PILLAR 2 IMPLICATIONS FOR PARTICIPATING JURISDICTIONS.

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INTRODUCTION

Base Erosion and Profit Shifting (BEPS) are tax avoidance strategies employed by Multinational Enterprises (MNEs) to reduce their tax bases.

MNEs utilize tax planning techniques to shift profits that exploit:

1. Gaps in international and domestic tax laws.
2. Mismatches between domestic tax systems.

As a result, corporate tax rates are unduly low and do not reflect the realities of the underlying economic transactions

Pillar 2 is one of the approaches put forward to tackle such issues and reign in harmful corporate tax competition among nations of the world. This approach is backed by the OECD/G20-Inclusive Framework

OPPORTUNITIES OF PILLAR 2

. Creates a level playing field to all large MNE’s.

. The minimum tax of 15% would raise Global revenues by 5.7% through the top-up tax, and 8.1% through reduced tax competition.

- QDMTT will cover companies with global turnover under 750 Million Euros that are dominating developing markets.

. International Tax Policy framework of most developing countries will adjust to accommodate the consequential changes that would come.

. Developing countries are expected to gain further revenues under the STTR.

- The adoption of Pillar Two is also an avenue to remove the use of several tax incentives to attract FDIs, which are critically needed to develop core sectors of the Nigerian economy.

DESIGN OF PILLAR 2

- Top-down approach of IIR implementation
- In-scope MNEs headquartered in developed countries' s jurisdiction.

IIR

- UTPR is a stop gap to the IIR
- UTPR 5 years Exclusion rule

UTPR

- Qualifying condition attached to the DMTT
- The complexities and disparities of the rules against the laws of most developing countries may cause the DMTT not to be qualified.

QDMTT

- Only taxes covered under Article 2 are considered
- Circuit breaker provision
- STTR MLI has limited flexibility

STTR

CHALLENGES OF PILLAR 2 GLOBE RULES

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The quantum of the amount proposed to be excluded from carve outs equals 8% of the carrying value of tangible assets and 10% of payroll, declining annually by 0.2 percentage points for the first five years, and by 0.4 percentage points for tangible assets and by 0.8 percentage points for payroll for the last five years.

Most jurisdictions will treat the 15% minimum rate as a ceiling and not a starting point.

Developing countries rely a lot on Withholding taxes (WHT) for revenue assurance, some WHT will not be treated as covered taxes under GloBE Rules.

Administrative complexity and compliance costs especially on developing countries who will bear the brunt.

The Globe rules mimics some European rules which means that in effect, we are not starting from the same take-off point. It will take us more time, resources and effort to administer the rules.

Some countries have already started implementing the GloBE rules in their jurisdictions. This implies that they have an added advantage over us and as such are eroding financial capital base.

FINANCIAL IMPLICATIONS FOR DEVELOPED COUNTRIES

01

- Among the Forbes 2000 list, 1955 companies report revenues of more than € 750 million (or $830 billion). Of these, 44% of the covered MNEs are from the US, 29.7% from the EU, 14.7% from China while the rest of the world share 11.6%.
- A study by Barake et al 2023, found that global revenue potential of a 15% global minimum tax is approximately EUR 179.1 billion (subject to SBIE).

02

- The 20 most developed countries of the world, using (HDI 2021 data) share estimated EUR 130.7 billion (supposing that the HQ collects top-up using IIR). Put differently, the OECD countries alone will collect EUR 162.6 billion (90.7%).

FINANCIAL IMPLICATIONS FOR DEVELOPED COUNTRIES

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03

- EUR 5.8 billion is therefore left for the rest of the world including all the developing countries. The non-OECD countries are left with 9.3% per the estimate.

04

- China , South Africa and Brazil collects EUR; 6.2 Billion, 3 billion and 1.5 billion respectively.

Note: this is due to the concentration of the HQs of the in-scope MNEs in the benefiting countries.

WAY FORWARD

1. Developing countries should as a matter of urgency, draw up a national strategy for immediate streamlining of tax incentives, to avoid ceding of tax base to other jurisdictions, owing to the implementation of Pillar 2 rules.

2. They should further take immediate steps to forge and implement policy options in response to Pillar 2, which action may include changing of income tax rule to raise effective tax rate to a minimum of 15% or introducing a Qualified Domestic Minimum Top-up Tax (QDMTT).

3. It is very important to note that a developing country or market jurisdiction's refusal to adopt the GloBE Rules will not impact the developed country's right to tax whatever tax is forgone in their jurisdiction

4. STTR provides developing countries and opportunities to claw back its taxing right ceded under its tax treaties to residence jurisdictions that are low tax jurisdictions. Developing countries are expected to sign up to the STTR MLI in to updates its existing tax treaties

THANK YOU