

CLIENT ALERT

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OECD Global Digital Economy Tax Reform: Current Developments

On July 10, 2021, the G20 Finance Ministers announced that they have endorsed the key components of the revised two pillar approach to address the tax challenges arising from the digitalization of the economy contained in the Statement by the OECD Inclusive Framework (“IF”) issued on July 1, 2021. The Statement provides that 132 of the 139 IF members had agreed on this approach. As of today, the only members of the IF that have not signed up to both pillars are Barbados, Estonia, Hungary, Ireland, Kenya, Nigeria and Sri Lanka.

The Revised Proposals

Pillar One introduces measures to allocate certain taxing rights over profits of multinational entities (“MNEs”) above a 10% “net profit margin” threshold to end-market jurisdictions (i.e. jurisdictions where end users and consumers of digital services are located). As originally conceived in the October 2020 Blueprint (“Blueprint”), Pillar One was intended to apply to MNEs operating in the Automated Digital Services (“ADS”) and Consumer Facing Businesses (“CFB”) industries. The Statement revises this approach so that Pillar One would instead apply to MNEs with a global revenue of at least EUR 20 billion (approximately \$ 23 billion) and a net profit margin above 10%. According to the Statement, after seven years, the scope could be further widened to apply to MNEs with a global revenue of at least EUR 10 billion (approximately \$ 12 billion), pending successful implementation of Pillar One. Certain businesses including regulated financial services businesses are excluded from the scope of Pillar One.

Pillar Two introduces a global minimum effective tax rate of at least 15% through the implementation of the so-called Global Anti-Base Erosion (“GloBE”) rules to ensure that MNEs are adequately taxed on their profits. The GloBE rules would function as a top-up tax on a parent entity of the MNE, where its affiliates are taxed in local jurisdictions below the minimum rate (certain other rules denying deductions for payments to such affiliates would also apply). Pillar Two would apply to all MNEs with a global turnover in excess of EUR 750 million (approximately \$ 880 million). The international shipping industry is excluded from the scope of Pillar Two.

Next Steps

Discussions with respect to the design elements of the agreed upon two pillar approach will continue, with the IF intending to finalize such issues and put forth a detailed implementation plan by October 2021. Pillar One will be implemented through a multilateral instrument, which will be developed and open for signature in October 2022,

and become effective in 2023. IF members will not be required to adopt the GloBE rules, but if they do, they would do so consistently with the approach of Pillar Two. Pillar Two is intended to be brought into law in 2022, and effective in 2023. The Pillar Two implementation plan would include mechanisms for coordinating GloBE rules implemented by the IF members.

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Please feel free to contact any of the persons listed below if you have any questions on this important development:

**Marco A. Blanco**

Partner, Global Tax Co-Chair
Geneva Managing Partner
mblanco@curtis.com
New York: +1 212 696 6128
Geneva: +41 22 718 3518
Paris: +33 1 42 68 72 00

**Klas Holm**

Partner, Global Tax Co-Chair
kholm@curtis.com
New York: +1 212 696 8800

**Olga R. Beloded**

Partner
obeloded@curtis.com
New York: +1 212 696 6124

**Eduardo A. Cukier**

Partner
ecukier@curtis.com
New York: +1 212 696 6107

**Christian Fingerhut**

Partner
Tax
cfingerhut@curtis.com
Frankfurt: +49 69 247 576 0