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OECD Pillar Two: Will it achieve its desired policy objective of globally taxing large multinational enterprises in a digitalized economy?

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## Abbreviations

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<th>Abbreviation</th>
<th>Description</th>
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<tbody>
<tr>
<td>BEPS</td>
<td>Base Erosion and Profit Shifting</td>
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<td>CIT</td>
<td>Corporate income tax</td>
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<td>EU</td>
<td>European Union</td>
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<td>G20</td>
<td>Group of Twenty (countries)</td>
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<td>GAAP</td>
<td>Generally Accepted Accounting Principles</td>
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<td>GloBE</td>
<td>The Global Anti-Base Erosion Rules</td>
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<tr>
<td>IFRS</td>
<td>International Financial Reporting Standards</td>
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<td>IIR</td>
<td>Income Inclusion Rule</td>
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<tr>
<td>MNE</td>
<td>Multinational Enterprise</td>
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<tr>
<td>OECD</td>
<td>Organisation for Economic Co-operation and Development</td>
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<td>SOR</td>
<td>Switch-Over Rule</td>
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<td>STTR</td>
<td>Subject-To-Tax Rule</td>
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<td>UPE</td>
<td>Unlimited Parent Entity</td>
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<td>UTPR</td>
<td>Undertaxed Payment Rule</td>
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1. Introduction

1.1 Problem

In recent years, many large Multinational Enterprises (MNEs) have developed their services, especially digitalized services that are operating all around the world covering many of the jurisdictions. Despite the fact, that even when MNEs have reached out to a vast number of consumers all around the world, these jurisdictions have not been able to cope with the fast globalization and digitalization of the economy and are subject to lost tax revenue due to the tax planning of the Multinational Enterprises. What the MNEs are doing is that they operate in different jurisdictions but are tax residents or subjects only in jurisdictions where they are taxed at a lower rate than in countries they are operating and creating the actual value, for instance, by the means of collecting, marketing, or using customer data.

Some of the jurisdictions apply the territorial principle to their tax regime which means that the profits, for example, corporate income, should be taxed in the jurisdiction where they arise. One of the major issues with the taxation of Multinational Enterprises is the difficulty to determine from where their actual value creation is sourced. That is why the author emphasizes to the reader to keep the value creation concept of OECD (if not familiar, see first Chapter 2.2.1) in mind when reading this thesis.

The Pillar Two rules are a part of the OECD/G20 BEPS Project, and its main objective is to address the challenges in taxation arising from the digitalization of the economy. In October 2021, over 135 jurisdictions have joined the plan to update the international tax system up to date. The Pillar Two Model rules are designed to ensure that MNEs pay a minimum level of tax in each country they operate.\textsuperscript{1} Quite recently, on the 14th of March 2022, the OECD/G20 Inclusive Framework on BEPS released technical commentary guidance on the Pillar two project, including its 15% global minimum tax, which was agreed upon in 2021 as a part of this “two-pillar solution.” The Global Anti-Base Erosion rules (GloBE) are one of the most important aspect of the

OECD’s Two Pillar project since it targets to ensure that large multinational enterprises pay a minimum level of tax on income arising from every jurisdiction they are operating. In more detail, the GloBE rules aim to provide coordinated taxation system that imposes so called “top-up tax” on profits arising in a jurisdiction where the effective tax rate is below the minimum rate.\(^2\)

The problem the research in this thesis is going to focus is related to this project and its policies that have faced heavy criticism among scholars. There are fears that Pillar Two project might fail with its policy objectives, contradict with excising legal doctrines, or even create unintended changes or unnecessary changes to the international tax system. However, the latter is rather debatable. Also, it might even contradict with tax treaty law (Chapter 3.4.) or with the European Union law (Chapter 3.5).

1.2 Objectives of the Thesis

In this thesis, the ultimate objective is to analyze whether the, soon to be enforced OECD Global Anti-Base Erosion Model Rules (Pillar Two rules), are set to achieve the policy objectives to solve tax challenges in digitalized economy. In this thesis, the author is pursuing this objective by providing discussion on the issue at hand and by analyzing the main research question of whether OECD Pillar Two project guidelines will achieve their desired policy objectives. The author is pursuing to achieve the answer to the research question by providing relevant discussion and trying to find answers on topics in three different levels:

- Background explanation and why a reform is required to combat tax challenges in digitalized economy?
- By interpreting the main policy objectives of the OECD Pillar Two GloBE Model rules.
- Providing analysis of the policy issues and effects that might occur when Pillar Two GloBE Model rules are implemented and applied to domestic legislation of the OECD member jurisdictions.

Firstly, for achieving the objective of the thesis, the author provides a comprehensive discussion based on the background of the Pillar Two project. This is to gather understanding towards the question of why these rules are needed and what kind of tax “phenomena” has caused the issues that the

OECD tries to solve. As described above, the digitalization of the economy has changed the need to update the international taxation regime. Consequently, other factors are included as well such as tax competition that has made MNEs to make tax strategies to pay low-rate corporate income tax, which has been going on for decades.

Consequently, in this thesis, the actual OECD Pillar Two proposed rules are under discussion to interpret the main policy objectives it tries to achieve in the international taxation system and more importantly, to prevent Base Erosion and Profit Shifting strategies of the MNEs. Global Anti-Base Erosion rules (GloBE) rules are one of the most important elements presented in the OECD Pillar Two proposal and this thesis will heavily focus on these rules.

Finally, in order to fulfill the ultimate purpose of this thesis, the discussion is going to be followed by the critical analysis of the OECD Pillar Two project provided solutions where the author states different tax law related categories where these model rules have contradictory elements and legal issues with them. In addition to GloBE rules issues that apply, in general, all around the world, the author will provide in Chapter 3.4 a further discussion concerning the issues from European Union’s perspective.

1.3 Delimitations

The author tries to delimit the scope of this thesis to the OECD Pillar Two GloBE model rules and to the challenges in taxation arising from the digitalization of the economy. Hence, the other parts of the former and current BEPS project as well as tax law principles will only be dealt with where necessary to provide background, or other relevant information in order to analyze OECD Pillar Two provided rules. This logically means that other OECD BEPS project policy objectives and issues will not be discussed unless they are specifically related to Pillar Two proposal. The author also focuses on the European Union’s perspective on the issue, in order to provide an example due to its unique multinational role in the world’s leading economies. Also, the European Union is closely following OECD model rules in general.

1.4 Method and Material Used

In this thesis the author is researching material that is evaluating the current state of the OECD Pillar Two rules. This includes OECD Pillar Two Model GloBE rules, Commentary to the GloBE rules and other sources from the
OECD Web page such as statistics. In order to gather supporting statements and offer different perspectives, the author of this thesis is researching other legal materials and sources such as books, journals, articles. This research follows a legal proposition model by analyzing the existing provisions of the OECD Pillar Two GloBE rules. The author has tried to select the materials that are as recently published as possible, since the topic in general, is relevantly new.

For the purpose of this thesis, the author tries to formulate critical discussion based on the sources used. The above-mentioned OECD rules work as a foundation for the discussion, whereas the other legal materials are used to formulate and create different perspectives and to evaluate the research question. It can be stated that to conduct proper research and fulfill the objective of this thesis a quality of the discussion and argumentation should be ensured.

The OECD and its guidelines and model rules are one of the most important actors in the field of tax law and world economy since they apply to the largest economies in the world, for instance, European Union, the United States, China, Japan, and India. Since OECD plays an enormous role globally in the field of tax law, the author is of the opinion that the OECD projects should be subject to a vast amount of critical thinking, in order to achieve the best possible outcome, they potentially can provide. Although many jurisdictions are OECD members, they still face potential reforms based on not only the OECD Two Pillar GloBE model rules but to other OECD proposals as well. It might also be the case that these countries are facing different issues to implement these rules in their jurisdiction, which is also being described further in this thesis.

Even though OECD BEPS project is not new it includes Pillar Two and GloBE project, which is a new set of model rules. Since its relevantly new, the actual changes and effects in the international tax regime are not yet visible. That is why it is important to introduce thoughts and concerns related to the OECD’s pursue to solve taxation challenges and issues of digitalization of the economy.

1.5. Outline

In the first part of this thesis, the main features of the OECD Pillar Two project will be described. This provides a background study where OECD’s previous attempts to tackle Base Erosion and Profit Shifting are explained, together with the OECD-created concept of value creation. This is followed by an
overview of the Pillar Two ruleset and its desired policy goals that allow for references in the subsequent chapters.

The second part of the thesis tries to examine the issues related to the rules that the Pillar Two project is trying to provide. This chapter consists of a discussion on different issues and risks that may arise when Two Pillar rules are applied. The chapter also analyses whether the OECD Pillar Two GloBE rules desired policy objectives will be achieved, and to see if there are any major changes or effects upcoming in the international tax environment. Different tax law-related principles will be examined such as worldwide taxation versus source taxation, tax base, the scope of the project, and tax treaty law.

The third chapter of the thesis will further continue the discussion on the issues arising from the Pillar Two rules. The chapter will conclude the most important issues and offer some thoughts and speculation of the author.

The final part of the thesis consists of concluding remarks of the author. There, the results of the analyses of the author will be concluded, and a general overview will be given.
2. Overview of Pillar Two rules

2.1 Introduction

This chapter will provide an overview of OECD BEPS Pillar Two project rules including its Global Anti-Base Erosion Model Rules. This chapter includes on the one hand some background information on why and how there is an urge from OECD member states to implement these Pillar Two rules and why there is an urgent need for updating the international taxation system.

Base erosion and profit shifting (BEPS) means tax planning scenarios and strategies used by multinational enterprises that are abusing a weakness in tax rules to avoid paying taxes. OECD/G20 BEPS Project is developed in order to address these tax challenges. One of the most interesting and important aspects of this project relates to tax challenges that arise from the digitalization of the economy. Over 135 jurisdictions have joined to OECD’s plan to update crucial elements of the international tax system which is very outdated for being fit to govern a modern globalized and digitalized economy.3

2.2 Background

2.2.1 Value creation concept

The OECD has created the concept of value creation as the ultimate central reason and criterion for the allocation of taxing rights between jurisdictions.4 The concept means that “the location of taxable profits should be aligned with the location where economic activities and value creation take place.”5 However, there is room left for interpretation for the objective definition of value creation since basically anything can contribute to the creation of value, and in that sense, it also differs from the source principle where the origin and

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3 OECD, supra nota 1
5 Ibid.
destination are clearly available.\textsuperscript{6} Thus, it can be said that the value creation concept and source principle are heavily linked to each other and that link is visible in Pillar Two GloBE rules.

2.2.2 The failure of taxation of the digital economy

The taxation of the digital economy has been incomplete in previous OECD BEPS projects. In 2013, OECD started to examine the digital economy and failed to make any comprehensive actions to tackle the tax issues related to digital business and new technologies.\textsuperscript{7} In 2018, new steps were made toward taxation of digitalized economies, where it was stated that there is no consensus between countries on what kind of changes to the current international tax regime is needed. The report also stated that OECD hopes to bring over 100 countries to an agreement by 2020.\textsuperscript{8} It can be said that with this project, OECD really succeeded by bringing over 135 jurisdictions to an agreement as stated previously in this thesis.

2.2.3 International demand for GloBE rules

When looking at the Global Anti-Base Erosion Model Rules it is important, as a basis, to understand what has led the companies to the strategies that cause profit shifting and base erosion. The Inclusive Framework of the OECD/G20 argues that tax competition between jurisdictions to tempt business and investments is one of the main reasons causing the occurrence of base erosion and profit shifting.\textsuperscript{9} This argument is true, since it is hard to imagine a more relevant reason for the loss of tax base and revenue than this. Also, OECD has previously stated that the reason for base erosion and profit shifting is this issue known as hybrid mismatches, as a phenomenon leading to base erosion and profit shifting. If a specific international transaction is treated differently in both or all the jurisdictions involved, it is likely for the corporation to achieve tax benefits where income is taxed at a lower rate than if the income has been covered by one tax jurisdiction only.\textsuperscript{10}

The Global Anti-Base Erosion Rules (GloBE), which is known as the Pillar Two project, is considered to be a key element of this plan since it should

\begin{footnotesize}
\begin{enumerate}
\item Ibid.
\item Ibid.
\item Ibid.
\item P. Das & A. Rizzo, (2022), \textit{The OECD Global Minimum Tax Proposal under Pillar Two: Will It Achieve the Desired Policy Objective?} 76 Bull. Intl. Taxn. 1
\end{enumerate}
\end{footnotesize}
ensure large MNEs to pay a minimum level of tax in each of the jurisdictions where they operate and are receiving income. One of the specifics of the GloBE rules is that they should de facto provide a unified structure of taxation that levies a tax on profits arising in a jurisdiction even though the effective tax rate would be below the minimum rate.\textsuperscript{11}

2.3 Pillar Two main rules explained

2.3.1 Scope

OECD Pillar Two project is seeking to implement and apply a global minimum level of effective taxation on income. This would only apply to MNE groups whose annual gross revenue is at least 750 million euros in the previous fiscal year.\textsuperscript{12} Specific investment funds, pension funds, and governmental entities would be excluded to respect their tax neutrality.\textsuperscript{13} OECD has tried to delineate the scope of Pillar Two rules in Article 1. The Globe rules that Pillar Two are proposing, according to Article 1 would apply to entities that are members of MNE groups and has an annual income of 750 million euros or more. One fiscal year is 12 months in this context and there are, so mentioned, Excluded Entities that are not subject to the GloBE rules.\textsuperscript{14}

Pillar Two describes an MNE Group as any group that includes at least one entity or permanent establishment located in another jurisdiction than the Ultimate Parent Entity is, whereas the latter is described as an entity that owns directly or indirectly a controlling interest in any other entity and is not owned by itself. Excluded entities are entities such as governmental entities, non-profit organizations, pension, and investment funds, et cetera.\textsuperscript{15}

\textsuperscript{11} OECD, Supra nota 1
\textsuperscript{12} H. van Dam et al., (2021), Taxing the Digitalized Economy: Key Takeaways from the OECD Public Consultation on the Pillar One and Pillar Two Blueprints, 28 Intl. Transfer Pricing J. 3
\textsuperscript{13} Ibid.
\textsuperscript{15} Ibid.
2.3.2 Four main rules

Here the author is looking to keep the summary of the OECD Pillar Two GloBE rules as short as possible. For more information, see the proposal.\textsuperscript{16} In general, the ruleset of Pillar Two is based on four different elements. By these model rules, OECD tries to offer its member economies keys to tackle tax challenges arising from the digitalized economy and the tax strategies of MNEs.

The main proposed rules are following:

a) The income inclusion rule (IIR) is the first step to implement the minimum tax rate rule. It extends residence-based taxation in a scenario where the effective tax rate of the source jurisdiction is below the minimum tax rate imposed.\textsuperscript{17} This said, it clearly requires the inclusion of certain income of a low-taxed MNE in the tax base of the Ultimate Parent Entity (UPE) if the income is not otherwise sufficiently taxed.\textsuperscript{18} The main effect of the Income Inclusion Rule is to ensure that the income of the MNE group is subject to tax at the minimum rate in every scenario and it should reduce the strategies to allocate profits to low-tax jurisdictions among the MNE group.\textsuperscript{19} For instance, it has been stated that the income inclusion rule would effectively protect the tax base of the parent entity jurisdiction among other jurisdictions due to reducing the incentive to put in place thick capitalization or other planning structures that are related to profit shifting,\textsuperscript{20} since every entity bearing the tax burden raised from value creation in a certain jurisdiction will be taxed at a minimum rate.

b) A switch-over rule (SOR) that is utilized in the application of IIR in a tax treaty by allowing to switch from the exemption method to the credit method where a permanent establishment that is tax-exempt in the parent jurisdiction based on the tax treaty or is taxed with a low rate in the other contracting state.\textsuperscript{21}

c) An undertaxed payment rule (UTPR), serves as a backstop for the IIR and is denying the deduction of specific transactions that are not

\textsuperscript{16} \textit{Ibid.}
\textsuperscript{17} C. Elliffe, (2020), \textit{International Tax Frameworks: Assessing the 2020s Compromise from the Perspective of Taxing the Digital Economy in the Great Lockdown}, 74 Bull. Intl. Taxn. 9
\textsuperscript{18} H. van Dam et al., \textit{Supra nota} 13
\textsuperscript{19} C. Elliffe, \textit{Supra nota} 18
\textsuperscript{20} \textit{Ibid.}
\textsuperscript{21} H. van Dam et al., \textit{Supra nota} 13
sufficiently taxed at the same level than a recipient.\textsuperscript{22} This undertaxed payment rule would mainly be used in scenarios where the parent entity is a resident in a country that has not enforced the Income Inclusion Rule.\textsuperscript{23}

d) Subject-to-tax rule (STTR), a minimum tax rate will be imposed on specific payments that are connected between members of the MNE Group which might lead to carry heightened base eroding.\textsuperscript{24} Which consists of a withholding tax on certain intra-group payments to a low tax group entity. This concerns mainly interest and royalties, but also other fees as well.\textsuperscript{25}

In addition, OECD has provided domestic and tax treaty-based measures that allow jurisdictions where the MNE group is operating to tax top-up amounts of tax on a resident entity with respect to the income of low-taxed entities that are forming part of the MNE group.\textsuperscript{26}

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\textsuperscript{22} H. van Dam et al., Supra nota 13
\textsuperscript{23} OECD, Supra nota 2
\textsuperscript{24} Ibid.
\textsuperscript{25} H. van Dam et al., Supra nota 13
\textsuperscript{26} Ibid.
\end{flushright}
3. Issues related to Pillar Two ruleset

3.1 Introduction

The purpose of this chapter is to provide a discussion and analysis of the issues and risks that arise by the implementation of Pillar Two rules. In general, OECD’s Pillar Two has been subject to disapprovals concerning contradictory elements in International tax law categories such as worldwide and territorial taxation, tax base provided by the model rules, the scope of the model rules and there are a couple of contradictory elements connected to tax treaty law as well. Major issues related to these categories will be described in this chapter of the thesis. Also, one of the main concerns that has risen is that even though the OECD Pillar Two and GloBE Model rules provide effective tools to the tax jurisdictions of the OECD member jurisdictions for monitoring their tax subjects, they fail to consider integrity problems to which a higher level of government surveillance can lead.27

3.2 Major policy issues and concerns in International Taxation System

3.2.1 Worldwide and territorial taxation

In the international tax system, the different types of income are allocated on the basis of the source principle or residence principle. Taxation can be allocated to the country of registration of the corporation, to the country where the income is sourced from, or to both of these jurisdictions. Practically, both source and residence jurisdictions have the right to tax the profits of MNEs. This means that in most cases the source jurisdiction which is acting also as a host country has the possibility to first actual taxation performance at taxing the profits where they are earned. The residence jurisdiction can then choose whether to increase the foreign tax with its own tax or exempt the foreign-

27 M. Berglund & K. Cejie, Supra nota 11
source income from further tax.\textsuperscript{28} If the residence jurisdiction chooses to tax the profits of an MNE based on worldwide income, it should provide “tax room” for the source country to avoid the likely double taxation situation of such profits.\textsuperscript{29}

3.2.2 Tax base and accounting standards

The issues related to the tax base are rather technical. One of the issues related is based on the accounting standards of the jurisdictions that would be subject to applying the global minimum tax rate on income. Especially in the current situation where there are contradictory elements to the practices between the economic giants. For instance, the accounting standards methods vary among several larger economies as some of them have adopted IFRS (International Financial Reporting Standards) method, such as European Union, whilst, for example, the USA, China, and Japan have adopted their own GAAPs (Generally Accepted Accounting Principles).\textsuperscript{30} The global minimum tax rate would require harmonization which would definitely bring its own problems and questions. One of them would be whether the harmonized accounting standards would reflect on true profits reported. Consequently, since GloBE seems to support IFRS\textsuperscript{31}, it is uncertain on what schedule and how would the large economies adopting their own GAAPs be able to transform to the preferred model, in case they even want to. Furthermore, it has been discussed whether the future tax planning of the MNEs will change towards manipulation of accounting net income or loss and the consolidated financial statements to dodge the application of GloBE rules.\textsuperscript{32}

3.2.3 Scope of Pillar Two proposal

One of the issues at hand. is that the global minimum tax rate that should tackle the issue of tax competition, only applies to MNEs that have a turnover exceeding 750 million Euros.\textsuperscript{33} According to OECD statistics, it would only apply to around 2000 entities.\textsuperscript{34} Also, it can be said that since the general tax competition is formulated by jurisdictions reducing their corporate tax rates in order to tempt business and investment, it should not be a concern that the

\textsuperscript{28} P. Das & A. Rizzo, Supra nota 10
\textsuperscript{29} Ibid.\textsuperscript{30} Ibid.
\textsuperscript{31} Ibid.
\textsuperscript{33} OECD, Supra nota 15
\textsuperscript{34} See OECD statistics, available at https://stats.oecd.org/
minimum tax rate would lower the tax rates even more, as it has been the trend for the last two decades.\textsuperscript{35} Perhaps it would be useful for scholars to research whether targeting only the highest revenue corporations would bring the desired policy objective.

3.2.4 Tax treaty law

Even though the Blueprint argues that only a few changes would be necessary for tax treaties to implement GloBE rules, at least the Switch-Over Rule and Subject-To-Tax Rule rules (chapter 2.3) would require changes to tax treaties.\textsuperscript{36} However, it seems that these changes would be relevantly marginal in contrast to the fact that IIR and UTPR rules are held to be compatible with tax treaty clauses inspired by the OECD Model Tax Convention.\textsuperscript{37}

3.3 Issues related to EU Law

European Union is a bit unique compared to other large economies in the world since it consists of multiple jurisdictions. European Union is a member of the Group of 20 (G20) as such. In that sense, it is important to analyze whether the harmonized legislation of the European Union reacts to possible reform in the international taxation system. Many scholars seem to share an opinion that the OECD Pillar Two project is contradictory to the EU primary and secondary law.

From the European Union’s point of view, when introducing a minimum tax level into the EU, the main objective is to ease the application of domestic or treaty-based anti-abuse rules to tax transactions.\textsuperscript{38} Whilst a promising-sounding method to recapture of missing tax bases is a tempting tool for tax administrations within the Union, with its nature of being convenient to avoid adjective costs and risks, it can be questioned whether this minimum tax level objective is justifying a complete reform of corporate income tax system. Since it comes with difficult analyses and computations related to the recaptured tax bases of associated corporate entities.\textsuperscript{39} Previously the European Court of Justice has stated that the only way to justify a restrictive

\begin{footnotesize}
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\item \textsuperscript{35} P. Das & A. Rizzo, \textit{Supra nota} 10
\item \textsuperscript{36} H. van Dam et al., \textit{Supra nota} 13
\item \textsuperscript{37} Englisch, Joachim, (2021) \textit{International Effective Minimum Taxation – analysis of GloBE (Pillar Two)}, SSRN
\item \textsuperscript{38} C. Brokelind, (2021) \textit{An Overview of Legal Issues Arising from the Implementation in the European Union of the OECD’s Pillar One and Pillar Two Blueprint}, 75 Bull. Intl. Taxn. 5
\item \textsuperscript{39} \textit{Ibid.}
\end{itemize}
\end{footnotesize}
tax rule is to tackle abusive practices, as in the Cadbury Schweppes case,\textsuperscript{40} for instance.

The Pillar Two proposal could do well if it would respect the EU primary law a little bit further. The other option is that the European Court of Justice would consider base erosion as a sufficient reason to control taxpayers, not only tax abuse. The Pillar Two proposals feature standard and circumstantial thresholds, and it would not pass the European Union’s anti-abuse restrictive legislation test if it does not leave the taxpayers the opportunity to prove themselves.\textsuperscript{41}

When it comes to the freedom of establishment provided by Treaty of the Functioning of the European Union Article 49,\textsuperscript{42} these GloBE rules have several frictions with them. The Income Inclusion Rule rule should face a test against the freedom of establishment since it is very likely that it restricts the establishment of Ultimate Parent Enterprises since it is possible that these entities are being treated differently and in a more restrictive manner than parent companies setting up subsidiaries in the same Member State.\textsuperscript{43} Also to mention, from a European Union law perspective, the Income Inclusion Rule would apply to third countries just fine but within the Union, it clearly carries restrictive elements with it.

The European Union has also published a proposal for a directive on ensuring a global minimum level of taxation for multinational groups in the Union.\textsuperscript{44} As the name of the directive states, its objective is quite clear. This would be a huge boost for OECD’s Pillar Two project to succeed if the European Union can effectively enforce this directive. It has been argued in the directive proposal that “the European Union with a Single Market is a closely integrated economy.”\textsuperscript{45} Also, the model rules are not binding within the Union and could create a risk of different applications of these rules.\textsuperscript{46} However, it is rather clear that the European Union is ready to do almost what it takes to implement these Pillar Two rules into its legislation. Interesting part will be to see whether the EU can do it without setting itself in a middle of contradictory legal doctrines.

\textsuperscript{40} Ibid.
\textsuperscript{41} Ibid.
\textsuperscript{42} Treaty of the Functioning European Union, § 49
\textsuperscript{43} Luc De Broe, Mélanie Massant, (2021), \textit{Are the OECD/G20 Pillar Two GloBE-Rules Compliant with the Fundamental Freedoms?}, 30, EC Tax Review, Issue 3
\textsuperscript{45} Ibid.
\textsuperscript{46} Ana Paula Dourado, \textit{Supra nota} 33
The main objective of the new EU Directive Proposal is to enforce rules that follow close as possible to the OECD GloBE Model Rules stated in Pillar Two.\textsuperscript{47} However, as stated above, (in chapter 3.2.2) the risks related to accounting are a threat to European Union to lose tax revenue despite the 15% minimum tax rate implementation.

\textsuperscript{47} Ana Paula Dourado, \textit{Supra nota 33}
4. Discussion on policy objective achievement

4.1 Introduction

The previous chapter discussed and analyzed the issues and their effects on the implementation and application of the OECD Pillar Two rules. For fulfilling the main purpose of the thesis, this chapter provides further concluding discussion and a more general approach to whether the policy objectives might be achieved.

4.2 Popularity of the project

OECD Pillar Two is supported by OECD members and G/20 countries. This is probably one of the most important facts when analyzing whether Pillar Two will achieve its desired policy objective. The support tells us that it is highly likely that OECD member countries and G/20 countries are willing to change their tax rules (and accounting standards) to the format that is required for the OECD Pillar Two GloBE model rules to work well in practice.

The discussion in this thesis led to the fact that the need to update the international taxation system is in the major interest of the world’s leading economies. When interpreting the OECD Pillar Two GloBE Model Rules, it can be stated that they are clearly formulated, and some room has been left for the OECD members and G/20 countries to implement them without impossible barriers to their legislation. What the author means by impossible barriers is that they can be changed if desired, and so far, as stated previously in this thesis, 135 jurisdictions have joined the project\(^48\), which is promising for Pillar Two objectives to succeed.

\(^{48}\) OECD, *supra nota* 1
4.3 The interpretation of possible risks that might occur

4.3.1 Risks in international taxation regime in overall

As discussed in the previous chapter of this thesis, the OECD Pillar Two GloBE rules have faced criticism concerning almost every major category of taxation. Most importantly the requirement to do huge reforms to the corporate income tax regime altogether with the other contradictory elements it is facing within the international taxation regime. In worldwide and territorial taxation principles, with the tax base and international accounting standards, or with tax treaty law. For the international taxation regime, these three issues are most likely to occur according to the findings in this thesis.

A) It seems that it is to be seen whether the OECD member states will provide necessary “room” for tax, concerning worldwide and territorial taxation principles. Lawmakers of the international legislation and domestic legislation are very likely to face an issue to try to find comprehensive solutions.

B) Also, there is uncertainty whether the harmonization of accounting standards will cause the MNEs to move from tax planning strategies to manipulation of accounting standards. The author is in the opinion that the extent and scope of this problem is too early to analyze without concrete evidence that this is going to be the case.

C) When it comes to the scope of Pillar Two, the relevant issue at hand is that now when the 750 million annual revenue applies only to MNE. It leaves a similar issue unsolved for the smaller multinational entities. Also, the scope might affect to tax competition by either making corporate income taxes to grow or getting lower. However, as stated in the previous chapter, if corporate income tax rates are getting lower, it would not probably be a concern for tax competition since it has been the trend for a couple of decades already.

D) From the Tax Treaty law perspective, the Switch-Over Rule and Subject-to-Tax Rule rules might require a change in the OECD Model Convention Articles, which would affect a vast amount of Tax Treaties that are already in force.

49 P. Das & A. Rizzo, Supra nota 10
50 Ana Paula Dourado, Supra nota 33
51 OECD, supra nota 15
52 H. van Dam et al., Supra nota 13
4.3.2 Risk concerning EU law

Regarding the topic of this thesis, a lot of the possible contradictory elements concerning the European Union primary law and secondary law have been stated by scholars\textsuperscript{53}, based on to the Freedom of Establishment provided by the Treaty of Functioning European Union or the previous rulings of the European Court of Justice (as mentioned above) that have based their rulings on tackling tax abusive practices. In this light, it seems to be a challenge for the European Union to get all the Member States behind the harmonization of the GloBE model rules within the Union, even though the Proposal Directive\textsuperscript{54} has been created already.

4.3.3 Determining the market country or value creation jurisdiction

One of the most interesting problems the GloBE rules might create is to actually block the growing tax base that comes with the digital economy. Since high value MNEs like Apple or Google are making enormous profits without being subject to heavy tax burden in the market countries,\textsuperscript{55} The market countries are trying to show with the help of the Pillar Two rules that the tax base is connected to their jurisdiction and have a tax claim based on that. However, the market country is not genuinely the only jurisdiction which is linked to the income of the MNE. The other country linked to this specific income is a country where the taxpayer has its data centers, research & development departments, and other production sites, that are linked to the taxpayer. It is rather logical, that the country at hand might be able to show similar link to the same income in their jurisdiction as well. This will definitely lead to competing claims between the jurisdictions concerning the same income. Hence, it is inevitable that this will lead to double taxation scenario unless agreement between the jurisdictions is found on how to allocate the taxing rights in the future.\textsuperscript{56}

\textsuperscript{53} C. Brokelind, \textit{Supra nota} 38
\textsuperscript{55} W. Schön, (2018), \textit{Ten Questions about Why and How to Tax the Digitalized Economy}, 72 Bull. Intl. Taxn. 4/5
\textsuperscript{56} \textit{Ibid.}
5. Conclusion

This thesis provided a further discussion on OECD Pillar Two rules, their background, main policy objectives, and most importantly to the possible risks and issues. As stated before, the OECD was able to bring over 135 jurisdictions to agree on this project which is equivalent to 95% of the GDP of the world. This clearly shows the importance and willingness to address the tax challenges that the digitalized economy has brought in front of us.

As discussed in this thesis, various scholars have argued and pointed out different issues in an international tax regime that might be at risk to apply when these OECD Pillar Two rules are effectively implemented and applied in domestic jurisdictions. However, the research showed that the issues at hand, that are arising from the OECD Pillar Two rules, are not insurmountable. The barriers presented in Chapter 3 seem to be of a nature that they can be changed if desired, by the jurisdictions participating in the OECD Pillar Two project. Hence, the demand and the support for the project have been enormous, it seems likely that OECD member states and G/20 countries that have opted for the project are willing to change and update the international taxation regime to tackle the tax challenges arising from digitalized economy and tax strategies of the MNEs.

The main purpose of this thesis was to examine OECD Pillar Two rules and analyze why they are needed and what kind of issues these rules might cause for the international taxation system. The main purpose of this thesis has been fulfilled by answering the main research question,

- Will OECD Pillar Two achieve its policy objectives of globally taxing large multinational enterprises in the digitalized economy?

With provided research and discussion in this thesis, it can be stated that when concerning the policy issues of Pillar Two rules, the author has reached to a conclusion. Pillar Two is a relevantly new set of model rules and the actual effects and results have not come to the daylight yet. The author wants to emphasize that there are foreseeable risks to the international taxation system that might occur when implementing and applying Pillar Two rules in force.

57 OECD, Supra nota 1
However, the barriers introduced in this thesis, which might seem problematic right now are not unchangeable. If the OECD member states and especially G/20 countries manage to implement and apply these rules to their domestic legislation - the author believes OECD Pillar Two will have the possibility to reach its desired policy objective of globally taxing large multinational enterprises in the digitalized economy. However, this research has shown that further and comprehensive research among scholars is required, or these Pillar Two rules are on the brink to go to the list of failed OECD projects concerning the solving of tax challenges of the digitalized economy.
List of References

Books and articles:


VII. Englisch, Joachim, *International Effective Minimum Taxation – analysis of GloBE (Pillar Two)*


European Union legal sources:

X. TFEU Art. 49


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