as large multinationals are expected to rely on external advisors to support this transition.


These costs may be reduced to some extent through the addition of safe harbour provisions. Pillar Two will require a new global income tax return (known as the GloBE Information Return) to be lodged and shared between tax administrations, and it is also likely that jurisdictions may require additional local lodgements associated with the GloBE Information Return and/or any domestic minimum taxes.

Compliance costs may be reduced where domestic minimum tax design mirrors the GloBE Model Rules. This is because there will be fewer intricacies that a multinational will need to understand to comply with the domestic minimum tax legislation. Since the absence of a domestic minimum tax would result in affected businesses being liable to pay top-up tax to other jurisdictions, interacting with a local tax authority in relation to a domestic minimum tax is potentially a less burdensome implementation option.

The OECD has argued that the existence of Pillar Two will help moderate countries going it alone with their own unique solutions, which may stifle global tax certainty. A globally harmonised approach could therefore lower overall compliance costs over time compared to ad-hoc unilateral measures (e.g. each jurisdiction adopting unique domestic minimum taxes).

Population of affected Australian businesses

Compared to Pillar One, the scope of Pillar Two is much broader due to a lower revenue threshold of only EUR750 million and no profitability threshold. The estimated population of businesses in Australia captured by Pillar Two is still uncertain at this stage, however, based on the number of multinationals self-identifying as Significant Global Entities, with global income exceeding \$1 billion is in the order of about 5,000. However, only a subset of these entities would be subject to top-up taxes requiring detailed engagement with the Pillar Two rules. It is currently estimated that there are about 140 Australian headquartered multinationals or Australian subsidiaries of foreign multinationals that would likely be subject to top-up taxes under the Pillar Two rules and/or a domestic minimum tax.



The design of Pillar Two is novel in that even if a country has not signed up to Pillar Two, multinationals operating in that country may still be obliged to comply if they have subsidiaries in countries that have adopted Pillar Two. Therefore, just one entity of the multinational operating in a single jurisdiction which implements Pillar Two could bring the whole multinational's global operations into scope of Pillar Two. This also means that the decision of any jurisdiction to implement Pillar Two or not will have limited impact on the compliance impact of Pillar Two across a multinational Group.

Regulatory obligations on in-scope Pillar Two companies

Multinationals will need to monitor whether the jurisdictions in which they operate implement Pillar Two and if so, determine whether they meet the revenue threshold to fall within the scope of the GloBE Model Rules. Where multinationals are in scope of Pillar Two, subject to the application of safe harbours, they will need to comply with complex domestic legislation to determine the effective tax rates and any potential under-taxation in jurisdictions in which they operate. If top-up tax is payable, multinationals will not only bear the cost of that top-up tax, but they will also need to determine where that tax should be paid.

Regardless of whether a top-up tax liability exists, all in-scope multinationals will need to complete the GloBE Information Return. It is likely Pillar Two will also require additional domestic forms to be filed in each jurisdiction they operate in. Where jurisdictions qualify for a safe harbour, this may reduce the amount of information required to be disclosed in any returns that are required to be lodged.

Most of the information that multinationals require should be available through existing internal accounting information systems. Nonetheless, significant upfront and ongoing costs associated with amending existing reporting processes as well as establishing new internal assurance processes may be expected.

Subject to Tax Rule (STTR) compliance costs

The Inclusive Framework will develop a Multilateral Instrument to facilitate implementation of the STTR in relevant bilateral tax treaties and a process to assist in implementing the STTR will be agreed. To the extent an STTR is included in relevant bilateral tax treaties (including bilateral tax treaties between jurisdictions other than Australia), multinational groups that seek treaty benefits in relation to their operations and activities will be affected, with the STTR applying to interest, royalties and a defined set of other payments yet to be settled. This may lead to additional compliance costs.

There will also be upfront costs for Australian entities to understand the STTR if Australia is required to implement one due to a request from a developing country for a respective bilateral tax treaty. The technical detail of precisely what income is included and the thresholds to trigger an STTR application are yet to be finalised. However, the rule draws on existing understood principles under tax treaties and the OECD work is looking into collection mechanisms that minimise complexity and eases administration.

Even if Australia is not requested to include an STTR in its tax treaties, Australian multinationals may be required to understand the STTR to the extent it operates in other countries and accesses other countries' bilateral tax treaties where an STTR is included.

Australian-headquartered multinationals will need to incur the following costs to comply with the Pillar Two rules:

- Upfront cost to understand the new Pillar Two rules;
- Upfront cost to update systems to gather data according to the Pillar Two rules; and
- Ongoing cost to file their annual global taxation forms.

Foreign Headquartered Multinationals with subsidiaries in Australia will be required to file a local DMT / GloBE Information Return with the ATO.

Using the Office of Impact Analysis's Regulatory Burden Framework, the total average annual regulatory burden on all businesses is estimated at \$31.6 million, with this cost concentrated among the estimated 100 MNE groups potentially liable to pay Australian DMT and the estimated 40 Australian headquartered MNEs potentially liable to pay Australian tax under the GloBE Model Rules due to having operations in foreign jurisdictions whose profits are insufficiently taxed.

This estimate relates only to Australian implementation of Pillar Two. While the global compliance impact of Pillar Two across affected Australian multinationals would potentially be even higher if Australia does not implement a domestic minimum tax, exposing these multinationals to top-up tax in other jurisdictions, this estimate aims to convey the fact that Australian implementation of Pillar Two would involve significant interaction with the ATO.

Impact on Australia from not implementing Pillar One

Revenue impact from not implementing Pillar One:

By not implementing Pillar One Australia will forgo taxation revenue that would otherwise be allocated to it.

Australia would continue to have corporate tax policy options outside of the Two-Pillar Solution.

Australia already has relatively comprehensive anti-avoidance measures, so the scope for additional action may be limited and unilateral action may not be able to effectively contend with the global nature of problems from 'scale without mass' and the 'race to the bottom'. The effectiveness and benefit of unilateral policy actions related to corporate taxation is also dependent on how well accepted they are by other jurisdictions and multinationals. Measures outside of the accepted multilateral framework are more likely to be challenged and provoke trade retaliation.

Economic impact from not implementing Pillar One:

If Australia does not implement Pillar One, while the rest of the world does, it may lead to greater investment uncertainty in Australia. This is because multinationals may factor in the sovereign risk of Australia implementing a Digital Services Tax or similar measure.

By being outside the tent, Australia may also lose influence over the future design of the international tax system. This may lead to a system that is not as favourable for Australia's special circumstances, for example taking account of the important role corporate income tax has in relation to the Australia community extracting fair value for the sale of its minerals.

Compliance Costs from not implementing Pillar One:

The current assumption is that all major countries will adopt Pillar One. So, even though Australia may not implement Pillar One, our headquartered multinationals will still do business in jurisdictions that have adopted Pillar One. In this way the compliance costs impact will be very similar, whether Australia adopts Pillar One or not.

Impact on Australia from not implementing Pillar Two

Revenue impact from not implementing Pillar Two:

By not implementing Pillar Two, Australia will forgo potential increased corporate taxation revenue.

For example, if a multinational's global tax rate is determined to be below the global minimum rate in a jurisdiction, Australia may miss out on the ability to apply a top-up tax on that multinational. This could mean that Australia is forgoing taxing rights, which would then be automatically picked up by other countries.

Other countries may also impose top-up taxes on Australian-headquartered multinationals, where the Australian jurisdictional effective tax rate is below the global minimum rate. This could happen in situations where due to industry concessions and investment incentives built into the Australian tax system, effective taxation of a company falls below the 15 per cent minimum rate. Whereas if Australia has implemented Pillar Two, with a qualified domestic minimum tax, it would mean Australia would have first rights over Australian undertaxed profits.

Economic impact from not implementing Pillar Two:

Presuming other major countries implement Pillar Two, there is an argument that Australia would still benefit off the actions of other countries given that the headline differential would still be reduced as low tax jurisdictions will be brought up to the global minimum rate of 15 per cent.

Although, in the longer term, multinationals may be less likely to have their headquarters in Australia if there is uncertainty as to where top-up taxes may be imposed if Australia is not part of Pillar Two. This would have a detrimental impact on Australian employment figures associated with the executive management of large multinationals.

Compliance Costs from not implementing Pillar Two:

The current assumption is that all major countries will adopt Pillar Two. By choosing not to implement Pillar Two, this does not stop multinationals operating in Australia from being subject to Pillar Two if they operate in another jurisdiction that does implement Pillar Two. Therefore, the compliance costs on Australian-headquartered multinationals will be similar or higher given the additional complexity of the Pillar Two rules being applied by multiple non-headquarter jurisdictions. However, should Australia not adopt Pillar Two, there would be slightly lower compliance costs on foreign subsidiaries operating in Australia, as they would not need to submit a separate global information return to the Australian Taxation Office.

Consultation

The OECD/G20 Inclusive Framework process has been the subject of multiple consultations since it began in 2013. The subject of Pillar One and Pillar Two has been consulted on since 2018 both by the OECD and Treasury. Comments garnered from respondents have been considered in the design of

Pillar One and Pillar Two and have informed Treasury's participation in the negotiations with the OECD/G20 Inclusive Framework, as summarised below.

Consultation by the OECD

A summary of the OECD consultations on the Two-Pillars Solution is presented as follows. Further details on each consultation are provided in Appendix A.

OECD Reports on the Pillar One and Pillar Two Blueprint and the OECD Business Advisory Group (2020 to 2022)

The OECD has released various reports on the Pillar One and Pillar Two Blueprints during the Two-Pillar Solution negotiations. These reports provide updates on the policy design proposals of the OECD secretariat, which are informed through the course of the OECD negotiations with country delegates. The Blueprint papers were released for consultation, and received 201 submissions from stakeholders on Pillar One, and 197 submissions from stakeholders on Pillar Two. The OECD has also been undertaking targeted consultation with the Business Advisory Group,¹⁹ which includes representatives of Australian businesses, throughout the negotiations.

Key comments received:

- Continue pursuing implementation on of the Two-Pillar Solution.
- Include a wide extractives carve-out from Pillar One.
- Include large transition period for revenue sourcing rules.
- General support for safe harbour concepts.
- Expansion of tax certainty options.
- Withdrawal of existing unilateral measures.

OECD response:

The OECD noted the importance of public consultation and committed to considering the public comments. In following OECD negotiations, the OECD Secretariat brought forward proposed policy designs related to some of the recommendations received from the public.

OECD Consultation: Pillar One Progress Report (2022)

In July 2022, the OECD released a Progress Report on Pillar One for consideration by country delegates.²⁰ This report garnered 71 submissions in relation to the progress of Amount A under Pillar One. Comments received contributed to updates being made to the policy design of various aspects of Pillar One's Amount A.

¹⁹ The Business Advisory Group (BAG) is a subgroup of *Business at OECD (BIAC)*, an international business association that advises government policy makers at the OECD.

²⁰ Organisation for Economic Co-operation and Development (2022), Progress Report on Amount A of Pillar One

Key comments received:

- Preferences for applying averaging mechanisms to the scope criterion.
- Ongoing support for a wide extractives carve-out from Pillar One.
- More specific guidance needed for revenue sourcing.
- Longer time limitations for loss carry-forwards.
- Request for more detail to the Return on Depreciation and Payroll metric in the Marketing and Distribution Profits Safe Harbour.
- Questions over how the Elimination of Double Taxation metric should relieve.
- Support for the inclusion of a prohibited unilateral measures list in the Multilateral Convention.
- Strong support for Amount B to provide tax certainty and for this work to be expedited.

OECD response:

The OECD hosted a panel discussion following receipt of the submissions from the public on the Pillar One Progress Report. At the panel discussion, representatives from some commentators were invited to discuss various aspects of the Progress Report. This resulted in the OECD Secretariat taking on suggestions to update the design of various Pillar One aspects.

OECD Consultation: Pillar Two GloBE Implementation Framework (2022)

In April 2022, the OECD conducted a public consultation process on the administration and implementation issues under Pillar Two's GloBE Implementation Framework. Written comments from 73 interested stakeholders were received and discussed in a public meeting. Key comments received:

- A workplan is needed for a peer review process for a jurisdiction's domestic implementation plans.
- The OECD should also develop the Implementation Framework addressing:
 - administrative guidance.
 - a standardised GloBE Information Return and information exchange between tax authorities.
 - safe harbours.
 - workshops and webinars to promote technical awareness.

OECD's response:

In response to stakeholders' feedback, the OECD designed a plan to develop the implementation framework. Further, the OECD has recently released an Implementation Framework package that contains administrative guidance on technical issues identified by stakeholders during the consultation process.

While stakeholder feedback has been noted and acknowledged by the OECD, there are limitations to what can be incorporated in the implementation framework, given that the Two-Pillar Solution is a globally negotiated agreement. It is necessary for the implementation framework to be agreeable by

all jurisdictions, as failure to ratify them, may undermine the multilateral process. In general, public stakeholder feedback on the technical design elements of both Pillars has been more directly addressed and incorporated compared with feedback on the fundamental approach of the work.

Consultation by Treasury

Treasury Discussion Paper: The digital economy and Australia's corporate tax system (2018)

Treasury released a discussion paper in 2018 titled: The digital economy and Australia's corporate tax system²¹, seeking comments on digital taxation issues.

Key comments received:

- Concerns about the impacts of a Digital Services Tax, such as the likely pass-through of costs to consumers, compliance costs, the effect on competition and innovation, retaliatory trade actions and the risk of double taxation. 44 submissions were received.²²
- Very strong support to continue participating in the OECD/G20 Inclusive Framework process to develop a multilateral solution.

Government response:

In response to stakeholders' feedback, the former Government announced that it would not be pursuing a unilateral measure, such as a Digital Services Tax, at that time and committed to working with the OECD to develop a multilateral solution.

Digital Tax Working Group, Board of Taxation and the National Tax Liaison Group (2020 to 2023)

Since 2019, Treasury has engaged with a Digital Tax Working Group, the Board of Taxation and the ATO's National Tax Liaison Group. In these groups, Treasury provides updates on digital tax matters, and benefits from discussing these with the representatives from the various bodies. Treasury has hosted at least one round of Digital Tax Working Group meetings every year between 2019 and 2022. In addition to these meetings, the Digital Tax Working Group has been kept up to date regarding developments at the OECD via email, and smaller group meetings have been held on specific issues.

Range of stakeholders:

The Digital Tax Working Group includes representatives from around 60 organisations and stakeholders, including multinationals such as Alphabet, Amazon, Meta and Rio Tinto. Advisory firms, academics, financial institutions, cloud computing companies, industry bodies, mining companies and other multinationals are also included to ensure that a broad cross section of views is captured. Membership has been broadened as the scope of the Two-Pillar Solution has shifted. The Group was

²¹ Commonwealth of Australia, The Treasury (2018), The digital economy and Australia's corporate tax system

established as an ongoing forum for discussion of options and issues being contemplated in the OECD/G20 Inclusive Framework process.

The Board of Taxation is a non-statutory advisory body charged with providing advice to the Treasurer. Its role is to contribute a business and broader community perspective to improving the design of taxation laws and their operation.

The National Tax Liaison Group is one of the Stewardship groups operated by the ATO as a means of improving the client experience and administration of Australia's taxation and superannuation system.

Key comments received:

- Desire for Australia to continue pursuing implementation on of the Two-Pillar Solution.
- Desire for Australia to provide ample transition time for implementation.
- Australia should continue to advocate to the OECD Secretariat to find more ways to reduce compliance costs.
- There is a preference for a global approach, as opposed to the current proliferation of unilateral Digital Services Taxes and the potential for trade sanctions.
- The Two-Pillar Solution is very complex, and simplification is desired.
- Concerns about the timing of implementation, given the need to update systems to collect data – as well as to inform business planning and future investment decisions.
- There are significant compliance challenges, such as calculation of profit using financial accounting statements under the rules.
- Concerns about the lack of principles underpinning design of the proposals.
- Desire for an extractives carve-out for Pillar One.
- Concerns about Pillar Two imposing top up taxes as a result of stimulatory policies like accelerated depreciation.
- Safe harbours under Pillar Two will be an important aspect to help reduce compliance costs.
- Concerns around “doubling compliance burden” where any domestic minimum tax does not mirror the Pillar Two calculations.

Treasury's response

Stakeholders' feedback has informed Australia's position during the multilateral negotiation of the two pillars. Treasury has advocated on behalf of the stakeholders who have provided their commentary in the Digital Tax Working Group, Board of Taxation and National Tax Liaison Group forums. Various points from the above that Treasury has advocated for, include: accommodation of Australian tax approaches in Pillar Two; the extractives carve-out from Pillar One which has greatly protected Australian interests; the restriction of Digital Services Taxes; and, the simplification of the design of the Two-Pillar Solution.

Owing to the multilateral nature of the proposed reforms, Treasury needs to analyse the merit of, and apply judgement to, the various comments it receives from the public. Multilateral projects generally involve a high level of negotiation and compromise between jurisdictions, and therefore, Australia's influence over the negotiations is not absolute and compromises are needed to ultimately reach

consensus. As such, the information and suggestions received have been used to varying degrees during the course of the negotiations.

Treasury Consultation on the Two-Pillar Solution (2022)

On 4 October 2022, Treasury launched public consultation to seek views from interested parties on how Australia can best engage with the Two-Pillar Solution, including the Pillar Two Model Rules and Commentary. The consultation included an explanation of the problem driving the Two-Pillar Solution, potential options and impacts. It sought feedback particularly on the interactions with Australia's existing corporate tax system, ways to minimise compliance costs, and the implementation of a Domestic Minimum Tax.

Range of stakeholders:

- Professional Services: EY, Deloitte and PwC
- Advocacy Group: Corporate Tax Association, Australian Chamber of Commerce and Industry, Association of Superannuation Funds of Australia, Law Council of Australia, Australian Retailers Association, Property Council, Public Services Union, Asia Internet Coalition, Uniting Church of Australia, National Foreign Trade Council, Information Technology Industry Council
- Academic: Professor Kerrie Sadiq and Professor Richard Krever
- Multinational: CSL, South32

Key comments received:

- Support for the Two-Pillar Solution.
- Consideration should be given to Australia's existing taxation system when translating OECD Model Rules into domestic legislation.
- Plans should be progressed for administrative and transitional support arrangements.
- Negotiations with the OECD should ensure effective safe harbours are in place for Pillar Two.
- Support for a qualified domestic minimum tax as part of Pillar Two implementation and that Australia should align implementation with EU countries and US.
- Common view that 2023 start dates for either Pillar are very challenging for businesses, given not all rules are clarified. Better to start in 2024.
- Widespread concerns over compliance costs and the need for Pillar Two safe harbours to lower compliance costs. Leverage existing CbCR rules and data to lower compliance costs.
- Franking credits should be allowed for GloBE taxes and DMT.
- Desire for a more defined extractive definition in Pillar One.
- Need to consult further on domestic legislation.

Treasury's response

The Two-Pillar Solution is a multilateral agreement that requires a high level of negotiation and compromise between jurisdictions. Hence, in considering the feedback from stakeholders, Treasury should ensure that Australia's implementation of the two Pillars aligns with the global agreement. This means that, while some stakeholders may prefer a different approach or treatment, the resulting products may not necessarily reflect the preference of individual stakeholders.

In light of the received feedback, Treasury has considered the following in its proposed approach for future implementation of Pillar One and Two:

- The implementation of Pillar Two in Australia should be aligned with the OECD's GloBE Model Rules, Commentary and Implementation Framework, to ensure that compliance burdens and costs are reduced as much as possible to support multinationals in the transition to the new rules;
- Australia should implement a qualified domestic minimum tax to avoid increasing compliance burden in Australia;
- Domestic implementation of the Pillars will ensure appropriate interaction with Australia's existing taxation system;
- In deciding whether top-up taxes under the GloBE Rules and DMT should give rise to franking credits or not, consideration has been given to aligning Australia's implementation with the policy intent of the GloBE Model Rules;
- Acknowledging the concerns of multinationals in introducing either Pillar too early, proposing implementation of Pillar One and Two from 1 January 2024 at the earliest, to ensure that multinationals have sufficient time to understand and prepare for the transition to the rules;
- We will ensure that further consultation is conducted at the time of drafting the domestic legislation for the domestic minimum tax and GloBE Model Rules; and
- Comments concerning the negotiations with the OECD, including on aspects such as safe harbours, have been noted in preparation for the respective OECD meetings.

Additional consultation 2023 and beyond

Both the OECD/G20 Inclusive Framework and Treasury intend to remain engaged with stakeholders. In preparation for the final stage of negotiations, Treasury will continue to consult with our Digital Tax Working Group to explain the current proposals and seek feedback on practical implications and implementation. Treasury will also continue to engage with the Board of Taxation, who already receive regular updates on the digital tax process.

Consultation with stakeholders and the public will occur at key points through the OECD and by Australia to support domestic implementation such as exposure draft legislation. As dates for commencement and implementation of some aspects are still the subject to negotiations, a precise timeline for consultation cannot be given at this point. The OECD/G20 Inclusive Framework has flagged that technical issues will continue to be developed, the pace of which may also affect future consultation and timing of implementation.

Recommended option

Based on the impact analysis the recommended option for Australia is to choose Option 1, Australia to implement Pillar One, and Option 2, Australia to implement Pillar Two. However, this recommendation is contingent on the policy design continuing to align with Australia's interests as the final details settled in the negotiations.

This would include:

- Continuing to work with OECD Inclusive Framework to finalise the outstanding details of the Two-Pillar Solution;
- Continuing consultation with key stakeholders, and assessment of the impacts on Australia; and
- Having a workplan to minimise complexity and compliance costs for business as part of implementation.

The implementation of both Pillar One and Pillar Two would ensure that Australia remains steadfast with the international community in combatting multinational tax avoidance and contributing to the stabilisation of the international tax framework. Failure to support the international tax community and not implement either, or both, Pillars, may negatively impact Australia's international reputation as a global contributor to a fairer international tax framework.

Further, both Pillar One and Pillar Two are generally expected to provide Australia with increased tax revenues. Failing to implement either Pillar One or Pillar Two, may mean that Australia misses out on the opportunity to receive additional taxing rights under Pillar One, or fails to apply top-up taxes to undertaxed profits under Pillar Two. As such, the implementation will not only protect, but increase, Australia's generation of tax revenue.

More broadly, Pillar One and Pillar Two work towards a more level playing field between the taxation of Australian and foreign-based businesses. They both also modernise the international corporate taxation system to take account of new digital business models. This should help promote greater investment into Australia and allow our businesses to be more competitive. The Two-Pillar Solution will not supplant the need for existing corporate tax integrity measures (which remain complementary).

Given the baseline assumption is that the rest of the world implements the Two-Pillar Solution, a decision by Australia to not implement the Two-Pillar Solution would undermine the international rules-based order that open economies like Australia benefit from. It would also reduce Australia's ability to influence the design and implementation manner of the Two Pillar Solution.

Implementation

Implementation requires work to be completed at the OECD level for both Pillars. This work includes the negotiations of the Multilateral Instrument and Convention, resolution of various significant and complex issues, and the finalisation of policy documents, such as the Implementation Framework for the GloBE Model Rules. Until key design elements are settled at the OECD level, it will be difficult to assess the magnitude, complexity and timeframe required for the implementation task, including interactions with Australia's domestic tax framework and administration.

Key elements of the policy involve Australia becoming a signatory to and implementing a Multilateral Instrument and Convention. Australia's domestic procedures for implementing a treaty involve many

steps including tabling the convention and instrument, policy impact analysis and national interest analysis before both Houses of Parliament. Major treaty actions must be tabled before Parliament for 20 joint sitting days to allow sufficient time for the Joint Standing Committee on Treaties to make a recommendation on binding treaty action.

Some elements of the new rules may be optional for individual countries to implement or may provide flexibility for countries to choose between various options. Additional decisions on implementation will be needed, including the dates of operation of parts of the consensus and timeframes for implementation (this is likely to be several years, however implementation timelines are under debate in the negotiations).

The development of domestic legislation involves drafting legislation and supporting material, as well as allowing adequate time for stakeholder consultation, which will be critical to successful implementation. Inadequate consultation would create the risk of substantial criticism from stakeholders.


Pillar One Implementation

Subject to a decision by Government to implement Pillar One, the steps below are indicative of the approach. Note that the timing is dependent on many variables and decisions by Government.

Approximate date	Step
2022 to 2023	<u>Negotiation</u> : OECD/G20 Inclusive Framework to agree on final design for Pillar One.
2023	<u>Decision</u> : Australia to consider being a signatory to the Multilateral Convention. Begin Australia’s standard treaty making process, including consideration by the Joint Standing Committee on Treaties.
2023	<u>Consultation</u> : Public consultation on exposure draft legislation to change Australia’s taxation laws to comply with the Multilateral Convention.
2024 onwards	<u>Implementation</u> : Treaty and domestic legislation (including subordinate law) comes into legal effect, presuming critical mass has been reached.
2029 onwards	<u>Review/Evaluation</u> : Post-Implementation Reviews are required after five years for proposals that have substantial or widespread impacts (Post-Implementation Reviews Guidance Note, Office of Impact Analysis).
2030 onwards	<u>Review</u> : OECD/G20 Inclusive Framework to facilitate review seven years after implementation.

According to the agreed OECD [implementation plan](#),²³ Pillar One would be made effective through a Multilateral Convention (MLC) (treaty) originally due to be signed by mid-2022 and come into effect in 2023 once a critical mass of countries have ratified it. However, on 11 July 2022, the OECD issued a revised timeline showing the MLC would come into effect in 2024 when a critical mass of jurisdictions has been achieved. The implementation plan also includes the development of model rules to assist countries with integrating the MLC into domestic law, where this might be needed.

²³ [Organisation for Economic Co-operation and Development \(2021\), Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy, 8 October 2021](#)



Australia will likely need domestic legislation to activate the MLC, that may specify how such payments may be made, as well as provisions around the assessment of and Commissioner of Taxation powers in relation to auditing and managing payments.

As part of Pillar One, negotiations will continue on Amount B, the simplified application of transfer pricing rules for baseline marketing and distribution activities.

The implementation plan also specifies that the scope threshold for Amount A will be reviewed after seven years of implementation. It is proposed that the threshold would be reduced to EUR10 billion to cover a wider range of multinationals.

The agreed building blocks explicitly state that extractives and regulated financial services will not be in scope of Pillar One. While the carve-outs have broad support in the negotiations, the detailed design principles underlying each carve-out may vary and are yet to be determined.

Pillar One will also require the signatories to remove their unilateral measures, such as Digital Services Taxes or similar measures and commit to not introducing such measures in future. Guidance for what constitutes a 'unilateral measure' (or similar measures) is still being developed and agreed through the OECD negotiation process.

Challenges to implementation

The key challenges to implementation of Pillar One will be agreement of the text of the model rules to inform domestic legislation, the text of the MLC and associated explanatory memorandum.

A failure to reach a critical mass of countries adopting Pillar One, may result in countries implementing unilateral measures to protect their corporate tax base. In this scenario, many countries may either continue or proceed with implementing Digital Services Taxes, to tax the revenue of large digital companies operating in their jurisdictions. As these Digital Services Taxes and other similar measures are applied to profits being taxed by other countries they may be viewed as discriminatory, which could in turn trigger trade sanctions. The OECD in their economic analysis has argued that in the absence of Pillar One, there would be an escalation of trade disputes globally.

Evaluation

The OECD will conduct a review of Pillar One, seven years from the agreement coming into force. Treasury will also prepare a Post-Implementation Review after five years in line with the Post-Implementation Reviews Guidance Note, Office of Impact Analysis. The five-year timeframe for the Post-Implementation Review considers that this policy proposal is expected to have a substantial or widespread impact on the Australian economy, as the implementation of the policy will significantly change the international taxation framework in Australia. Further, a five-year Post-Implementation Review will allow sufficient time for the impacts of the policy to be seen and assessed, as well as it allowing sufficient time to identify any issues that may have arisen.

Treasury's Post-Implementation Review will commence gathering data on the effectiveness of the policy proposal upon the commencement of the policy's implementation. Some of the data points that may be captured to be considered in the Post-Implementation Review include, but are not limited to:

- Multinational tax compliance data points, taken from the time of implementation, during implementation, and at the time of drafting the Post-Implementation Review;
- Multinational tax revenue figures generated from the implementation, compared to the multinational tax revenue figures pre-implementation;

- Consideration of the net public benefit from the implementation of the policy, including any observed changes in multinationals goods and services supplies made to the Australian market, against the overall utilisation by the Government of the increased tax revenues generated;
- Consideration of the presence or absence of tax related trade disputes for Australia or others;
- Comparison of Australia’s implementation and results against those of other jurisdictions who have implemented similar policies in line with Pillar One of the Two-Pillar Solution; and
- Level of multinational investment in Australia.

Some of the above datasets are currently being captured by various Government agencies, such as the datasets relating to the tax compliance, revenues, profit shifting, and foreign investment, which would currently be gathered, and/or estimated, by Treasury, the ATO, and the ABS. Treasury will also conduct consultation with stakeholders impacted by the proposed policy’s implementation, which will allow Treasury to gain a deeper understanding of how the policy’s implementation has impacted the wider public and how groups of taxpayers may have been affected differently. A consideration of these against pre-implementation data and/or estimates would allow Treasury to determine whether the policy’s implementation was successful in its intent.

The policy will be deemed to have been successful to the extent it has:

- Been complied with in Australia by relevant multinationals;
- Contributed to multinationals paying a fairer share of tax on their profits earned in Australia (likely quantified by an increase in tax payments);
- Reduced the incentive for multinational profit shifting from Australia to low-tax jurisdictions to avoid tax (potentially observed in investment patterns or cross-border payments);
- Not significantly contributed to changes in the prices or the availability and supply of multinationals’ goods and services in the Australian market; and
- Helped Australia and/or other countries avoid tax related trade conflicts.

Amount B

Agreement on how Amount B will operate has not yet been reached. The OECD work on Amount B is proceeding with a view to completing it in the first half of 2023, and may progress separately to the work on Amount A. Amount B is not expected to be reflected in the Amount A MLC or Model Rules.

Pillar Two Implementation

Subject to a decision by Government to implement Pillar Two, the steps below are indicative of the approach. Note that the timing is dependent on many variables and decisions by Government.

Pillar Two Implementation Timetable

Approximate date	Step
2023	<u>Negotiation</u> : OECD/G20 Inclusive Framework to continue to work on administrative processes for Pillar Two.
2023	<u>Decision</u> : Australia to consider being a signatory to the Multilateral Instrument to implement the STTR, which will follow Australia's standard treaty making process, such as consideration by the Joint Standing Committee on Treaties.
2023	<u>Consultation</u> : Public consultation on exposure draft legislation.
2023	<u>Decision</u> : Australia to consider introducing domestic legislation based on the OECD Globe Model Rules to implement Pillar Two.
2024 onwards	<u>Implementation</u> : Treaty and domestic legislation (including subordinate law) comes into legal effect.
2029	<u>Review/Evaluation</u> : Post-Implementation Reviews are required after five years for proposals that have substantial or widespread impacts (Post-Implementation Reviews Guidance Note, Office of Impact Analysis).

The [implementation plan](#)²⁴ envisages that the global minimum tax rate would become operational as individual jurisdictions adopt legislation.

Under the OECD/G20 October Statement, countries implementing the GloBE Model Rules are required to do so in a manner consistent with the GloBE Model Rules, Commentary and Examples agreed by the Inclusive Framework. The OECD have developed an Implementation Framework. There are still further implementation and administration issues to be developed through 2023. Through the Implementation Framework, the OECD will provide agreed administrative guidance, peer review processes and develop safe harbours to facilitate the co-ordinated implementation and administration of the GloBE Model Rules.

While the OECD timeline indicates that the GloBE Model Rules can come into effect from 2023, there are many countries that have already announced delayed implementation to 2024, with a one-year delayed commencement of the UTPR from 2025.

The United States' global intangible low-tax income (GILTI) regime applies to companies with presence in the United States and involves a similar, but still somewhat different, set of rules to the ones proposed in Pillar Two. The October 2021 agreement established that GILTI will co-exist with the Pillar Two proposals, meaning that American companies in Australia may have different rules to comply with. Specific details on how these rules will interact are yet to be finalised through the OECD.

²⁴ Organisation for Economic Co-operation and Development (2021), Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy, 8 October 2021

Challenges to implementation

The key challenge to the implementation of Pillar Two is designing the complex legislation within the required timeframe so that it interacts appropriately with other Australian legislation and is recognised by other jurisdictions which implement Pillar Two.

Under Pillar Two there is no requirement for a critical mass of countries to implement before Pillar Two is activated. However, a Pillar Two that is not widely implemented will be less effective in addressing the global 'race to the bottom'.

Evaluation

A standard five-year post-implementation review of Pillar Two legislation will be conducted, in line with the proposal for the Pillar One evaluation. Treasury's Post-Implementation Review will commence gathering data on the effectiveness of the policy proposal upon the commencement of the policy's implementation. As discussed in the section above relating to Pillar One's evaluation, some datasets to evaluate the success of the policy may include, but are not limited to:

- Multinational tax compliance data points, taken from the time of implementation, during implementation, and at the time of drafting the Post-Implementation Review;
- Multinational tax revenue figures generated from the implementation, compared to the multinational tax revenue figures pre-implementation;
- Consideration of the net public benefit from the implementation of the policy, including any observed changes in multinationals' goods and services supplies made to the Australian market, against any change in tax revenues generated;
- Consideration of the presence or absence of tax related trade disputes for Australia or others;
- Comparison of Australia's implementation and results against those of other jurisdictions who have implemented similar policies in line with Pillar Two of the Two-Pillar Solution; and
- Level of multinational investment in Australia.

Similarly discussed in the section above relating to Pillar One's evaluation, some of the above datasets are currently being captured by various Government agencies, such as Treasury, the ATO, and the ABS. Treasury will also conduct consultation with stakeholders impacted by the proposed policy's implementation, which will allow Treasury to have a deeper understanding of how the policy's implementation has impacted the wider public and how groups of taxpayers may have been affected differently. A consideration of these against pre-implementation data and/or estimates would allow Treasury to determine whether the policy's implementation was successful in its intent.

The policy will be deemed to have been successful to the extent it has:

- Been complied with in Australia by relevant multinationals;
- Contributed to multinationals paying a fairer share of tax on their profits earned in Australia (likely quantified by an increase in tax payments);
- Reduced the incentive for multinational profit shifting from Australia to low-tax jurisdictions to avoid tax (potentially observed in investment patterns or cross-border payments);

- Not significantly contributed to changes in the prices or the availability and supply of multinationals' goods and services in the Australian market; and
- Helped Australia and/or other countries avoid tax related trade conflicts.

Subject to Tax Rule

The Inclusive Framework is still developing a model treaty provision to give effect to the STTR, and a Multilateral Instrument to facilitate implementation of the rule. The Multilateral Instrument will help jurisdictions amend their existing bilateral tax treaties where relevant, to include a STTR when requested to do so by a developing country treaty partner. This is not part of the GloBE Model Rules.

Australian implementation of the GloBE Model Rules

The public release of the GloBE Model Rules in December 2021, and the Commentary and Examples in March 2022 provided the opportunity for interested stakeholders to gain an understanding of how the GloBE Model Rules will operate.

The Pillar Two STTR has not yet been finalised by the OECD Inclusive Framework. However, the GloBE Model Rules (together with the Commentary and Examples) reflect the framework agreed for jurisdictions to proceed with implementation.

Readiness for implementation

Successful implementation of GloBE Model Rules in Australia will in part depend on stakeholders' understanding of and ability to apply the GloBE Model Rules as well as the ATO's system readiness.

Document Status

The User Guide to the Australian Government Guide to Regulatory Impact Analysis suggests agencies describe the status of the document at each major decision point of policy development.

Date	Decision	Status
July 2022	Australia to support the OECD Inclusive Framework conducting public consultation on a Progress Report for Pillar One	Draft
October 2021	Australia to support the OECD Inclusive Framework releasing an implementation plan for the Two-Pillar Solution.	Draft
July 2021	Australia to support the OECD Inclusive Framework releasing the building blocks of the Two-Pillar Solution.	Draft
October 2020	Australia to support the OECD Inclusive Framework consulting on the blueprints for the Two-Pillar Solution.	Draft

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Appendix A: Additional information on OECD consultations

OECD Reports on the Pillar One and Pillar Two Blueprint and the OECD Business Advisory Group (2020 to 2022)

Consultation Process

In October 2020, the OECD released for consultation their blueprint documents for the Two-Pillar Solution, which included:

- [Pillar One](#) Blueprint²⁵ (relocation of profits of multinational enterprises)
- [Pillar Two](#) Blueprint²⁶ (effective global minimum taxation of multinationals)

The OECD also released its [Economic Impact Assessment](#) of the blueprint proposals. Subsequent negotiation through the OECD/G20 Inclusive Framework has shifted many of the details from the blueprint proposals, most notably expanding the scope of Pillar One to go beyond digital companies, to target the top 100 largest and most profitable multinationals.

The OECD received 201 submissions related to Pillar One and 197 submissions related to Pillar Two from a range of businesses and organisations.

Range of stakeholders:

- Large multinationals, large accounting firms and tax justice advocates.

Key comments that were taken on board and noted:

- Continue pursuing implementation on of the Two-Pillar Solution.
- Find more ways to reduce compliance costs.
- Include an extractives carveout from Pillar One.
- Include large transition period for revenue sourcing rules.

Typical Pillar One Comments raised:

- Broad support for a multilateral solution.
- Business concerned about complexity.
- Submissions from Australian, American and Japanese interests supported the carve-out for extractives from Amount A and a broad interpretation that would cover the entire value chain for non-renewable, new and renewable resources. There was also support for the proposed exclusion of commodities and products such as petrol, diesel and automobile lubricants.

²⁵ Organisation for Economic Co-operation and Development (2020), Tax Challenges Arising from Digitalisation – Report on Pillar One Blueprint

²⁶ Organisation for Economic Co-operation and Development (2020), Tax Challenges Arising from Digitalisation – Report on Pillar Two Blueprint

- The novelty and complexity of Pillar One warrants a phased introduction (e.g. over several years), starting with a narrow group of multinationals.
- General support for the marketing distribution safe harbour concept, but consensus that it needs more work to be an effective double tax relief mechanism. Some suggested it should be expanded.
- Segmentation: Submissions generally opposed any mandatory segmentation for tax purposes.
- Revenue sourcing: Most submissions requested less stringent revenue sourcing rules. Many considered the proposed rules impractical and inflexible.
- Tax Certainty for Amount A: Some requests for expansion of tax certainty options (e.g. early certainty mechanisms, panels to advise on whether a company is in scope). There were some concerns over how the system will cope with demand, some suggestion access should be limited, at least to begin with.
- Unilateral measures: Most stakeholders suggested that existing unilateral measures, such as Digital Services Taxes or similar measures, must be withdrawn as a condition to the Pillar One and Pillar Two consensus.
- Dispute resolution beyond Amount A: Most of the submissions agreed that mandatory dispute resolution prevention is necessary to ensure tax certainty for multinationals. Some have suggested that public rulings be provided by the OECD. Submissions were generally supportive of mandatory binding dispute resolution beyond Amount A for all multinationals. Joint submission by NGOs expressed concern over the lack of transparency afforded to binding dispute decisions.

Typical Pillar Two Comments raised:

- Regime application: submissions called for the application of one regime (Pillar Two or unilateral measures), with GILTI (and similar regimes) being treated as Pillar Two compliant and interactions between GILTI and GloBE Model Rules needing to be addressed.
- Simplification options: Many submissions stated all options could be adopted and others further developed (e.g. a global ETR calculation). Varying views on appropriateness of a Country-by-Country safe harbour given the level of adjustments needed.
- ETR calculation:
 - Timing differences: submissions expressed that the carry-forward approach does not adequately address timing differences (particularly for extractives and insurance businesses), with deferred tax accounting being a better option. If the carry-forward approach is adopted, there should be no look-back period or it should be extended, or IIR tax credits more efficiently returned.
 - Transition: most stakeholders agreed that pre-regime losses should be fully recognised, and many considered carried-forward indefinitely.
- Covered Taxes: submissions sought more inclusions (those related to extractives, banks and Digital Services Taxes) or more certainty.
- Blending: submissions preferred worldwide-blending to jurisdictional-blending.
- Carve-outs:

- Exclusion for investment funds: several submissions sought refinements or clarifications.
- Further carve-outs: several submissions advocated for further carve-outs, particularly for Action 5 compliant regimes, and infrastructure.

Subject to Tax Rule (STTR): many submissions opposed the STTR, preferring it be limited and optional, and the covered payments need to be clear.

OECD Consultation: Pillar One Progress Report (2022)

Consultation Process

The OECD has continued public consultations on various aspects of the Two-Pillar Solution in order to inform the final aspects of the design. Consultation papers on the Pillar One (Amount A) building blocks have been released on a rolling basis, as the core design features of each building block have stabilised. In July 2022, the OECD also released a Progress Report on Pillar One for consultation.²⁷ The OECD received 71 submissions from business, lobby groups, advisors and individuals in relation to their public consultation document on the Progress Report of Amount A.


Range of stakeholders:

The Pillar One progress report received public submissions from 71 stakeholders. The range of stakeholders included business and business representation (66%), advisors (15%), civil society (6%), and other stakeholders (13%).

Key comments that were taken on board and noted:

- OECD to examine ways to further reduce complexity and compliance burdens, particularly for the Extractives exclusion.
- OECD to continue to develop the requirement to remove Digital Services Taxes as key component of Pillar One.
- Extractives exclusion:
 - Comments generally called for an expanded scope of the extractive definition to include more downstream services, such as processing that leads to the creation of refined raw materials.
 - Comments were also concerned by the complexity of the rules, and that they do not necessarily align to existing tax administration practices and concepts.
 - The rules were inherently complex in their current state; and
 - Concern that, due to the complexity, the rules would have no consistency in their application between tax administrations.
- Marketing & Distribution Safe Harbour:
 - Comments were generally concerned on what set of metrics would be used, such as depreciation and payroll;
- Elimination of Double Taxation:

²⁷ Organisation for Economic Co-operation and Development (2022), Progress Report on Amount A of Pillar One

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- Discussions focused on the administrative method by which double taxation would be relieved.
 - Withholding Taxes:
 - There is no consensus as to whether withholding taxes should be included in the Amount A calculations – with some countries noting their exclusion would allow double taxation while others noting that withholding taxes are a separate taxing right from Amount A.