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To: OECD Centre for Tax Policy and Administration

By e-mail: cfa@oecd.org

From: Foglia & Partners

Re: Comments on the Reports on Pillar One and Pillar Two Blueprints

Date: 14 December 2020

Ladies and Gentlemen,

We appreciate the opportunity to submit these comments on behalf of Foglia & Partners on the public consultation documents "Report on Pillar One Blueprint" ("**Pillar One Blueprint**") and "Report on Pillar Two Blueprint" ("**Pillar Two Blueprint**") released by the Organisation for Economic Cooperation and Development ("**OECD**") on 12 October 2020 (together the "**Blueprints**") and to contribute to the ongoing global discussion of these important tax policy matters.

In these comments, we first provide general observations on the Blueprints and then turn to some specific substantive topics and issues to be addressed also according to the public consultation document released on 12 October 2020 ("**Public Consultation Document**").

In order to facilitate the analysis of our comments, please find below a table of contents:

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A. Foreword and general comments on the Blueprints

As first, we would like to emphasise that we appreciate the work done and the steps forward taken from the previous consultation documents issued on 9 October 2019 and 8 November 2019, on the "Unified Approach"[1] and "GloBE"[2] proposals, respectively, also considering that this work was carried out despite the lack of global consensus among the members of the OECD/G20 Inclusive Framework on BEPS ("**Inclusive Framework**") and, therefore, political decisions are still required on several issues.

In addition, we noted that some observations submitted by the stakeholders[3] are in some way reflected in the Blueprints, denoting an actual involvement of the interested parties in the on-going projects, aiming to properly address and finalize the relevant topics.

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[1] We refer to the public consultation document "*Secretariat Proposal for a "Unified Approach" under Pillar One*" released by the OECD on 9 October 2019.

[2] We refer to the public consultation document "*Global Anti-Base Erosion Proposal ("GloBE") – Pillar Two*" released by OECD on 8 November 2019.

[3] Please also refer to our comments submitted on 12 November 2019 and 2 December 2019, on the "Unified Approach" and "GloBE" consultation documents, respectively.

However, we believe that – as a main guiding principle – the current complexity of the two Blueprints should be minimized as much as possible, to (i) achieve the set objectives, whilst (ii) seeking "tax certainty" and (iii) preventing additional new tax disputes arising from the implementation of the new systems under the Blueprints.

In this respect, following the rationale of the Blueprints, our comments are also grounded on the fact that any definitive solution to the matters should be built on the principles of simplicity, tax certainty and consistency among jurisdictions, avoiding double taxation, and minimizing (i.e. preventing) disputes.

In light of the above, as general comment with respect to each proposal, we can state that:

(i). the **Pillar One Blueprint**, and especially Amount A, is clearly designed and structured as a separate new income taxing right at the level of the MNE group as a whole, including a new nexus and a profit allocation rule. In particular, Amount A consists of a strictly formula-based system originating from accounting standards and not linked with the existing tax system based on the arm's length principle ("**ALP**").
However, with respect to certain aspects (e.g. Amount B and identification of "paying entities"), the Pillar One Blueprint still relies on the ALP, although such principle has not been adapted to the challenges of digitalisation.
As a result of such interaction and attempt to link the new system with the existing one (including the ALP), potential gaps and issues (e.g. "double counting") are around the corner[4].
Therefore, only a definitive system that is simple, transparent, and administrable will prevent the Pillar One project from introducing complexities that will trigger additional tax disputes between taxpayers and tax administrations, as well as among market jurisdictions;

(ii). the **Pillar Two Blueprint** is comprised of two proposals[5], which – either on

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[4] This is clearly acknowledged, inter alia, in paragraph 528 of the Pillar One Blueprint, where is stated that "*Amount A will be allocated as an overlay to the existing income tax system. This means interactions between Amount A and the existing income tax system are inevitable. The interactions between Amount A and the existing taxing rights of market jurisdictions on business profit, including withholding taxes, is conceptually challenging and an area where members have expressed different views. An important issue identified by the Outline is whether some of these interactions (i.e. between Amounts A and existing ALP-based profit allocation rules) could result in a duplicative taxation of the same profit of an MNE group in a particular market jurisdiction, which could be inconsistent with the policy intention of Pillar One (the issue of "double counting")*.".

[5] GloBE rules (applied through the income inclusion rule – "**IIR**", and undertaxed payment rule – "**UTPR**") with support from the switch-over rule ("**SOR**") as required; and (ii) a minimum level of tax on

domestic or treaty level and essentially independently of each other – ensure minimum levels of taxation of MNEs.
Whilst pursuing its set objectives, careful and effective co-ordination among the different measures of the Pillar Two package should be granted, in order to ensure that no unwanted over-taxation would burden taxpayers.
Moreover, on the same path of simplicity undertaken with respect to the Pillar One project, any possible interaction between the new designed measures under Pillar Two and the already existing provisions developed under BEPS Action Plan (e.g. country by country reporting, "**CbCR**") should be evaluated, in order to achieve the chosen objectives without placing an excessive burden on taxpayers, also seeking simplifications through the introduction of safe harbour packages.

Lastly, as already outlined in our comments on the previous consultation documents, as both Blueprints require – inter alia – domestic implementation and, namely, changes in the local law of the relevant jurisdictions, it will be crucial to correctly address their implementation phase and their joint impact and interactions, in order to avoid any unwanted distortion of the market and of the global tax environment, due to – by way of example – different timing of implementation in the different countries.

We are aware that this implementation process will be difficult and time-consuming to monitor, since it will (hopefully) involve all the BEPS participating countries. However, for this very reason, we strongly believe that it will be important to align – both in terms of timing and effectiveness – domestic implementation and the correct interaction between these new taxing rights in all the participating countries in order to avoid any cross-border distortion or disputes among the different market jurisdictions (and any consequent negative effects for the MNEs).

In this sense, as correctly pointed out in the Pillar One Blueprint[6], any risk of double taxation should be avoided by first removing any uncoordinated "unilateral measures" already adopted (or under development) by some countries and after implementing a robust, mandatory and binding dispute resolution process that can provide and guarantee both certainty and timely outcomes to taxpayers.

On the basis of this foreword, please find below our comments on the specific substantive topics to be addressed also according to the Public Consultation Document.

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certain payments between connected parties which are perceived to carry heightened base eroding potential (the subject to tax rule – "**STTR**").

[6] In particular, Chapter 10.3 ("*Removal of unilateral measure*"), paragraph 847, clearly states "*As stated in the Outline, it is expected that any consensus-based agreement must include a commitment by members of the Inclusive Framework to implement this agreement and at the same time to withdraw relevant unilateral actions, and not adopt such unilateral actions in the future.*".

B. Comments on the "Questions" formulated in the Public Consultation Document with respect to the Pillar One Blueprint

I. The activity test to define the scope of Amount A

The Pillar One Blueprint lays out a system under which a business would be within the scope of Amount A if (i) it performs in-scope activities and (ii) meets certain thresholds (i.e. the "global revenue threshold" and the "foreign in-scope revenue threshold").

The scope identified responds to the need to revisit taxing rules in response to a changed economy in which, given globalisation and the digitalisation of the economy, businesses can "*participate in an active and sustained manner in the economic life of a market jurisdiction*" with or without the benefit of local physical operations. This means that the allocation of taxing rights and taxable profits can no longer be exclusively circumscribed by reference to physical presence[7].

In this respect, "in-scope activities" under the Pillar One Blueprint include both "automated digital services" ("**ADS**") and "consumer-facing businesses" ("**CFB**").

ADS and CFB definitions

Firstly, we note that the ADS definition under the Pillar One Blueprint is significantly broader than the digital services taxes ("**DSTs**") scope under discussion in the European Union[8] and already implemented in Italy[9].

More in detail, under the activity test, the ADS "positive list"[10] includes "*online advertising services; sale or other alienation of user data; online search engines; social media platforms; online intermediation platforms; digital content services; online gaming; standardised online teaching services; and cloud computing services*"; while the "negative list"[11] of non-ADS activities includes "*customised professional services; customised online teaching services; online sale of goods and services other than ADS; revenue from the sale of a physical good irrespective of network connectivity ("Internet of things"); and services providing access to the Internet or another electronic network*".

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[7] Please refer to paragraph 22 of the Pillar One Blueprint.

[8] Please refer to the original proposal for Council Directive "*on the common system of a digital services tax on revenues resulting from the provision of certain digital services*" of March 2018.

[9] Introduced by Law 145/2018 and amended by Law 160/2019.

[10] Please refer to paragraph 29 of the Pillar One Blueprint.

[11] Please refer to paragraph 30 of the Pillar One Blueprint.

Notwithstanding the appreciable attempt to ring-fence in-scope digital services, also through a positive and a negative list, there are cases where the activity test may be challenging, thus requiring further technical guidance in order to avoid uncertainty and disputes about the actual characterization of an activity. By way of example, the positive list includes "standardised cloud services", but seems to exclude "customised cloud services"[12]. It is clear that distinguishing standardised cloud services (in-scope) from customised cloud services (out-of-scope) may be challenging without further in-depth technical guidance.

Moreover, the actual characterization of activities performed by businesses becomes even more challenging where an MNE is engaged in multiple activities that are not clearly severable and represent a "dual category" or "bundled package"[13]. In this respect, the Pillar One Blueprint requires relevant taxpayers to "unbundle" transactions to identify elements that are in scope and elements that are out of scope, in order to assess – inter alia – whether the ADS activity may be considered to be a "substantial part" of or highly integrated as part of an overall service. However, it is evident that such rule could significantly increase the complexity of Amount A and lead to many more disputes about whether a business activity is in-scope or out-of-scope.

As a result, we believe that an overall assessment of the "activity test" cannot be made without clear (and above all) straightforward guidelines regarding the correct segregation of bundled services; this also considering that most of the time digital businesses offer complex integrated services.

On the other hand, the broad coverage of the Pillar One Blueprint includes CFB, thereby comprising in the scope of the activity test also business that may not be purely "digital", but "*that generate revenue from the sale of goods and services of a type commonly sold to consumers, including those selling indirectly through intermediaries and by way of franchising and licensing*"[14].

In this respect, we believe that such inclusion of CFB could lead to complexities and conflicts also with respect to the current rules for the attribution of profits to existing permanent establishments ("**PEs**") in the market jurisdictions, for instance with respect

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[12] Please also refer to Chapter 2, Boxes 2.19 and 2.20, of the Pillar One Blueprint.

[13] Please refer to paragraph 48 of the Pillar One Blueprint.

[14] Please refer to paragraph 29 of the Pillar One Blueprint.

to the Amount B[15]; and thus – in the view of the inclusion of CFB in the scope of Pillar One – specific considerations also in this respect should be made.

"Safe harbour" election

The Pillar One Blueprint also recognises the United States' proposal to implement Pillar One on a "safe harbour basis"[16], subject to the replacement of digital services taxes and similar unilateral measures. In other words, under this proposal, MNEs would be able to "opt-in" to Amount A as a means to achieve enhanced tax certainty and to disapply any applicable unilateral measure on digital services.

Even if this alternative could eliminate the need to reach a global agreement on the ADS and CFB definitions, also leading MNEs to make such election in case they are subject to DSTs, we agree on the fact that – in such a case – the objective of Pillar One would be frustrated. Indeed, such "safe harbour" election could (i) incentive the introduction of a unilateral measure by the market jurisdictions as protection from the possible non-election of MNEs, thus creating (ii) distortions in the global tax environment among the different market jurisdictions.

II. The design of a specific Amount A revenue threshold (in addition to a global revenue threshold) to exclude large MNEs that have a *de minimis* amount of foreign source in-scope revenue

The Pillar One Blueprint defines two "threshold tests" which would need to be met in order for the activities of the MNEs to be considered in-scope:

(i) the "global revenue test", which would exclude MNEs having annual consolidated group revenue (shown in the consolidated financial statements) below the Euro 750 million threshold, as currently applied also for country-by-country reporting ("**CbCR**") purposes[17]. In this respect, the Pillar One Blueprint acknowledges that applying any lower global revenue threshold would increase compliance and

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[15] In this respect, the application of the Amount B, which generally follows ALP, may trigger inconsistencies with the remuneration attributable to a PE according to the Authorised OECD Approach in the 2010 "*Attribution of Profits to Permanent Establishments*".

[16] Please refer to paragraphs 165-169 of the Pillar One Blueprint.

[17] Even if, according to that stated in the Pillar One Blueprint (paragraph 175, note 25), it seems that no decision has yet been taken by the Inclusive Framework on the amount or design of the revenue thresholds for the application of Amount A.

administrative costs, while not leading to any substantial additional allocation of residual profits to market jurisdictions[18];

(ii) the "*de minimis* foreign in-scope revenue test", aimed at excluding MNEs which generate only a small portion of their revenues from "foreign" market jurisdictions. Under the Pillar One Blueprint this test would be set at an "absolute number" rather than relative to the size of the "domestic business" of the MNEs. If an MNE did not meet the *de minimis* foreign in-scope revenue threshold, it would not be included within the scope.
In other words, under this test, the amount of total revenue from in-scope activities (i.e., from ADS or CFB) should be determined first. Subsequently, it should be assessed whether this revenue is related to "foreign" activities, which are those activities that occur outside an MNE's "domestic or home market", based on the Amount A revenue sourcing rule.

With particular regard to the "*de minimis* foreign in-scope revenue test", the Pillar One Blueprint does not delimit a definitive approach to identifying the "domestic or home market"[19] of an MNE group. In this respect, for the sake of simplicity, the market jurisdiction in which the ultimate parent entity ("**UPE**") is resident may be the most suitable and straightforward criteria to identify the "domestic or home market" of an MNE group.

However, it is worth acknowledging that (for several reasons) the UPE market is not always the main market in which an MNE operates its business. As a result, by adopting this approach there could be the risk that – for instance – the revenues earned by an MNE group in only one additional market where it is headquartered would be characterised as "foreign in-scope revenues", thus debasing the actual purpose of the test at hand, aimed at avoiding the allocation of the Amount A tax base in the same jurisdiction that already has taxing rights under the current ALP-based allocation rules[20].

As a result, the chance of introducing a "rebuttable presumption" should be investigated, according to which the UPE residence market is – in principle – the "domestic or home market" (for the sake of simplification), whilst providing the MNEs with the chance to reject such a presumption on the basis of specific criteria and requirements aimed at identifying the actual "home market" of the MNE group.

[18] Please refer to paragraphs 179-180 of the Pillar One Blueprint.

[19] Please refer to paragraph 184 of the Pillar One Blueprint.

[20] Please refer to paragraph 184 of the Pillar One Blueprint.

III. The development of a nexus rule

Differently from ADS (for which a nexus is established when exceeding a certain market revenue threshold), under the Pillar One Blueprint, for CFB "*the ability to participate remotely in a market jurisdiction is less pronounced*"[21]; thus specifying that "*This, together with the additional complexity and compliance costs associated with sourcing revenue derived by CFB (e.g. third party distribution) and the broad acknowledgement that profit margins are typically lower for CFB compared with ADS , could justify a higher nexus standard for CFB*". According to the Pillar One Blueprint this "higher nexus standard" could be achieved by applying (i) a market revenue threshold in conjunction with (ii) one or more "plus factors" (indicating a sustained engagement with the market).

With regards to this latter requirement, the Pillar One Blueprint identifies "physical presence" in the form of a subsidiary or PE in the market jurisdiction as a possible "plus factor". In this respect, the existence of a PE in the market jurisdiction would be determined using a single self-standing "group-permanent establishment" ("**group-PE**") definition, instead of relying on PE definitions in tax treaties or domestic law[22]. This group-PE test would be based on the commonalities of the PE definitions in the UN and OECD Model Income Tax Conventions, though further work would be needed in certain areas.

On this point, we highlight that, even if the group-PE definition to be introduced under the Pillar One Blueprint is not intended to affect the application of PE rules in existing tax treaties or domestic legislation, it will however be difficult to effectively segregate these concepts. As a result, it will be likely that the new "group-PE" concept will suffer all the interpretation issues and tax uncertainties that the PE definition has caused over the recent years to MNEs (especially the "digital" ones) in the context of tax audits.

Therefore, on the basis of the experience in tax audits on PE matter and also taking into account the possible behaviour of tax administrations (which would be interested in identifying a possible group-PE to claim the right to a share of Amount A), the concern is that the introduction of a "plus factor" linked to the "physical presence" could create uncertainty in the application of Amount A.

As a result of the above, if the political agreement is to include CFB in the scope, seeking simplicity, we agree that for CFB, a straightforward alternative method as the "deemed

[21] Please refer to paragraph 191 of the Pillar One Blueprint.

[22] Please refer to paragraph 210 of the Pillar One Blueprint.

engaged" provision[23], based on a certain market revenue threshold, would avoid the complexities and uncertainties that more factual and expansive plus factors would create. However, we believe that – in such a case, in line with paragraph 213 of the Pillar One Blueprint – the relevant market revenue thresholds should be calibrated to ensure – *inter alia* – that jurisdictions with smaller economies can also benefit from the new rules. More in detail, this calibration could be reached by agreeing on different revenue thresholds for each industry, also taking into account the level of economies of each country on a global scale. In this sense, the relevant threshold could be periodically updated on the basis of the underlying rationale chosen.

Finally, with respect to the "temporal requirement" for market revenues threshold, we believe that, as outlined in the Pillar One Blueprint, a "multiple-year" approach would help to avoid covering isolated or one-off transactions that may not demonstrate a sustained level of engagement with a market. Moreover, such approach would prevent distortions caused by: (i) the seasonality of some businesses (achieving most of their revenues at the end of a certain fiscal year and the start of the following one); (ii) any attempt to circumvent the revenue threshold test by postponing or antedating revenues.

IV. The development of revenue sourcing rules

Chapter 4 of the Pillar One Blueprint lays out detailed sourcing rules that would determine where revenue is deemed to arise for the purposes of determining scope and nexus, and for making Amount A allocations. These rules vary significantly between ADS and CFB, and among different business models within those broad categories.

More in detail, MNEs would be required to apply the first indicator in the "hierarchy" provided for each category of business (such as geolocation of the user, Internet Protocol (IP) address, user profile information) unless this information is "unavailable" or "unreliable". As a result, in principle, lower-level indicators could be used for revenue sourcing purposes only if higher priority indicators are not "reasonably available" or are "unreliable". In this respect, according to the Pillar One Blueprint:

(i) information would be considered "unavailable" if it is not in the MNE's possession, and "reasonable steps" taken to obtain it have been unsuccessful[24]. Only once such

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[23] Described in paragraph 212 of the Pillar One Blueprint, according to which "*One approach could be, therefore, to assume that once a group's CFB sales in a market reach a certain threshold it will no longer be necessary to establish the existence of plus factors (i.e. the group could be treated as having a nexus). This deemed engagement provision would avoid the complexities and uncertainties that more factual and expansive plus factors would create, but further policy discussion is needed*".

[24] Please refer to paragraph 292 of the Pillar One Blueprint.

steps are taken and the information is unable to be obtained by the MNE may it move on to a secondary indicator;

(ii) information would be considered "unreliable" if the MNE can justify that the indicator is not a true representation of the principle in the source rule[25].

With respect to the above sourcing rule, it is worth noting that for transactions in which the customer is a business (e.g. revenue from consumer-facing goods sold through an independent distributor), a significant number of indicators require obtaining information from the third-party business customer about the location of the ultimate consumer of the good or service. Under a practical standpoint, obtaining the required information from business customers or independent distributors will likely be challenging, and will trigger additional compliance costs and complexity for MNEs.

In other words, differently to that assumed in the Pillar One Blueprint[26], such an indicator may require additional costs and complexity for MNEs which – according to the "reasonable steps" currently provided – will also have to "*seek to change in the contractual arrangement with the distributor*"[27] before using alternative data sources.

Moreover, in order to seek certainty and avoid disputes, we believe that the Pillar One Blueprint should:

(i) provide objective or bright line tests to ascertain when an MNE has exercised "reasonable" (and not excessively burdensome) steps to collect information;

(ii) clarify the extent of inquiry required by an MNE to determine whether information it possesses accurately reflects a sourcing principle;

(iii) set a precise methodology of "tracking and reporting", especially for revenues made in markets through non-related distributors.

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[25] Please refer to paragraph 293 of the Pillar One Blueprint.

[26] Please refer to paragraph 402 of the Pillar One Blueprint, according to which "*asking the holder of the information (such as the customer or distributor), but would not be expected to include a requirement to incur more than insignificant costs (such as a not insignificant increase in price as part of a renegotiation of a contract)*".

[27] For example, please refer to paragraph 379 of the Pillar One Blueprint on "*Revenue from consumer-facing goods sold through independent distributor*".

V. The framework for segmenting the Amount A tax base, and how it could be further developed to deliver its objectives

Under the Pillar One Blueprint view, though it is feasible for taxpayers to break down their revenues into ADS, CFB and out-of-scope, it may not be possible for them to compute separately the net profits attributable to these activities (i.e. segmentation of the tax base). On the basis of such consideration and also taking into account that the "new system" applies the principle of net (rather than gross) basis taxation, in order to reallocate profits attributable to in-scope activities, the Pillar One Blueprint suggests calculating "*the Amount A tax base on a consolidated basis and use the consolidated profit margin of the group as a proxy for the in-scope profit margin, applying it to in-scope revenues to produce a proxy for in-scope profits*"[28].

In a nutshell, under the segmentation framework provided in the Pillar One Blueprint, the following three-step process can be outlined:

(i) MNEs in scope of Amount A would break down their revenue into ADS, CFB and out-of-scope activities;

(ii) to limit the number of MNEs required to segment their Amount A tax base, MNEs with global revenue less than an as yet undefined amount would benefit from a "segmentation exemption", which would require them to compute the Amount A tax base on a "group basis". The Pillar One Blueprint notes that, alternatively, this exemption could be designed as a "safe harbour";

(iii) MNEs not eligible for the "segmentation exemption" (or that do not elect for the safe harbour, if designed as such), would then test whether they are required to segment their Amount A tax base and on what basis, using the three sub-step criteria[29], which includes a "segmentation hallmark" to determine whether the

[28] Please refer to paragraph 412 of the Pillar One Blueprint.

[29] According to such three-sub-steps summarised in paragraph 413 of the Pillar One Blueprint:

- "*MNEs will apply the as yet undefined "segmentation hallmarks" to determine whether they are required to segment their tax base. If they are not required to segment, they will compute their Amount A tax base on a group basis;*
- *For MNEs that do display these segmentation hallmarks, the disclosed segments in the MNE group financial statements will be tested to ascertain whether they meet the agreed hallmarks. If so, Amount A tax base will be computed on the basis of these segments. There will be an exemption for groups whose disclosed segments have similar profit margins to compute the Amount A tax base on a group basis.*

relevant MNE is required to segment its tax base.

Under the Pillar One Blueprint, these "segmentation hallmarks" are yet to be determined, but might be based on the now-superseded guidance of International Accounting Standard ("**IAS**") 14, which supplied a set of factors for determining whether segmentation should be applied and preceded the more flexible approach currently adopted under IFRS 8[30].

In this respect, we note that such superseded accounting standard was not originally formulated or issued with particular regard to "digital" business, so there is no guarantee that the criteria provided therein would appropriately determine whether an MNE group is required to segment its tax base (especially considering the several different features of the various digital businesses). As a result, it cannot be excluded that tax authorities may not agree with management's segmentation choices, with potential challenges and disputes in this respect.

In light of the above, as a general comment, always on the path of simplicity and tax certainty, we believe that the adoption of only the consolidated account financials would avoid introducing further areas of complexity and dispute.

In this respect, it is also worth noting that, differently from consolidated financials, generally geographical/regional segmentations, as well as "business segmentation" would not exclude "inter-segment transactions", which may lead to artificial shifting of profits and losses among the different segments.

As a result of the above, we believe that the closer you can get to consolidated audited financials, the fewer disputes are likely to arise over the accuracy of financials used for the Amount A tax base calculation.

VI. The development of a loss carry-forward regime that would ensure that Amount A is based on an appropriate measure of net profit

According to the Pillar One Blueprint approach, loss carry-forward rules will apply through an "earn-out" mechanism, according to which losses generated over a given tax period under Amount A ("in-regime" losses) will not be allocated to market jurisdictions,

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- *MNEs that are not eligible to use their disclosed segments will be required to compute the Amount A tax base on the basis of alternative segments. The report states that this is expected to be relevant for only a small number of MNEs.*".

[30] Please refer to paragraph 458 of the Pillar One Blueprint.

but pooled in a "single account" (at the level of the adjusted group PBT as a whole or, where the segmentation framework applies, at the level of the relevant segment)[31]. As a result, under this mechanism, no profit under Amount A would arise for that "single account" until historical losses reported in such account have been fully absorbed[32].

In addition, the introduction of a transitional regime which would allow certain net "pre-regime" losses (i.e. losses incurred before the introduction of Amount A that exceed profits earned during that pre-regime period) to be preserved and deducted against Amount A in-regime profits is under discussion.

With respect to the possible implementation of such "pre-regime" loss carry-forwards, it is worth considering that the businesses in the scope of Pillar One (e.g. digital businesses or businesses without physical presence) typically have models with long-term and costly initial investments, and thus would likely suffer the most from an arbitrary restriction on the availability of "pre-regime" losses.

Therefore, if losses incurred by those businesses in a multinational's jurisdiction of residence are arbitrarily restricted (e.g. with a specific time limitation) while profits are subject to allocation to market jurisdictions, there would be systematic over-taxation of those MNEs, as well as profit allocation that does not fairly represent the value created in market jurisdictions.

The above considerations are further supported by the circumstance that companies that have accumulated profits may also incur cyclical losses, especially in the context of the COVID-19 environment and of the relevant period of financial crisis.

In addition, we point out that even if economic (and "symmetry") principles suggest that ("in-regime" and "pre-regime") losses should be allocated to market jurisdictions and allowed to be used or carried forward indefinitely, that approach is likely not pragmatic and unlikely to be acceptable to many countries whose current practices are incompatible with it. As a result, seeking simplicity, we believe that the more pragmatic approach is the "earn-out" mechanism adopted in the Pillar One Blueprint both with respect to "pre-regime" and "in-regime" losses.

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[31] Please refer to paragraph 458 of the Pillar One Blueprint.

[32] As clearly stated in paragraph 486, the Amount A loss carry-forward regime will be kept separate from any existing domestic loss carry-forward rules. This means that losses generated at entity level under the ALP-based profit allocation system would not alter the Amount A tax base, nor vice versa.

VII. The scope and relevance of possible double counting issues arising from interactions between Amount A and existing taxing rights on business profits in market jurisdictions

The overlay of Amount A on top of existing taxing rights could lead to duplicate taxation of the same MNE group profit in multiple jurisdictions (i.e. "double counting").
In this respect, the Pillar One Blueprint seeks to address "double counting" issues, *inter alia*, through the "marketing and distribution profits safe harbour"[33] and the "domestic business exemption"[34].

With specific reference to the first method, the "marketing and distribution profits safe harbour" "*would cap the allocation of the Amount A to market jurisdictions that already have taxing rights over a group's profit under existing tax rules*"[35]. Such "cap" is represented by the "safe harbour return", calculated as (a) the allocable Amount A as computed by the formula, plus (b) the "fixed return for in-country routine marketing and distribution activities" (which could include regional and industry uplifts).

With respect to this latter item, it is not clear in the Pillar One Blueprint whether and how (i) the routine marketing and distribution profit measure that would be used for the marketing and distribution safe harbour would relate to either the (ii) fixed profitability threshold used in the first step of the Amount A calculation, or (iii) the Amount B return for baseline sales and distribution activities. Therefore, further clarification would be needed on their interaction.

Even if we understand that the "fixed return" at hand "*would not seek to be consistent with the ALP*"[36], nevertheless, for sake of simplification and in the light of the similar purposes of the above three items, the chance to provide for a common agreed measure for all of them could be investigated. Indeed, such a solution, could simplify the overall Pillar One mechanism and would also facilitate political agreement within the Inclusive Framework, that will have to define only a single set of "fixed remunerations" (per country and industry).

Stated the above, even if we know that a single "fixed return" applicable across the countries would certainly simplify the situation, we believe that – in order to properly limit

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[33] Please refer to paragraphs 533-546 of the Pillar One Blueprint.

[34] Please refer to paragraphs 547-553 of the Pillar One Blueprint.

[35] Please refer to paragraph 533 of the Pillar One Blueprint.

[36] Please refer to paragraph 533 of the Pillar One Blueprint.

"double counting" within the Amount A mechanism – the "fixed returns" to be defined for in-country routine marketing and distribution activities should have to be aligned as much as possible to the ALP, also taking into account (i) the industry sector and (ii) the level of economies of each country/region on a global scale. Such approach would also be in line with the Amount B "quantum" determination outlined in section 8.2.2. of the Pillar One Blueprint.

Lastly, we note that the above theoretical alignment of the "fixed return for in-country routine marketing and distribution activities" with the ALP would also support the concept that, in case of transfer pricing adjustments, any additional tax due under the existing profit allocation rules being offset against the tax that would no longer be due under Amount A.

VIII. The development of a process to identify the entities in an MNE group that bear the Amount A tax liability (the paying entities) for the purpose of eliminating double taxation

In order to identify the entity/entities liable to pay the Amount A tax liability (i.e., the "paying entities"), Pillar One contemplates four steps: (i) the "activities test" (step one); (ii) the quantitative "profitability test" (step two); (iii) the "market connection priority test" (step three); and (iv) the "pro-rata allocation" (step four)[37].

Focusing on first step one, namely the "activities test", we note that paying entities are not identified using the Amount A allocation methodology (e.g., PBT/revenue, in excess of x%), but through a kind of analysis that reflects transfer pricing DEMPE and risk analysis under the OECD Transfer Pricing Guidelines ("**TPG**")[38]. In this respect, it is also specified that "*the transfer pricing master file and relevant local files prepared by MNE groups provide a first point of reference for the application of the activities test*"[39].

Such a method, based on the analysis of the functions, assets and risks in relation to intangibles is to some extent at odds with the formulaic nature of Amount A, triggering complexity in a "core" step of the overall Pillar One mechanism, which instead, requires

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[37] Please refer to paragraph 560 of the Pillar One Blueprint.

[38] Please refer to paragraph 582 of the Pillar One Blueprint, where the relevant footnote also specifies that the "*OECD (2017), Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, OECD Paris, paragraphs 1.60, 1.61, 6.51 and 6.56 constitute primary sources of reference, together with further examples derived from the concepts outlined.*".

[39] Please refer, *inter alia*, to paragraph 580 of the Pillar One Blueprint.

simplicity (i.e. who pays taxes). Indeed, the Pillar One Blueprint seems not to consider that within an MNE group there might be many intangibles, whose key DEMPE functions might be managed by multiple entities. Therefore, a DEMPE method would be difficult to apply.

Moreover, it's worth noting that – in general – there is still a lot of uncertainty on the correct application of the DEMPE approach and, in this respect, we have experienced a high degree of subjectivity in the assessment of transactions involving intangibles on the part of tax administrations.

In this respect, the Pillar One Blueprint clearly recognises that transfer pricing audits may have an impact on the identification of the paying entity, explicitly stating that "*Transfer pricing audits may also lead to a reassessment of an entity's FAR profile, its characterisation for transfer pricing purposes and the transfer pricing method used to determine its arm's length profits, which may have an impact on whether the entity has been correctly identified (or not identified) as a paying entity*"[40].

As a result, in practice, we believe that the identification of the paying entities through the "activity test" under step one could be a challenge, especially in cases where there are MNEs entities that carry out both routine and non-routine activities, with the risk that, as a result of a transfer pricing audit: (i) the paying entity could be disregarded and, as a consequence, (ii) the tax administration could also deny the double taxation relief originally granted to such paying entity; or otherwise (iii) an entity that an MNE group has not classified as "paying entity" could be classified as such.

On the basis of the foregoing, we believe that, instead of the four-step approach formulated under the Pillar One Blueprint, simplifications should be explored in this identification mechanism, for example by developing only a single bright and straightforward "profitability test" (to be applied on financials), in line with the formulaic approach pursued under Pillar One, in order to identify paying entities that have the capacity to bear the Amount A tax liability.

IX. The issue of scope of Amount B and definition of baseline marketing and distribution activities

Summarising the rationale underlying the Amount B, as outlined in the Pillar One Blueprint, we note that it "*aims to standardise the remuneration of related party distributors that*

[40] Please refer to paragraph 615 of the Pillar One Blueprint.

perform "baseline marketing and distribution activities" in a manner that is aligned with the ALP"[41]. More in detail, its purpose is two-fold: "*First, Amount B is intended to simplify the administration of transfer pricing rules for tax administrations and reduce compliance costs for taxpayers. Second, Amount B is intended to enhance tax certainty and reduce controversy between tax administrations and taxpayers.*"[42].

Having regards to the above principles and in order to seek the simplicity originally pursued by the proposal, we believe that Amount B (i) should be introduced as a "rebuttable presumption", and that (ii) its scope should be as broad as possible.

Following such a design, this mechanism would allow MNEs in the scope of Amount B (and thus owning the "indicators" that will be ultimately defined) to set the margin of their "baseline" entities according to the remuneration proxies provided (thereby (i) reducing compliance costs and (ii) avoiding transfer pricing disputes and controversies), save that the relevant MNEs would provide evidence that another transfer pricing method would be the most appropriate to use under the ALP[43].

On the basis of the foregoing, the broader the scope of Amount B would be set, the higher the chance would be for MNEs and tax administrations respectively to (i) avoid compliance costs related to transfer pricing benchmarking and (ii) simply carry out transfer pricing audits on the matter. In this respect, we suggest that "commissionaires" and "sales agents" should also be included in the scope of the Amount B, also taking into account the subtle difference between these functional profiles with respect to "routine marketing and distribution activities"[44].

For the same reason as above, we believe that the application of Amount B to multifunctional entities with in-scope transactions should be possible, but subject to an accurate delineation of the transactions – according to TPG – indicating that that the "Amount B activities" and the "additional transactions" performed by the entities are not so closely linked that they cannot be evaluated adequately on a separate basis.

We understand that a broader scope would further complicate the implementation of Amount B, thus requiring, *inter alia*, (i) the review and integration of the "positive" and "negative" list of indicators designed, as well as a (ii) changes in existing domestic law and

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[41] Please refer to paragraph 649 of the Pillar One Blueprint.

[42] Please refer to paragraph 650 of the Pillar One Blueprint.

[43] As proposed in paragraph 654 of Pillar One Blueprint.

[44] As also noted at paragraph 684 of the Pillar One Blueprint.

treaties, but, if properly designed and implemented, it could be a great chance to integrate tax certainty into the transfer pricing environment.

X. The appropriate profit level indicator for calculating Amount B, and how it should be calculated assuming Amount B is based on a narrow scope

Considering that the fixed return provided to remunerate baseline marketing and distribution activities under Amount B is intended to deliver a result that approximates results determined in accordance with the ALP, and that the TNMM has been identified by the Pillar One Blueprint as the most appropriate transfer pricing method for activities in scope of Amount B[45], we tend to believe that, in general, the return on sales set on the (potentially adjusted) EBIT should be a reasonable profit level indicator, reflecting the remuneration attributable to such baseline services within the scope[46].

Moreover, as a general principle[47], in setting Amount B fixed returns as much as possible in accordance with the ALP, different margins need to be proposed, as the margins applied for baseline distribution or marketing activities differ from one industry to the next. For example, the margins applicable to distribution structures in the fast-moving consumer goods sector are different from the margins applicable in the luxury goods, chemical or pharmaceutical sectors.

Likewise, such fixed margins will also have to be calibrated with respect to each region/country, thereby reflecting the specific characteristics and market conditions of each region/country (e.g. market restrictions, regulatory framework).

As an alternative to many different fixed remunerations (by country and industry), the above industry/region "calibration" may be designed as a (periodically updated) adjustment (e.g. uplift) to the base fixed remuneration to be determined for the baseline activities that will be included in the scope.

[45] Please refer to paragraphs 685-686 of the Pillar One Blueprint.

[46]EBIT figures are usually used to calculate net profits in transfer pricing analysis (although in a separate entity context). Please refer to OECD TPG 2017, Section B.3.3. paragraphs 2.83 - 2.91 (with an emphasis on paragraph 2.86). However, further consideration will have to be made once all the functional profiles within the scope of Amount B are defined.

[47] In line with that proposed in Section 8.2.2. of the Pillar One Blueprint.

XI. The development of an early tax certainty process to prevent and resolve disputes on Amount A

Taking into account the complex system currently provided in the Pillar One Blueprint, the still unclear scope of Amount A, as well as the self-assessment procedure designed, the "early tax certainty process" would represent an important instrument, allowing MNEs to gain "tax certainty" on the overall Amount A process[48]; this, especially considering that affected tax administrations ("**ATAs**") should not commence any audit activity or issue assessments with respect Amount A for the relevant tax year pending the outcome of the certainty procedure[49].

The main challenge in the early tax certainty process will surely be related to the actual management of the entire process by the several tax administrations: an excessive length on the tax certainty mechanism may discourage MNEs to submit a request for the early certainty process.

In this respect, the optional initial review by the lead tax administration ("**LTA**") could ultimately be one of the most significant elements of the early certainty procedure, as it could screen out low-risk taxpayers and avoid time-consuming and administratively burdensome panel processes. This could be particularly important during the early years of implementing Amount A, as tax authority requests for review panels could exceed the capacity of the relevant administrations to undertake such reviews. Therefore, the entering by the LTA in such an initial review must in some way be stimulated.

As a result of the above, we believe that some of the features that may encourage MNEs to enter into the early certainty procedure would be:

(i) precise and short deadlines for each step of the procedure; as well as

(ii) extended duration of the effects of the process determination. In this respect, for instance, the chance to provide multiple-year effects to the process determination could be investigated, save for changes in the facts and circumstances at the base of it (e.g. if, as a result of a procedure, a MNE group is not considered within the scope of amount A, it will be considered as such until any change in the business model is made).

Lastly, we believe that in the context of the overall procedure the UPE would reasonably

[48] Including whether an MNE group is within the scope of Amount A.

[49] Please refer to paragraph 733 of the Pillar One Blueprint.

be the most suitable company to be the co-ordinating entity, since it generally has (or can gather) the information needed and requested by the LTA about the MNE group for the purposes of the Amount A process.

However, to provide flexibility and in some way spread the work among tax administrations, the chance to let the MNEs decide and appoint the most qualified group entity to take on this role could be explored.

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C. Comments on the "Questions" formulated in the Public Consultation Document with respect to the Pillar Two Blueprint

As already outlined in our comments on the previous GloBE consultation, in general, we believe that the goal of a fair and simple tax base for GloBE purposes could be achieved by providing only certain simple and straightforward targeted adjustments to the financial results of MNEs in order to align the accounting results with a proper measure of taxable income, thereby also obtaining a harmonised tax base determination criteria across jurisdictions.

In this respect, we welcome and acknowledge the analysis and work done in the Pillar Two Blueprint with respect to adjustments that will need to be made to financial accounting rules for GloBE effective tax rate ("**ETR**") purposes. However, we believe that the current package should be simplified in order to find a proper balance between the Pillar Two objectives and the relevant additional compliance burdens that taxpayers would suffer.

On the basis of the foregoing, please find below our comments.

III. Chapter 3: Calculating the ETR under the GloBE Rules

The GloBE ETR is determined by dividing the amount of "covered taxes" by the amount of income as determined under the GloBE rules. Under the Pillar Two Blueprint, the GloBE rules start with the financial accounts that are prepared under the same accounting standard that is used by the parent of the MNE to prepare its consolidated financial statements. The rules then require certain adjustments to be made to the tax base, *inter alia*, "*in order to more closely align the GloBE tax base with the computation of taxable income under the rules of the jurisdiction where the MNE operates*"[50].

[50] Please refer, *inter alia*, to paragraph 175 of the Pillar Two Blueprint.

On this basis, taking into account that in many Inclusive Framework jurisdictions, dividends and gains from the disposition of stocks in a corporation are generally excluded, in whole or in part, from the taxable income, based on the Pillar Two Blueprint only dividends and stock gains where the MNE groups own a low percentage of equity interests (to be defined[51]) are included in the GloBE tax base.

In this respect, we tend to believe that it would be consistent and appropriate to exclude from the GloBE tax base also the related expenses, which could be identified on the basis of the relevant applicable accounting standard.

On the other hand, to address timing differences introduced by immediate expensing and accelerated depreciation of business assets, the Pillar Two Blueprint has identified two possible solutions, either: (i) a deferred-tax based approach[52] or (ii) an approach based on the use of (local) tax depreciation rules in the ETR calculation[53].

Subject to an assessment based on the overall design of the GloBE proposal, in principle, either method may be acceptable for the purpose of finally neutralising such timing differences. However, we tend to believe that the deferred tax-based approach would (i) likely result in a smaller administrative burden and (ii) also seems more suited to consistently address timing issues arising from book and tax accounting differences in general.

Although making further tax adjustments or deferred-tax adjustments of course add complexity to the GloBE calculation, we acknowledge that it should, however, be advantageous – from a financial perspective – to mitigate the risk of depreciation timing differences resulting in IIR taxation in one year and "excess tax" in later years.

In any case, regardless of the method that is eventually adopted, we believe that it is

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[51] Please refer, *inter alia,* to paragraphs 182 and 191 of the Pillar Two Blueprint.

[52] As illustrated in paragraph 222 of the Pillar Two Blueprint "*Deferred tax accounting neutralises the effect on the ETR of immediate expensing and accelerated depreciation for tax purposes, just like any other temporary difference. Leveraging from deferred tax accounting principles, the carry-forward approach could be modified such that the numerator of the ETR fraction (i.e., taxes paid) is increased by the deferred tax liability associated with an investment in property or accelerated depreciation during the year.*"

[53] As illustrated in paragraph 223 of the Pillar Two Blueprint "*Another approach would be to compute the GloBE tax base using the cost recovery allowance or depreciation rates and conventions that the MNE used for local tax purposes in place of the depreciation rates and rules used for financial accounting purposes. Under this approach, the local tax depreciation rules would be applied to the carrying cost of assets as determined for financial accounting purposes. The relevant depreciation rules would include depreciation rates, depreciation periods, and placed in service conventions. It would not, however, permit deductions in excess of the actual cost of the asset.*".

important to combine it with a strong (local tax) carry forward regime.

Finally, we agree that – consistently with the jurisdictional blending under the Pillar Two Blueprint – cross-jurisdictional taxes, such as withholding taxes and controlled foreign corporation ("CFC") tax should be included as covered taxes within the GloBE tax base for the entity which books the income the tax is levied on (e.g., for withholding taxes, the recipient of the dividend, interest, royalty or service fee).

In this respect, a specific anti-avoidance rule could be developed in order to disregard "artificial" flows substantially "aimed at shelter" income arising in low-tax jurisdictions from GloBE rules.

IV. Chapter 4: Carry-forwards and carve-out

Treatment of pre-GloBE losses and excess taxes under the carry-forward approach

By supporting the need for "transactional rules"[54] to ensure that pre-regime losses and excess taxes are duly taken into account for GloBE tax liability purposes, we believe that – in line with that already argued with respect to the Pillar One Blueprint – an unlimited (i.e. without time restriction) carry-forward of such "tax assets" should be allowed.

Indeed, it is clear how failure to take appropriate account of such items could result in a distorted picture of the MNE group's tax position in that jurisdiction, and may subject the MNE group to taxation in excess of its economic profit[55]. In other words, providing a time limit for such carry-forward would amount in a high risk of over-taxation of the relevant MNE beyond the purposes of the GloBE rules. This is a critical issue also considering the ongoing burdensome context of the COVID-19 crisis, which currently entails devastating economic effects on many businesses.

In terms of compliance, the obligation to establish and maintain carry-forward accounts would rest on the taxpayer, with no additional administrative burden placed on tax authorities or on taxpayers that do not demand to carry-forward from "pre-regime" periods.

The foregoing being stated, we however highlight that the following technical issues are to be addressed:

[54] As acknowledged in paragraph 315 *et seq.* of the Pillar Two Blueprint.

[55] As recognised in paragraph 316 of the Pillar Two Blueprint.

(i). the definition of "pre-regime losses" indicated in paragraph 287 of the Pillar Two Blueprint provides that "*Losses also include* ***qualified*** *pre-regime losses that are incurred by a Constituent Entity prior to the MNE Group becoming subject to the rules*." (emphasis added). However, the Pillar Two Blueprint seems not to address how a pre-regime loss can be characterised as "qualified". In this respect, the possibility that the term "qualified" would indicate pre-regime losses "determined according to GloBE rules" would amount to a burdensome (and maybe, in certain cases, impossible) complexity for many businesses that have a long-term business cycle and losses originating from many years ago. As a result, for the sake of simplicity, we would suggest eliminating such characterisation from the relevant definition of "pre-regime losses", thus allowing the company to carry forward pre-regime losses determined according to the relevant local tax rule;

(ii). it is not clear how the carry-back, to the extent permitted under the laws of the relevant jurisdiction, is to be aligned with the GloBE rules. For instance, in cases where domestic law allows a carry-back of losses on an entity-by-entity basis, there is uncertainty about how the carry-back of losses will be treated and allocated for the purposes under the GloBE rules. Therefore, we suggest that clear guidance in this respect be provided.

Formulaic substance-based carve-out

The Pillar Two Blueprint proposes an adjustment to the GloBE tax base to carve out a fixed return based on a payroll component and some tangible asset components. More in detail, such carve-out is computed on a jurisdictional basis, as the sum of:

- a fixed percentage of the "depreciation" of property, plant and equipment, taken into account in the jurisdiction of the Constituent Entity that uses the assets[56];

- a fixed percentage of the "deemed depreciation" of land, taken into account in the jurisdiction in which the land is located[57];

- a fixed percentage of the "depletion" of natural resources, taken into account in the jurisdiction in which the natural resource is located[58]; and

[56] Please refer to paragraph 353 of the Pillar Two Blueprint.

[57] Please refer to paragraph 358 of the Pillar Two Blueprint.

[58] Please refer to paragraph 363 of the Pillar Two Blueprint.

- a fixed percentage of the "depreciation" of a lessee's right-of-use tangible asset, taken into account in the jurisdiction of the Constituent Entity lessee that uses the property in its business[59].

While recognising and sharing the purpose of the carve-out, we note that some calculation criteria should be revised, as it could undermine its actual purpose (i.e. acknowledging the contribution to the business of both employees and tangible assets). Indeed, considering that a method based on a percentage of depreciation would entail a return that is too low to reflect the actual contribution of assets to the business, we suggest that the relevant calculation be based on the "carrying value" of the assets rather than on their "depreciation".

From an economic perspective, such an approach would be in some way also consistent with the TPG, which provides that a return on assets is appropriate in evaluating the profits of manufacturing or other asset-intensive activities[60].

V. Chapter 5: Simplification options

The Pillar Two Blueprint illustrates four potential simplification measures, including (i) Country by Country Report ETR safe harbour[61] ("**CbCR ETR Safe Harbour**"), (ii) *de minimis* profit exclusion[62], (iii) single jurisdictional ETR calculation to cover several years[63], and (iv) tax administrative guidance[64].

On the basis of our thoughts formulated with respect the needs of simplification of the overall proposal, already expressed with respect to the previous GloBE consultation[65], we welcome the possible introduction of these simplification options that – in our view –

[59] Please refer to paragraph 369 of the Pillar Two Blueprint.

[60] Please refer, *inter alia*, to the OECD Transfer Pricing Guidelines 2017, paragraphs 2.98 and 2.103.

[61] Please refer to paragraphs 381-390 of the Pillar Two Blueprint.

[62] Please refer to paragraphs 391-398 of the Pillar Two Blueprint.

[63] Please refer to paragraphs 404-409 of the Pillar Two Blueprint.

[64] Please refer to our comments submitted on 2 December 2019 with respect to the public consultation document "*Global Anti-Base Erosion Proposal ("GloBE") – Pillar Two*", issued by the OECD on 8 November 2019.

[65] Please refer to our comments submitted on 2 December 2019 with respect to the public consultation document "*Global Anti-Base Erosion Proposal ("GloBE") – Pillar Two*", issued by the OECD on 8 November 2019.

should all be integrated together and simultaneously implemented, in order to achieve a higher grade of simplification for MNEs falling under the Pillar Two scope.

The foregoing being stated, please find below our specific considerations with respect to each measure:

(i). CbCR ETR Safe Harbour:
Under this safe harbour measure "*if the jurisdictional ETR based on the CbC report was above a certain threshold, which could be set above the agreed minimum rate, then no further work would be required for that jurisdiction. In other words, the filing of the CbC report would be all that is required for that jurisdiction for purposes of the GloBE rules*".
Considering the same shared threshold (i.e. Euro 750 million), we believe that it is a good idea to try "merging" the CbCR and the GloBE measures in order to limit the compliance burdens of MNEs as much as possible.

However, in order not to undermine the simplification purposes of this safe harbour rule, we believe that only certain targeted adjustments (to be defined) should be required, without introducing too many complexities or burdensome information in the CbCR. Indeed, the risk is that, as the CbCR report is only a high-level risk assessment tool, the introduction of too many (unnecessary) adjustments would undermine both the Pillar Two and CbCR purposes.

In this respect, the Pillar Two Blueprint noted that as part of the 2020 review of the CbCR, consideration is being given to including movements in deferred tax and some of other additional information in the CbCR rules[66]. To the extent that the CbCR ETR Safe Harbour would be implemented, the CbCR information would have the potential to avoid duplicate efforts with respect to Pillar Two. Conversely, if the CbCR ETR Safe Harbour were not implemented, no reduction in the administrative burden would occur.

The above being stated, consistent with the previous comments on the "pre-regime" loss carry-forward (please refer to paragraph IV of this Section), we believe that the safe harbour at hand should not undermine the loss carry-forward, which could, however, be recorded by the requiring taxpayers (e.g. in or out of the CbCR, based on the envisaged new design) and used when needed in order to avoid over-taxation. In other words, under such approach, in instances where the MNE has an ETR that is above the safe harbour ETR for one or more prior years, but one that is below the safe harbour ETR in the current year, the MNE should be allowed to go back and compute its carry-forward attributes for the prior years. However,

[66] Please refer to paragraph 390 of the Pillar Two Blueprint.

further considerations in this respect should be made once the overall Pillar Two measure is finally designed;

(ii). *De minimis* profit exclusion:
The *de minimis* profit exclusion would require MNEs to apply the GloBE rules only to jurisdictions in which profits exceed a minimum threshold. This approach would rely on the TPG principles introduced under Actions 8-10 of the BEPS Action Plan to prevent splitting of ownership of valuable IP among a large number of low-taxed IP vehicles.
Under the Pillar Two Blueprint this measure could be structured as a (i) *de minimis* threshold amounting to 2.5% of group profit, (ii) a fixed *de minimis* threshold of. Euro 100,000, or (iii) a combination of both (i.e. the lesser of the thresholds (i) and (ii)).
With respect to this simplification, we note that – although this safe harbour seems to entail *prima facie* a higher amount of work than the CbCR ETR Safe Harbour – it would however be less burdensome than having to perform all of the required GloBE tax base adjustments for all jurisdictions.
Moreover, we believe that a proper integration of this measure with the CbCR would amplify the simplification of this measure
Lastly, subject to a proper assessment of the final design of this measure, we however tend to believe that – in principle – also in this case, loss carry-forward should be allowed based on the same approach already outlined with respect to the CbCR ETR Safe Harbour;

(iii). Single jurisdictional ETR to cover several years:
Under this simplification, where a jurisdiction's ETR is above a certain threshold rate (which would be higher than the minimum rate), an ETR calculation would not be required for anywhere from 3 to 5 years (known as the "grace period").

As currently designed, we believe that this simplification would be considered as insubstantial (or at least not very useful) by MNEs, since this option would, however, require ETR calculation at least once in every jurisdiction every few years, possibly also based on data from multiple years (as envisaged in paragraph 403 of the Pillar Two Blueprint).

Moreover, as currently designed, it may provide restriction, as it requires MNEs "*to make annual representation that no business change occurred over the grace period*" [67] (even if, for the time being, the Pillar Two Blueprint does not address the meaning of

[67] Please refer to paragraph 401 of the Pillar Two Blueprint.

"business change").

The above, together with the understandable need to implement a special anti-avoidance rule, results in a measure that is still too complex to provide an actual simplification for MNEs. As a result, works to streamline the measure are required, in our view;

(iv). Tax administration guidance**:**
This measure, which aims at implementing a process to identify *ex-ante* "low-risk jurisdictions" where the MNEs would enjoy a presumption that their ETR in those jurisdictions exceeded the agreed minimum rate, appears to represent by far the greatest potential provision to simplify compliance and improve certainty for taxpayers. As correctly noted in the Pillar Two Blueprint, such an approach would be most effective if it took place before the GloBE rules become effective[68].

However, to make this simplification measure effective even in the long-term period, a specific procedure should be set to undertake (on the basis of the criteria to be defined) a risk assessment of the relevant jurisdictions' tax legislations, also by analysing any "*tax law revision or reform that materially changed the jurisdiction's tax base and/or tax rate*" [69].

In this respect, the "tax administration guidance" could be complemented by a system providing a notification obligation on the relevant jurisdictions for the benefit of taxpayers, in cases where they plan tax reform that "materially changes" the ETR and/or the tax base.

X. Chapter 10: Implementation and rule co-ordination

Effective co-ordination of the GloBE rules

As preliminary comment, we concur with the idea that (i) a phased introduction of the four measures under the Pillar Two Blueprint should be followed in order to carefully and properly implement either the new domestic (i.e. IIR and UTPR) or treaty (i.e. STTR and SOR) rules. In this respect, we believe that (ii) a model legislation and relative guidance developed by the Inclusive Framework on BEPS[70] may help to provide co-ordination and

[68] Please refer to paragraph 406 of the Pillar Two Blueprint.

[69] Please refer to paragraph 408 of the Pillar Two Blueprint.

[70] Please refer to Section 10.5.1. of the Pillar Two Blueprint.

consistency in the implementation process within the relevant jurisdictions.

The prior implementation of the IIR would represent a first significant step in the overall implementation procedure, also to test the actual alignment of the jurisdictions involved in the process. However, considering its nature as a "domestic measure", in order to ensure an effective and timely coordinated implementation (thus avoiding any unwanted distortion), countries should already start assessing how such provisions would be compatible with their domestic law provisions, by also brainstorming about any incompatibility to be removed.

In the same sense, with particular regards to the European law framework, specific considerations and assessments will have to be performed to evaluate whether such provision would be in line with all existing legislation and applicable principles.

The above being stated, although the Pillar Two Blueprint sets out detailed arguments for considering the IIR and UTPR as already compatible with current treaty provisions, we would welcome the introduction of a new multilateral convention[71] to ensure, *inter alia*, the consistency and co-ordination of the IIR and UTPR (even if, in principle, the former has priority over the latter[72]), as well as their actual compatibility with current treaty obligations. Such a multilateral convention could also be the chance to include the provisions of the Pillar One package, in order to ensure a good understanding of the interaction between the two Pillars.

With particular regard to the STTR, being a "top-up withholding" tax regime to be applied on a gross basis over a wide range of payments, with volatile and unpredictable outcomes (also in terms of over-taxation), we believe that such a measure should possibly be implemented in a later stage, only if necessary, in order to complement other measures in case they will result ineffective (and thus, not as a priority rule over the GloBE measures).

Dispute prevention and resolution

In order to grant tax certainty and confidence in the implementation of the new measure, as also envisaged in the Pillar Two Blueprint, we suggest that the Inclusive Framework on BEPS also explore the development of a dedicated dispute resolution mechanism into

[71] As specified in paragraph 707 of the Pillar Two Blueprint "*Unlike the MLI used to implement the tax treaty related BEPS measures, the provisions would not seek to modify existing treaty provisions. Instead, the provisions could be included in a new multilateral convention, which would be a standalone international public law instrument designed specifically for the purposes of ensuring consistent, coordinated and comprehensive application of the GloBE rules, and which would coexist with the existing tax treaty network.*".

[72] Please refer to Section 7.2. of the Pillar Two Blueprint.

the abovementioned multilateral convention (to be possibly combined or integrated with the envisaged "binding dispute resolution mechanism" described in the Pillar One Blueprint), in order to provide taxpayers with a proper fast and effective multilateral instrument, aimed at quickly resolving any arising double taxation.

Indeed, as already outlined in our previous comments on the project, as a general comment based on our experience, we believe that a dispute resolution mechanism similar to those currently provided for in bilateral tax treaties to resolve cases of double taxation (e.g. MAP/MAP arbitration) might not achieve the effective resolution of such disputes in all cases in a timely manner.

More in detail, in our experience, we found some significant shortcomings, in particular as regards the length and the effective conclusion of such procedures, and so we believe that – in any case – any dispute resolution mechanism which will have been deemed as suitable for the new rules should be strengthened by also providing, *inter alia*, shorter and more reasonable deadlines to resolve them.

We are aware that all the above improvements would entail a greater commitment by tax administrations, but it is undeniable that it would be a necessary step to guarantee tax certainty to taxpayers.

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Hoping that you will find our comments useful, please do not hesitate to contact us if you require any clarification.

We welcome the opportunity to discuss these comments in greater detail and to continue to participate in the dialogue as the OECD and country policymakers advance the work on this important project.

Yours sincerely,

Foglia & Partners

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