AMRO
ASEAN +3 MACROECONOMIC RESEARCH OFFICE

Analytical Note

Global Tax Reform: What It Means for ASEAN+3 – Progress and Challenges[1]

January 26, 2024

I. Developments in Global Tax Reforms

1. **The loss of tax revenues due to tax avoidance and the changing global business environment have shifted the primary concerns of international tax policy from 'double taxation' to 'double non-taxation'.** Among these issues, the international community is now addressing the tax challenges arising from the digitalization of the economy. Before widespread digitalization, multinational businesses with a physical presence in more than one jurisdiction could be taxed on the same income twice, once in the source jurisdiction where the income is generated and also in the jurisdiction where the income is received. Various countries thus entered into Avoidance of Double Taxation Agreements (DTAs) to resolve the issue of double taxation. Meanwhile, the emergence of the digital economy has presented another challenge to tax authorities. Discrepancies in domestic and treaty laws in treating digital businesses have created cross-border tax planning opportunities for multinational businesses through tax avoidance and double non-taxation.[2] To achieve a fair sharing of the tax base, governments need to address and solve for these tax leakages as soon as possible.

2. **The Organisation for Economic Co-operation and Development (OECD), at the request of the Group of 20 (G20), has worked on the Base Erosion and Profit Shifting (OECD/G20 BEPS) project since 2013, which is commonly referred to as BEPS 1.0.** According to OECD (2023a), governments worldwide incur losses between USD100 billion and USD240 billion annually as a result of BEPS tactics. This amount is equivalent to 4-10 percent of the global corporate income tax revenue. Therefore, 15 Action Plans have been published under the OECD/G20 BEPS project to ensure that governments are equipped with rules and instruments to address tax avoidance such that the profits are taxed where the economic activities are performed and where value is created. Despite the success of the BEPS Project in limiting multinational enterprises (MNEs) from shifting profits to low-tax

[1] Prepared by Ravisara Hataiseree (Ravisara.Hataiseree@amro-asia.org, Fiscal Surveillance); reviewed by Seung Hyun (Luke) Hong (Fiscal Surveillance Group Head and Lead Economist); authorized by Hoe Ee Khor (Chief Economist). The author would like to thank Tetsuya Utamura (AMRO Deputy Director) and Andriansyah (Fiscal Surveillance) for the valuable comments. The views expressed in this note are the author's and do not necessarily represent those of the AMRO or AMRO management. Unless otherwise indicated, the analysis is based on information available up to 3 January 2024.

[2] A common example is a 'Double Irish Tax Sandwich', in which large multinational digital companies based their headquarters in countries with low corporate income tax rates and leveraged loopholes in tax rules, often avoiding the establishment of a permanent set up in a country where they generated substantial revenue, all while artificially shifting profits to locations with no or low tax rates and little or no economic activity.

jurisdictions where they conduct little or no economic activities, the BEPS 1.0 project seems insufficient to address specific challenges posed by digitalization.

3. **Named the BEPS 2.0 project, the OECD and G20 have established the OECD/G20 Inclusive Framework on BEPS (IF) to permit wider participation from interested jurisdictions to address global tax challenges arising from digitalization and globalization.** Established in 2016, the OECD/G20 Inclusive Framework on BEPS aims to continue pursuing tax avoidance reduction and develop standards on BEPS-related issues through the participation of interested countries, including developing economies. Later in 2018, the IF introduced a *Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy* (Two-Pillar Solution). The Two-Pillar Solution answers the calls of developing countries for a more coordinated taxation system (i) to redistribute the taxing rights to market jurisdictions where sales and users are located regardless of physical presence (Pillar One); and (ii) to ensure that MNEs contribute their fair share of tax revenues to countries in which they generate profits by imposing a global minimum tax (Pillar Two).

4. **The COVID-19 pandemic accelerated the digitalization of traditional businesses and drove digital service revenues up, leading more countries to participate in global initiatives for improved international tax regulations.** As of November 2023, 145 economies have become members of the OECD/G20 Inclusive Framework on BEPS. Of these, 139 have already agreed on the Two-Pillar Solution of October 2021. Within this OECD/G20 Inclusive Framework on BEPS group, 140 members have given their approval to the *Outcome Statement on the Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy* (Outcome Statement), published in July 2023. The Outcome Statement acknowledges the significant progress made on the Two-Pillar Solution, reflecting compromise among all participating jurisdictions during extensive negotiations within IF members, and addressing the remaining elements of the Two-Pillar Solution.

5. **Three ASEAN+3 economies—Cambodia, Lao PDR, and Myanmar—have not yet participated as IF members.**[3] However, non-IF countries can also incorporate certain BEPS addressing measures into their domestic laws to address tax challenges related to the digital economy without participating in the IF, or could participate in the IF later as their capacity[4] improves. In this manner, these countries can keep up with tax revenue gains to support economic recovery and preserve taxing rights and tax revenue.

6. **This analytical note aims to provide an update on significant advancements made until 2023 in the Two-Pillar Solution since AMRO's two previous publications.** [5] [6] This includes revenue estimations and the latest development in implementing Pillar One and Pillar Two across participating economies. The progress made and challenges faced by the United States, Europe, and ASEAN+3 member economies are also discussed. In the

[3] Lao PDR has requested AMRO and the OECD Korea Tax Policy Centre to provide technical assistance (TA) aimed at helping the Ministry of Finance grasp the necessary steps it needs to take to prepare to join the Inclusive Framework. This TA initiative is scheduled to take place in Lao PDR in April 2024.

[4] IF participation requires the jurisdiction's commitment to adopting four BEPS minimum standards (i) treaty shopping (BEPS Action 6); (ii) transfer pricing documentation and country by country reporting (BEPS Action 13); (iii) harmful tax practices (BEPS Action 5); and (iv) tax treaty dispute resolution measures (BEPS Action 14).

[5] AMRO published two Analytic Notes on the Two-Pillar Rules. These are "The Analytical Notes on Global Tax Reform: What It Means For ASEAN+3", published in September 2021; and "The Analytical Notes on Global Tax Reform: What It Means For ASEAN+3 – An Update", in November 2021.

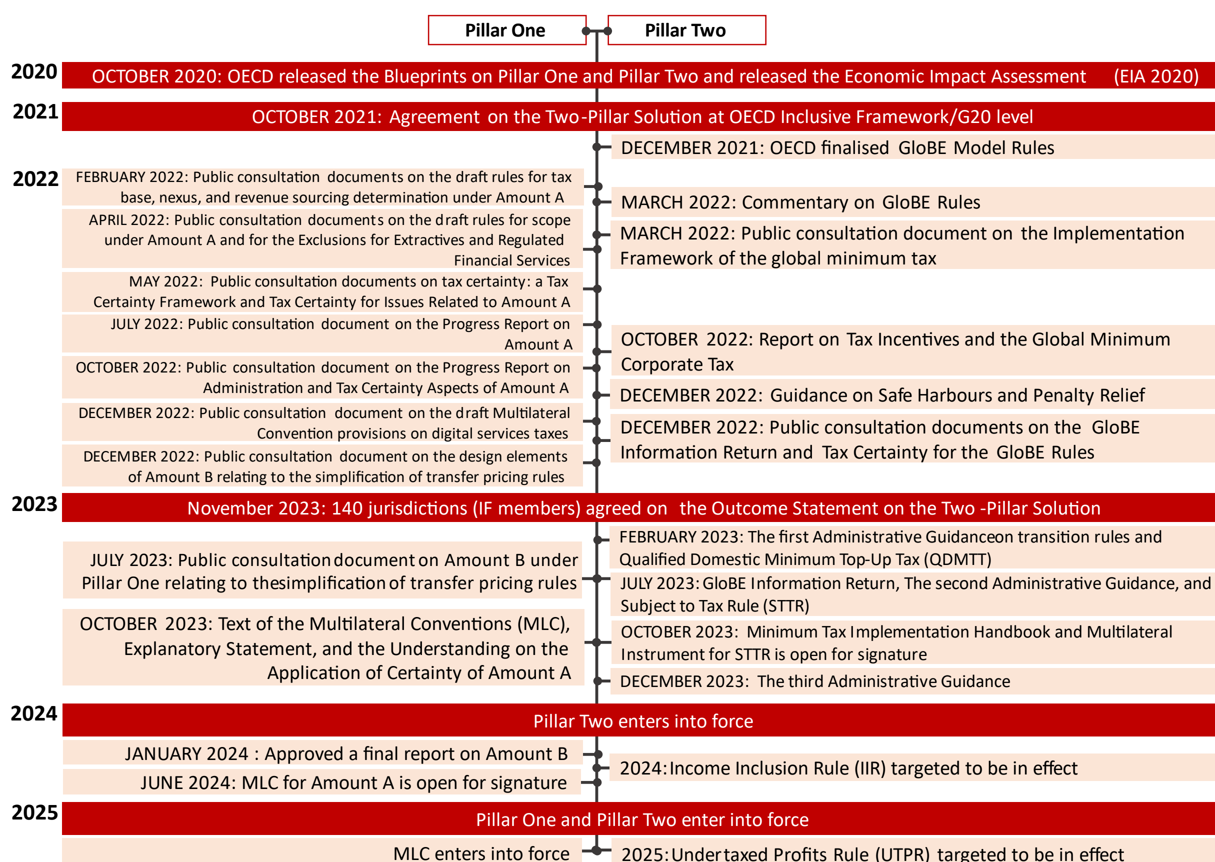
[6] This analytic note summarizes the progress in country plans by end of 2023 but the actual implementation schedule may change given the dynamic nature of Pillar Two's implementation.

final section, the note outlines essential policy responses and administrative considerations for governments preparing to implement the Two-Pillar Solution in their economies.

II. Progress in the OECD/G20 Two-Pillar Rules

7. **Economies are set to implement Pillar Two from 2024.** While its original intention was in 2023, the OECD/G20's accommodates that individual countries are adopting their own schedules on the global minimum tax under Pillar Two within the 2024-2025 timeframe. The EU, Japan, Korea and Vietnam along with many other individual jurisdictions are on track to implement the Two-Pillar Rules starting from 2024. Delaying the implementation of these rules could result in lost revenue and erode the existing tax base. Most IF member countries and jurisdictions have been actively modernizing their tax systems to align with the Two-Pillar solution. Likewise, many participating ASEAN+3 economies have embarked on the journey to implement Pillar One and Pillar Two.

Figure 1. OECD/G20 Key Timeline of Two-Pillar Solution



Source: OECD (2021a, 2023a, 2023b, 2023g, 2023h, 2023j, 2023k, 2023l); AMRO staff compilation

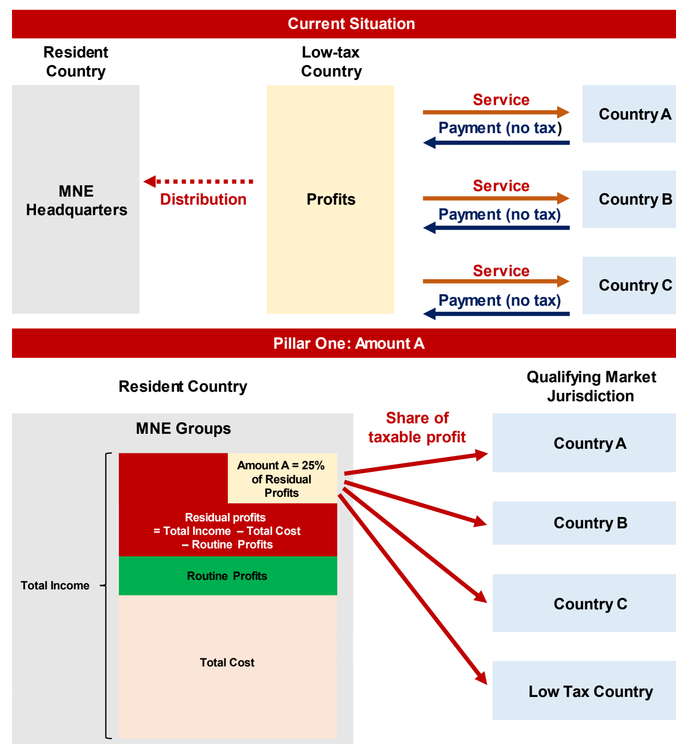
Pillar One

8. **Pillar One consists of two main elements, Amount A and Amount B.** Amount A modernizes the international taxation framework by allowing market jurisdictions to tax the income of large and highly profitable foreign MNEs, irrespective of their taxable presence in

that jurisdiction. Amount B, meanwhile, simplifies the existing transfer pricing rules for all taxpayers. Both Amount A and Amount B will likely require amendments to domestic laws and treaties.

9. **Amount A of Pillar One establishes a new nexus[7] and co-ordinates a profit allocation for large MNEs.** Amount A will apply to large and profitable MNE groups with an annual global turnover of more than EUR20 billion and a pre-tax profit margin of more than 10 percent (in-scope MNEs).[8] A new nexus will determine whether a jurisdiction qualifies for profit reallocation from in-scope MNEs. Any in-scope MNE that derives at least EUR1 million[9] in revenue from a particular market jurisdiction will reallocate 25 percent of its residual profits[10] back to that market jurisdiction using a revenue-based allocation key regardless of its physical presence (Amount A). Amount A profits will be reallocated among qualifying market jurisdictions, based on the share of revenue sourced from each of those jurisdictions where goods or services are used or consumed (Figure 2).[11] The market jurisdictions will then apply their domestic corporate income tax system to tax allocated residual profits.

Figure 2. Profits Allocation under Amount A



Source: AMRO staff illustration
Note: (1) The dotted arrow line implies that the distribution itself could be taxed by the resident country.
(2) Amount A under Pillar One employs a group-based taxation approach, departing from entity-based discourse, and considers MNE groups as a whole rather than entity-by-entity.

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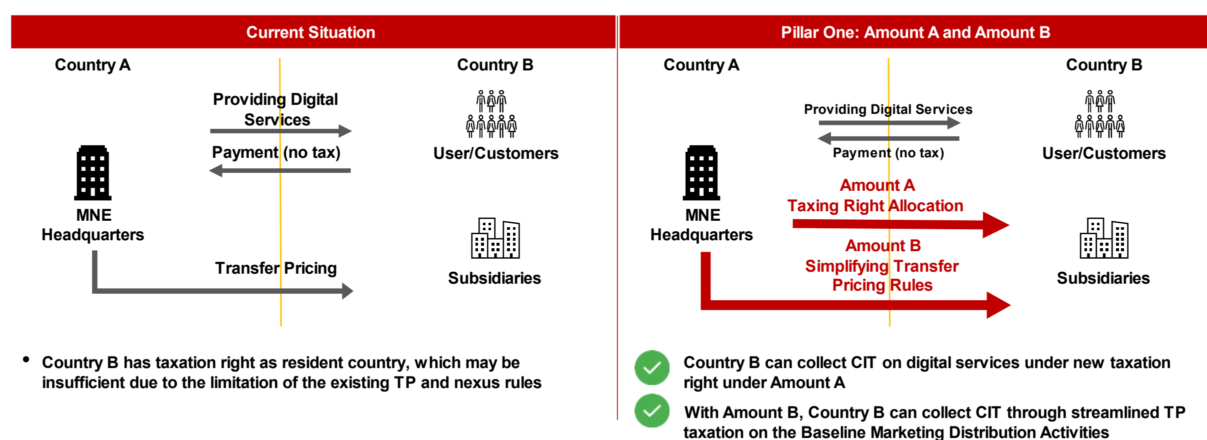
[7] Nexus means a business has a tax presence in a particular state. A nexus must exist before an authority can impose a tax on the enterprise, and there must be a substantial link between the jurisdiction and the business.
[8] MNE groups that operate in the financial and natural resource sectors are excluded. The turnover threshold might be reduced to EUR10 billion with a review beginning seven years after the agreement comes into force.
[9] For smaller jurisdictions with GDP of less than EUR40 billion, the nexus threshold will be set at EUR250,000.
[10] Residual profits are defined as a profit margin that is over 10 percent of revenue (OECD, 2021).
[11] Revenues are sourced according to the type of revenue as specified in the MLC. Note that revenues and profits related to extractives and regulated financial services will be excluded.

10. **Discussions on Amount A have made good progress, but its implementation timeline depends on the acceptance by a certain number of jurisdictions.** Amount A will be implemented through the MLC,[12] which is a consensus-based solution to avoid unilateral tax measures such as Digital Service Taxes (DSTs).[13] The draft text of MLC for Amount A, including the repeals of DSTs, was released by the OECD in October 2023, and are expected to be published for endorsement once the MLC wording is agreed with a signing ceremony to be organized by the end of June 2024.[14] While the MLC is expected to come into force in 2025,[15] its entry into force will hinge on its acceptance by a certain number of jurisdictions.[16] Once it becomes effective, the MLC will require participating economies to withdraw all existing DSTs and similar measures (Rollback), and not introduce DSTs or similar measures in the future (Standstill).[17] The standstill aims to avoid double taxation, especially on major digital companies whose profits will be reallocated under Pillar One. Nevertheless, the elimination of DSTs has raised concerns among many countries that currently collect tax from digital services.[18]

Figure 3. Pillar One Principles



Source: AMRO staff illustration

11. **Discussions on Amount B of Pillar One, which aims to increase tax certainty by creating standardized transfer price benchmarks and decrease costly transfer pricing disputes, have focused on the needs of countries with limited capacity.** Jurisdictions

[12] The IF has set up the Task Force on the Digital Economy (TFDE) to determine details related to Amount A. The MLC ensures that Amount A will be implemented in a consistent and legally binding manner.
[13] Many jurisdictions have independently introduced DSTs to protect their tax base and revenue from digital activities. DSTs focus on MNEs offering online goods or services without offering a creditable system, potentially resulting in multiple DST obligations for these companies.
[14] In October 2023, the OECD released the draft of the MLC to implement Amount A of Pillar One, accompanied by an Explanatory Statement, and the Understanding on the Application of Certainty of Amount A in preparation for the opening for signature.
[15] In 2025, when it takes effect, there will be ample time for domestic consultation, legislative, and administrative processes in each jurisdiction.
[16] The Outcome Statement confirms that Pillar One will come into effect once 30 jurisdictions, accounting for at least 60 percent of Ultimate Parent Entities of in-scope MNEs, sign the MLC in 2024. The MLC requires U.S.'s ratification to take effect, given the 60-30 requirement. The commitment of the U.S. is particularly crucial as it hosts several world's largest tech companies, which are a key focus for the levy (Tamma and Smith-Meyer, 2023).
[17] According to the Outcome Statement, 140 Inclusive Framework members agreed to extend the existing standstill (ending on 31 December 2023) to 31 December 2024 or until the entry into force of the MLC, whichever is earlier.
[18] See Section IV for DSTs in ASEAN+3 economies.

with restricted capacity typically have limited local comparable data, and their transfer pricing rules are often the subject of international tax disputes.[19] Amount B intends to simplify the application of the arm's length principle to in-country baseline marketing and distribution activities. This will improve tax certainty in the international tax system and reduce administrative costs for tax administrations and taxpayers on transfer pricing rules. Following the public consultation that ended on 1 September 2023, the OECD intends to approve a report on Amount B and to integrate essential content into the OECD Transfer Pricing Guidelines by January 2024.

Pillar Two

12. **Pillar Two introduces mechanisms to enforce a global minimum tax.** Pillar Two consists of two main rules, the Global Anti-Base Erosion (GloBE) rules and the Subject to Tax Rules (STTR). GloBE Rules apply a 15 percent minimum corporate income tax on in-scope MNEs' foreign profits. The STTR, a treaty-override provision, allows a source state to tax certain gross incomes up to a globally agreed minimum rate of 9 percent.

13. **Approximately 1,000 MNEs globally are expected to be subject to GloBE rules.**[20] The GloBE rules under Pillar Two present a coordinated tax system to ensure that the large and profitable MNEs with annual global revenue above EUR750 million[21] pay a minimum corporate income tax (CIT) rate at 15 percent.[22] Through a top-up tax on the profits taxed at less than the minimum 15 percent in any jurisdiction, GloBE rules increase the effective CIT rate on large MNEs to at least of 15 percent in each jurisdiction they operate.

14. **The STTR specifically aims to protect developing countries' tax base by ensuring MNEs pay a minimum tax on a broad range of cross-border intra-group payments for services.** The STTR permits source jurisdictions, which are usually developing countries, to withhold tax on certain types of related party payments, such as royalties and interest, if the recipient is either not taxed or is taxed at a corporate income tax rate of less than 9 percent.[23] Unlike the GloBE rules that allow substance-based carve-outs, the STTR rate is set at 9 percent with no carve-out (Table 1). The STTR is a treaty provision that will be inserted in bilateral double tax treaties. IF members have two options to implement the STTR – they can either choose to sign a multilateral instrument for STTR (STTR MLI) amending all treaties to include the STTR, or they can choose to implement the STTR in a specific tax treaty through bilateral negotiations.

[19] According to OECD (2023c), transfer pricing disputes relating to distribution activities represent around 30-70 percent of all limited capacity jurisdictions' transfer pricing disputes.
[20] Estimated by the ADB and Chulalongkorn University (May 2023).
[21] The EUR750 million threshold is calculated from the consolidated financial statements of ultimate parent entity revenues in two or more of the preceding four years. A jurisdiction is free to apply a lower threshold when applying the Income Inclusion Rules (IIR) to MNEs headquartered in its country; however, the government should weigh the compliance and administrative costs and benefits of taxing more entities than large MNEs when lowering the threshold.
[22] Taxpayers with no foreign presence or less than EUR750 million in consolidated revenues are not in the scope of the Model Rules. In addition, Pillar Two Model Rules exclude government entities, international organizations, non-profit organizations, and entities meeting the definition of pension, investment, or real estate funds.
[23] The STTR is a treaty-based rule that may override treaty benefits in existing treaties for certain payments.

Table 1. Comparison of GloBE Rules and Subject to Tax Rule

GloBE Rules	Subject to Tax Rule
• Apply to in-scope MNEs with annual revenues exceeding EUR750 million	• Materiality threshold: the STTR only applies if the aggregate sum of Covered Income[24] paid in a fiscal year exceeds EUR1 million (or EUR250,000 for jurisdictions with GDP below EUR40 billion)
• Jurisdictional approach	• Transactional approach (Treaty-based rules)
• Effective Tax Rate of 15 percent	• Nominal CIT rate of 9 percent
• Top-up tax on excess profits with substance carve-out	• Top-up tax on certain payments with no carve-out, but the 9 percent tax rate may be reduced by the nominal rate in the recipient jurisdiction and by any existing taxing right of the payor jurisdiction under the applicable tax treaty.[25]

Source: OECD (2023d, 2023e); AMRO staff compilation

15. **Pillar Two is becoming a reality with around 55 jurisdictions taking steps toward implementation.[26]** Set to come into effect in many jurisdictions starting in 2024, the OECD/G20 IF on BEPS has released several key documents—GloBE Model Rules in December 2021, the Commentary in March 2022, and three sets of Administrative Guidance in 2023[27] — to help jurisdictions instate Pillar Two into domestic law. A new Minimum Tax Implementation Handbook, released in October 2023, is also available to assist governments and other stakeholders in assessing implementation options and potential impact of moving forward with GloBE rules. Several jurisdictions have now released draft domestic legislation shepherded by GloBE Model Rules, Commentary, and Administrative Guidance, to implement Pillar Two. The EU as well as many non-EU members, including Korea, Japan, and Vietnam in this region, plan to implement Pillar Two starting in 2024, while Singapore, Hong Kong,[28] Malaysia, and Thailand intend to do that in 2025. For STTR, the OECD has concluded negotiations on STTR MLI, and it is now open for signature, representing a significant step in finalizing the work under Pillar Two.

16. **Country-by-Country Reports (CbCR) indicate that the effective corporate income tax rates of Ultimate Parent Entities (UPEs) from developed economies are below 15 percent in some partner jurisdictions (Figure 4).[29]** For example, the average ETR of UPEs from the U.S. operating in Hong Kong and Singapore was lower than 15 percent in 2020. Similarly, UPEs from other developed economies operating in this region paid a lower than 15 percent ETR in some member economies. Consequently, an UPE with subsidiaries in partner jurisdictions with ETR under the global minimum rate may face top-up tax, resulting in a 15 percent global minimum effective CIT rate in those foreign jurisdictions.

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[24] Covered Income consists of interest, royalties, and a specified list of other payments.

[25] In the STTR, there is a provision for 'low-profit exclusion,' which stipulates that STTR does not apply if the gross income of the relevant income does not exceed the total costs of the said income plus 8.5 percent.

[26] Pillar Two was initially planned to come into effect from 1 January 2023; however, it has been postponed to 1 January 2024.

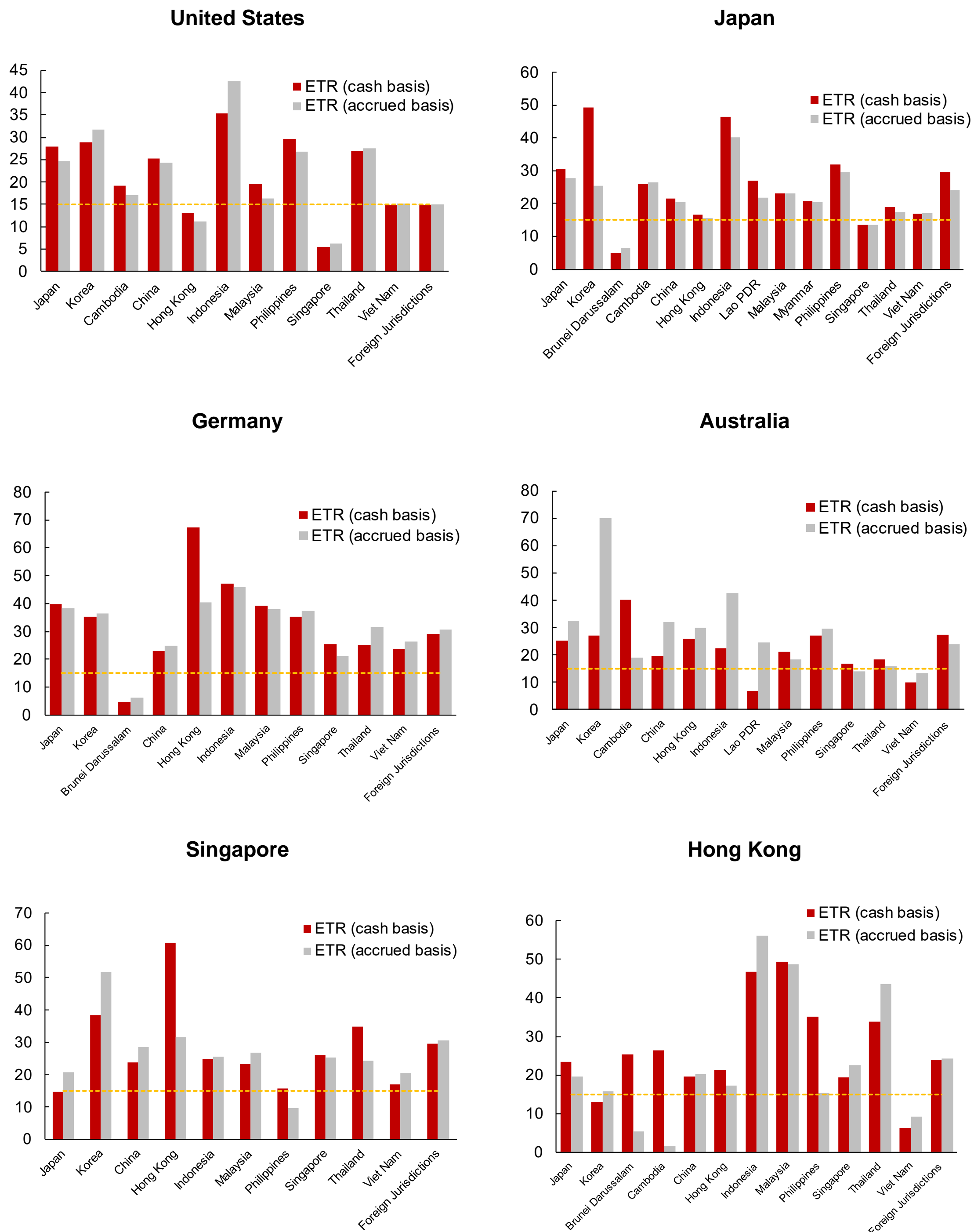
[27] IF released the three sets of Administrative Guidance in February 2023, July 2023, and December 2023. The IF will continue to produce additional Administrative Guidance on Pillar Two topics in the first half of 2024 and the Administrative Guidance will be incorporated into a revised version of the Commentary that is aimed for release in 2024 and will replace the Commentary issued in March 2022.

[28] For brevity, Hong Kong, China will be referred to as Hong Kong hereafter.

[29] Under BEPS Action 13 report (Transfer Pricing Documentation and Country-by-Country Reporting), all large MNEs, including MNEs with consolidated group revenues of at least EUR750 million, are required to prepare a CbCR with aggregate data on the global allocation of income, profit, taxes paid and economic activity among tax jurisdictions in which they operate.

While effective tax rates from CbCR statistics may differ from those under GloBE rules, they serve as an initial indicator of effective tax rates in foreign jurisdictions for large MNEs (Box A).

Figure 4. Effective Corporate Income Tax Rates of Select Ultimate Parent Entities Operating in ASEAN+3 Partner Jurisdictions



Source: OECD Statistics; AMRO illustrations

Note: (1) To calculate the effective tax rate, the income tax is divided by profit before income tax.

(2) The estimate of the ETR does not consider the substance-based income exclusion (SBIE).

(3) Cash basis ETR includes all taxes paid during the reporting fiscal year, including advance payments fulfilling the relevant fiscal year's tax obligation and payments fulfilling the previous year(s)'s tax obligation. Accrued basis ETR includes all taxes that have been assessed against a company's earned revenue or property value that has not been paid yet (Tsamparlis and Piligou, 2017).

(4) The latest available CbCR in OECD Statistics is in 2020.

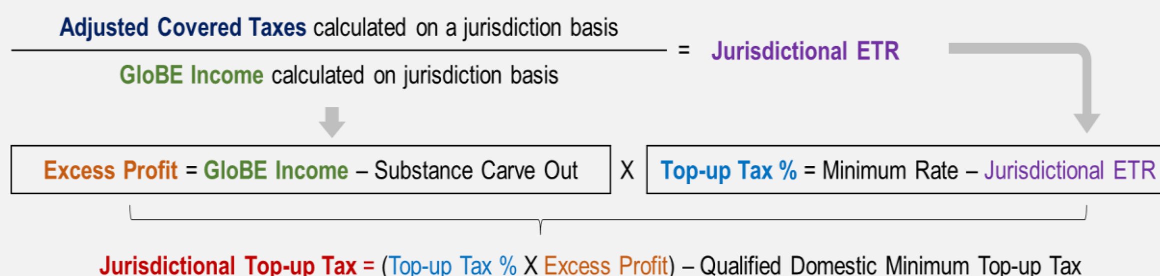
Box A. Calculating the Top-up Tax under Pillar Two

The Pillar Two GloBE effective tax rate (ETR) is a crucial part in the computation of the top-up tax. Like the traditional method of calculating the ETR, where it is determined by dividing income tax by pre-tax profit, the GloBE ETR is determined as the total adjusted covered taxes for the constituent entities[30] in a jurisdiction, divided by the net GloBE income or loss of the jurisdiction for each fiscal year. The UPE primarily will bear the obligation to calculate the ETR under GloBE rules and pay any top-up tax for onshore and offshore jurisdictions with an ETR of less than 15 percent. [31]

Once the jurisdictional ETR is computed, if it falls below the 15 percent global minimum rate, the amount of top-up tax needs to be calculated. To get a top-up tax payable, the top-up tax percentage is multiplied by GloBE income for the jurisdiction after a deduction for the substance-based income exclusion (SBIE), essentially a carve-out for expenditure on tangible fixed assets and payroll costs.[32] The amount of top-up tax payable is then reduced by Qualified Domestic Minimum Top-Up Tax (QDMTT).

The top-up tax payable will be attributed to constituent entities in proportion to their GloBE Income in the jurisdiction. Whilst the Pillar Two GloBE ETR calculation is based on a jurisdictional basis, the distribution of top-up applies on an entity basis. There are rules to allocate the computed top-up tax back to the constituent entities based on each constituent entity's share of the total net Pillar Two GloBE income in the jurisdiction.

Figure A.1. Jurisdictional Top-up Tax Calculation



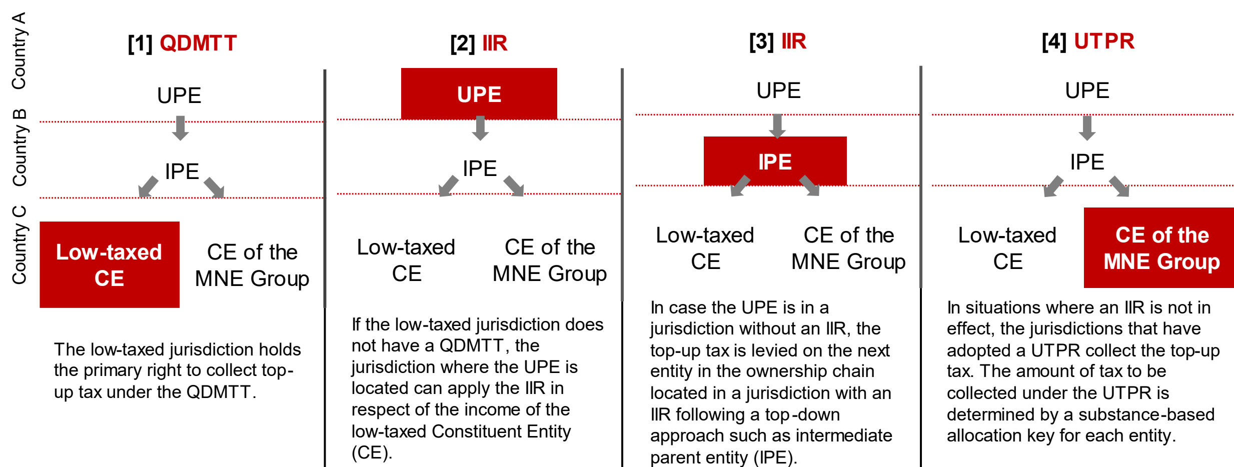
Source: AMRO illustration; adapted from OECD (2023e)
Note: (1) The jurisdiction may implement a domestic top-up tax (DMT) that does not qualify as a QDMTT and ensure a 15 percent effective tax rate in the jurisdiction. If it does so, the DMT would be treated as Covered Tax under the GloBE rules.
(2) Taxes paid under a QDMTT are creditable against GloBE liability, while credit will not be given for DMT or non-qualifying minimum taxes paid on profits.
(3) The QDMTT does not impose any significant additional cost on business as the MNE Group will already need to perform the calculation under another jurisdiction's IIR or UTPR.

17. **Separate laws or amendments to existing legislation are needed to promulgate Pillar Two GloBE rules.**[33] The resulting top-up tax is collected under three types of provisions: QDMTT, the Income Inclusion Rule (IIR), and the Undertaxed Profits Rule (UTPR). The OECD's overarching advice is to contemplate introducing the QDMTT to protect the local tax base and bring the ETR up to the 15 percent minimum rate. If the low-

[30] A Constituent Entity consists of a separate business unit that it is included in the consolidated financial statements of the MNE Group (OECD, 2023e).
[31] The top-up tax uses an effective tax rate calculated on a country-by-country basis where a common definition of covered taxes and tax base will be used.
[32] The substance carve-out begins at 8 percent for tangible assets and 10 percent for payroll, before eventually equaling 5 percent after a 10-year phase-down period.
[33] See Section IV for the Pillar Two implementation progress in ASEAN +3 economies.

tax jurisdiction does not have a QDMTT, the top-up tax will be distributed to overseas jurisdictions using two main rules, an IIR and an UTPR. To enforce these top-up taxes, individual jurisdictions will need to transpose them into their domestic laws in accordance with the GloBE Model Rules.[34]

Figure 5. Agreed Rule Order of Pillar Two Principles



Source: AMRO illustration; adapted from OECD (2023e)
Note: (1) A Constituent Entity (CE) refers to an entity or a permanent establishment within an in-scope MNE group subject to the Pillar Two GloBE Rules. A Low-taxed CE is a CE situated in a jurisdiction where the MNE group is subject to an ETR under 15 percent, and the CE itself is subject to an ETR of less than 15 percent.

(1) **QDMTT** is a domestic top-up tax to preserve a jurisdiction's primary taxing right over income generated in its territory. The low-tax income is first subject to tax in the local jurisdiction, a so-called a domestic top-up tax (DMT); however, to qualify as QDMTT, a DMT is required to follow the GloBE rules. The QDMTT is a key part of top-up tax calculation which entails a dollar-for-dollar reduction in any Pillar Two top-up tax liability. It is paid before the IIR and the UTPR are applied sequentially by a foreign jurisdiction. For MNE groups, the QDMTT will impact on where the top-up tax is paid. Therefore, numerous jurisdictions are in the process of commencing the QDMTT to maintain taxing rights over low taxed profits within their jurisdiction.

(2) **IIR** is a primary rule of distributing top-up tax under Pillar Two, if the source jurisdiction does not impose a QDMTT. The obligation to pay the top-up tax will be imposed at the level of parent entity. Therefore, the UPE jurisdiction is encouraged to apply the IIR; otherwise, the right to collect the top-up tax flows down the ownership chain to the next parent company (intermediate parent entity) with the IIR. This rule would include the income of the foreign constituent entity that has an ETR of less than 15 percent in the income of the UPE sufficient to raise the CIT rate on the foreign constituent entity's income to 15 percent. The IIR then requires the UPE to pay a top-up tax on the income of any low-taxed subsidiary. Thus, if the foreign income was taxed in the source jurisdiction at a rate lower than the minimum rate, the resident jurisdiction, where the UPE is resident, can impose a

[34] The GloBE Model Rules serve as a template that can be used as a basis for domestic legislation either by incorporating them directly or by reference into domestic law.

top-up tax on foreign source incomes by increasing the income of the parent subject to tax. The IIR is expected to come into effect in 2024.

(3) **UTPR** operates as a backstop to IIR. In cases where not all top-up tax is attributed under the IIR—such as when there is no IIR in the ultimate or partially-owned parent entity's home jurisdiction—the UTPR divided residual taxing rights on the low-taxed income between the jurisdictions implementing the UTPR. The UTPR allows the denial of deductions, which increases the tax at the subsidiary level. This results in an additional tax amount that is sufficient to cover the remaining top-up tax after the IIR. The share of the top-up tax each entity pays is proportional to its share of tangible assets and employees, ensuring that the rule is administrable and attaching the adjustment to entities with most ability to pay the required top-up tax. The UTPR is expected to come into effect in 2025.

18. **To minimize compliance cost and alleviate difficulties of MNEs during the early stages of complying with GloBE regulations, the OECD has released a series of guidance and simplified rules.** The guidance on "Safe Harbors and Penalty Relief"[35] includes several measures, such as introducing Permanent Safe Harbors to simplify income and tax computations, and a clear explanation of the Transitional Penalty Relief Regimes.[36] Additionally, the "*De minimis*" provision allows to deem the top-up tax as zero in jurisdictions where an MNE has revenues less than EUR 10 million and profits less than EUR1 million. Released in July 2023, the second set of Administrative Guidance on the GloBE Rules introduces a "QDMTT Safe Harbour" and a "Transitional Undertaxed Profits Rule Safe Harbour" to reduce the compliance burdens for MNE groups by deeming the top-up tax as zero when certain standards are met.[37] This guidance also covers currency conversion rules for GloBE calculations and the treatment of tax credits. The third tranche of administrative guidance, released in December 2023, is intended to clarify the operation of the GloBE rules before they come into effect in many countries from 1 January 2024, bringing the OECD closer to the implementation of BEPS 2.0's Two-Pillar Solution.

19. **In addition, Pillar Two's administrative framework has been developed to potentially apply to more than 140 jurisdictions.** The OCED/G20 IF on BEPS has continued to provide deliverables to increase certainty for the government and companies for the swift coordinated application of the GloBE rules. To this end, the OECD has released the standardized tax information template called 'the GloBE Information Return (GIR)' to simplify reporting requirements that allow MNEs to report their GloBE calculations at a jurisdictional level. As next steps, the OECD aims to coordinate and centralize filing requirements and enable automatic exchange of GloBE information among tax administrations. The public consultation on 'Tax Certainty for the GloBE Rules' also outlines several mechanisms such as dispute prevention, dispute resolution, and peer review processes to avoid inconsistent outcomes in the application of the Pillar Two rules across participating jurisdictions.

[35] Released by OECD on 15 December 2022.

[36] This regime considers MNEs' reasonable efforts to comply with GloBE regulations before any penalties or sanctions are imposed.

[37] For example, for fiscal years beginning before 2026, the OECD effectively suspends the application of the UTPR top-up tax to UPE if the statutory tax rate in the UPE jurisdiction exceeds 20 percent.

III. Revenue Estimates and Impact Assessment for the Two-Pillar Solution

20. **Due to significant design changes in Pillar One and Pillar Two since OECD's 2020 economic impact assessment, the OECD released revised revenue estimates in 2023, illustrating increased revenue gains for both pillars.** The change in Pillar One estimation stems from several key factors: design changes in Amount A that reduce the surrender of taxing rights for low- and middle-income jurisdictions such as de minimis rules; increases in the number of global MNEs in-scope of Amount A and their residual profits; and additional recent data and data quality improvements through anonymized CbCR data, offering a more accurate view of profit distribution in investment hubs.[38] As for Pillar Two, the changes in revenue gains primarily result from the growing profitability of in-scope MNEs, enhanced data coverage of globally low-taxed profits due to expanded and aggregated CbCR data, the recent introduction of design features such as the revised UTPR allocation key, and the assumption of consistent application of GloBE rules across all jurisdictions (OECD 2023f, 2023g).

21. **The revenue gains from Pillar One are projected to increase over time due to the higher profits of the in-scope MNEs and the design changes of Pillar One.** According to OECD (2023g), digital businesses contributed around 53 percent of total residual profits in 2021. As a result, regarding taxing rights, more than USD200 billion in profits are likely to be allocated to market jurisdictions each year. This is much higher than the 2016 estimation of USD125 billion. The new projection expects the implementation of Pillar one to generate tax revenue gains of around USD17-32 billion each year globally, substantially higher than the 2020 projection of USD5-12 billion, by reallocating tax rights from lower-tax to higher tax jurisdiction (O'Reilly et al., 2023).

Table 2. Comparison of the OECD's Revenue Estimates for a Two-Pillar Solution

	Pillar One		Pillar Two
	Taxing rights in profits allocated to Market Jurisdictions (per year)	**Tax revenue gains** (per year)	**Tax Revenue gains** (per year)
New estimates	**USD200 billion** (USD132 billion on average over the period 2017-2021)	**USD17-32 billion** (USD12-25 billion on average over the period 2017-2021)	**USD200-220 billion**
Previous estimates	**USD125 billion** (projected in 2016)	**USD5-12 billion** (projected in 2020)	**USD150 billion** (projected in 2021)

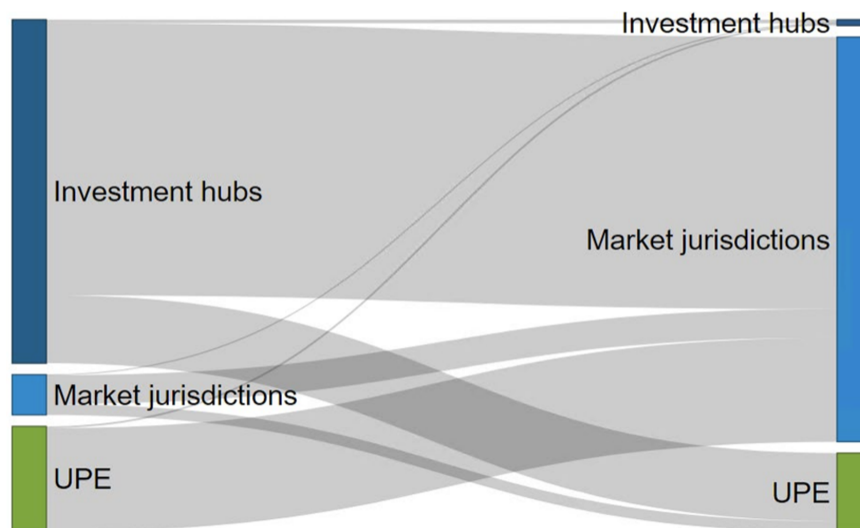
Source: AMRO illustration, adapted from O'Reilly et al. (2023) and OECD (2023f, 2023g, 2023h)

22. **Pillar One primarily shifts taxing rights from investment hubs to market jurisdictions, and these investment hubs account for 70 percent of the total relinquished taxing rights.** According to the OECD's economic impact assessment in July 2023, revenue gains are distributed to all jurisdictions except for investment hubs, leading to a larger percentage increase in corporate income tax revenue for smaller and low-income countries or market jurisdictions (Figure 6). The higher tax revenue estimates for low- and middle-income jurisdictions also stem from key design features of Amount A, including: (i)

[38] Investment hubs are jurisdictions where total inward FDI exceeds 150 percent of GDP, such as Luxembourg, the Netherlands, and Ireland, whose inward FDI to GDP ratio in 2022 is 1,405 percent, 280 percent, 266 percent, respectively (OECD Statistics).

the lower nexus threshold from EUR1 million to EUR250,000, aiming to increase the share of taxing rights to low- and middle- income jurisdictions; (ii) the de minimis threshold, ensuring that developing countries do not give up their existing taxing rights; and (iii) the tail-end revenue provisions, directing undecided revenue towards low-income countries. Hence, the overall design of Amount A aims to benefit developing countries but in economies where MNEs are mainly attracted by tax incentives, they may lose share of residual profits and taxing rights to market jurisdictions where the consumers are based (OECD 2023f).

Figure 6. Impact on the Allocation of Taxing Rights



Source: O'Reilly et al. (2023)
Note: The left column indicates the origin jurisdiction and the right column indicates the destination jurisdiction. The thickness of the bands and the vertical bars correspond to the amount of profit on which new taxing rights are to be granted under Amount A.

23. **OECD estimates suggest that Pillar Two could yield an additional USD200 billion in annual global tax revenue.** By incorporating recently agreed Pillar Two features, the new estimate of the annual additional global tax revenue by Pillar Two has increased from USD150 billion to USD200 billion. Approximately one-third of these revenue gains are expected to result from decreased profit shifting, potentially reducing globally low-taxed profits by approximately 70 percent (OECD 2023f). The impact of Pillar Two is likely to fall mostly on the large MNEs that pay GloBE effective tax rates of less than 15 percent. Nevertheless, the implementation of Pillar Two will favor companies with high payroll costs and tangible assets, the indicators of genuine economic activities, which can reduce their excess profits and bring down the top-up taxes by substance-based income carve-outs.

IV. Progress and Challenges Towards the Implementation of the Two-Pillar Solution

ASEAN +3 Economies

Pillar One

24. **Countries have the option to impose withholding tax (WHT), indirect taxes such as value added tax (VAT), corporate income tax on deemed permanent establishments (Digital PE),[39] and Digital Service Taxes (DSTs) to tax digital transactions (Table 3).** However, the standstill and rollback clause in Amount A of Pillar One seeks to avoid the proliferation of unilateral and uncoordinated measures, including DSTs, which are considered unilateral taxes that can potentially subject companies to multiple DSTs without the option of tax credits, resulting in double taxation and significant revenue loss for companies.[40] Additionally, DSTs allow individual countries to independently tax digital companies operating within their borders, without the need for mutual agreements or cooperation with other nations. This not only results in international tax conflicts and double taxation, but also places significant compliance burdens on MNEs owing to the extensive array of tax regulations (Box B). To address these challenges, 140 members of the IF on BEPS, including most ASEAN+3 economies, have endorsed the OCED's July 2023 Outcome Statement. The endorsing economies commit to reallocate taxable profits to jurisdictions that remove DSTs and agree not to introduce new domestic DSTs or similar measures from 8 October 2021 until 31 December 2024 or until the MLC is in force, whichever is earlier. Existing DSTs are expected to be withdrawn upon the MLC's entry into force, avoiding double taxation. A successful MLC is set to create a global consensus on the nexus for taxing digital services and eliminate the need for DSTs.

Table 3. Taxes on Digital Services in ASEAN+3 Economies (as of 13 December 2023)

	Direct Taxes (DSTs/ WHT/ Digital PE)	Indirect Taxes (1)
Brunei	No development on DSTs	No VAT or sales tax
Cambodia	No development on DSTs	Legislation enacted (January 2022)
China	No development on DSTs	Legislation enacted (April 2016)
Hong Kong	Legislation Enacted for Digital PE (March 2020)	No VAT or sales tax
Indonesia	No development on DSTs	Legislation enacted (July 2020)
Japan	No development on DSTs	Legislation enacted (July 2015)
Korea	No development on DSTs	Legislation enacted (August 2015)
Lao PDR	Proposal rejected (February 2023)	Proposed (2) (January 2023)

[39] Under VAT and WHT, taxing rights are defined under tax treaties and domestic tax law, respectively. The Digital PE generates taxing rights in market jurisdictions from deemed permanent establishment (Box B).
[40] As of 2023, 38 countries globally have imposed DSTs on multinational enterprises offering online transactions within their borders (Stotzky and Fano, 2023).

Malaysia	Legislation Enacted for WHT (May 2019)	Legislation enacted (January 2020)
Myanmar	No development on DSTs	No development
Philippines	Proposed WHT (April 2023)	Proposed (3) (July 2023)
Singapore	No development on DSTs	Legislation enacted (January 2020)
Thailand	Proposed WHT (May 2019)	Legislation enacted (September 2021)
Vietnam	Legislation Enacted for WHT (January 2021)	Legislation enacted (January 2022)

Source: KPMG (2023a); AMRO staff compilation
Note: (1) While VAT is the most common indirect tax system in ASEAN+3 economies, Singapore employs Goods and Services Tax (GST), and Malaysia employs Sales and Service Tax (SST) in their respective indirect tax systems.
(2) A draft instruction will be effective on 1 January 2024, and non-resident vendors of digital services to customers in Laos have been able to start registering from May 2023.
(3) The Senate of the Philippines held its first session on Senate Bill and House Bill to require non-resident digital services to register for and collect VAT on 6 July 2023.
(4) Dates in parentheses represent the latest development or the implementation date.

25. **In the absence of multilateral rules and delays in the implementation of Pillar One, a few ASEAN+3 economies have instituted their own direct tax on digital services.** Hong Kong and Indonesia enacted legislation to tax Digital PE through corporate income tax by deeming PE of overseas e-commerce companies which have a significant economic presence in their jurisdictions. However, although the legislation was enacted, taxing income sourced from digital services in Indonesia is contingent upon a global consensus on digital taxation. Malaysia, Vietnam, the Philippines, and Thailand commenced the imposition of withholding tax on remittances made by e-commerce platforms. Meanwhile, Japan and Korea have opted for broadening the scope of VAT taxable electronic services, instead of new DST, and simplifying VAT system for foreign digital service providers, regardless of their physical PE in Japan and Korea. Lao PDR is foregoing direct digital service taxes due to its limited capacity and is focusing instead on its VAT regime. As a result, non-resident digital service providers with no physical presence in Laos will not need to pay tax even on income sourced in Laos.

26. **To seize revenue opportunities from digitalization, ASEAN+3 economies have consistently amended their domestic indirect tax laws to cover digital sales.** Following the OCED's nonbinding international standards and guidance on how to collect indirect taxes from cross-border digital services,[41] ASEAN+3 members have strengthened and streamlined their tax codes and administrations to collect indirect tax from foreign digital service providers in their jurisdictions. Japan, Korea, and China are among the first countries to require non-resident digital businesses and e-commerce marketplace to register with local tax authorities and collect VAT on their sales. Similarly, a majority of ASEAN countries with indirect tax regimes have gradually extended their indirect tax law to digital services, and the Philippines and Lao PDR are following suit. According to Dabla-Norris, et. al. (2021), taxing e-commerce is expected to raise revenue between 0.04 and 0.11 percent of GDP, translating to additional USD1.1 billion in Indonesia, and USD365 million in the Philippines, and USD264 million in Vietnam.

[41] The OECD's International VAT/GST Guidelines released in 2015 and updated in 2017.

Box B. Development in Taxing Digitalized Economy

Governments generally implement three main measures to tax profits from foreign digital service providers. (i) Digital Service Tax (DST) is a new kind of tax imposed on the revenues or profits of non-resident firms that provide digital advertising, services, or content to a local user base; (ii) Withholding Tax (WHT) applies to revenue received from providing digital services; and (iii) Deemed Permanent Establishment (Digital PE) is to consider a digital service provider having PE in a jurisdiction when digital services are provided above a certain threshold, taking into account the volume of payments and the number of users located in the economy.

Among these three digital tax measures, DSTs will need to be eliminated under Pillar One. DSTs pose a risk to the mechanisms for relieving double taxation since they are unilateral measures that can subject a company's revenue to both DSTs and CIT in multiple jurisdictions without being creditable or with no exemptions against CIT liabilities arising from the payment of DSTs to foreign jurisdictions. In particular, DSTs generally tax companies on gross revenue rather than profit, implying a broader tax base regardless of a digital service's profitability. Furthermore, DSTs have varying definitions and designs in different counties, leading to inconsistency in the tax system. For instance, DSTs may be levied based on terms such as revenue generated from certain services in one jurisdiction, while in another jurisdiction, they might be collected based on the number of users or the size of digital companies.

In addition, the introduction of DSTs could risk the retaliation tariffs by the U.S. DSTs are considered discriminatory digital service taxes against U.S. technology companies and impose a burden on U.S. commerce. Consequently, after several European countries enacted DSTs, the U.S. Trade Representatives (USTR) initiated trade retaliation procedures under Section 301 of the Trade Act of 1974 to discourage the use of DSTs. The USTR determined that the DSTs adopted by Austria, France, Italy, Spain, Turkey, and the United Kingdom discriminated against U.S. digital companies. As a result, the USTR warned of trade tariffs against these countries if the DSTs were not repealed. However, the U.S. shelved its retaliatory tariffs after reaching an agreement with these countries in conjunction with the Pillar One agreement to oppose the implementation of DSTs (PwC, 2021).

Amount A under Pillar One updates the international corporate tax system to better reflect digitalization and to address uncertainties surrounding DSTs. Amount A establishes the coordinated right to tax digital services by reallocating profits to market jurisdictions, where the revenue is sourced from, even when there is no permanent establishment within those jurisdictions. Amount A thus solves the issue of determining a taxing right to tax digital services and ends the needs for unilateral DSTs. Additionally, DSTs impact all companies, irrespective of their profitability and may lead to negative effects on investment, whereas Amount A exclusively affects the largest and most profitable firms that have gained the most from globalization and digitalization. Therefore, the MLC to implement Amount A of Pillar One will abolish DSTs and prohibit their future introduction, while WHT, Digital PE,[42] and value-added taxes on digital services will remain effective.

The IF members of the ASEAN+3 region have collectively mobilized efforts to advance Amount A, which aims to achieve a fairer burden and stabilize the international tax system. Japan and Korea, members of both the OECD and the G20, have been early adopters and key players in shaping the historic Two-Pillar deals. Most members in the region, irrespective of their

[42] India, among other jurisdictions, introduced a deemed permanent establishment in 2018, referred to as 'Significant Economic Presence (SEP)' within its tax legislation. However, the MLC may prohibit the application of certain types of SEP and Digital PE measure. Therefore, until the OECD reaches a consensus on a new tax regime for the digital economy, India's domestic provisions for SEP may undergo periodic changes (Popli, 2023).

membership status in the IF, are actively committed to pursuing the solution provided by Amount A, rather than posturing towards unilateral DSTs.

Pillar Two

27. **Several ASEAN+3 economies have started reviewing and amending their domestic laws in order to implement the GloBE Rules given developments in international collaboration to combat tax avoidance (Table 4).** However, due to the complexity of Pillar Two, only Korea and Japan have enacted legislation to fully implement it in 2024, while many others have postponed the commencement date to 2025. After introducing the global minimum tax into their domestic law, jurisdictions must undergo a peer review process established by the IF on BEPS. This process ensures compliance with GloBE rules and provides certainty to both implementing jurisdictions and MNE groups, helping companies anticipate the jurisdictions where they need to apply Pillar Two rules.

Table 4. Progress Towards the Implementing of the Two-Pillar Solution in ASEAN+3 (as of 15 December 2023)

	IIR	UTPR	QDMTT	Status
China	Awaiting details	Awaiting details	Awaiting details	Commentary
Hong Kong	January 2025	January 2025	January 2025	Official plan
Indonesia	Timing uncertain	Timing uncertain	Timing uncertain	Formal indication
Japan	1 April 2024	Timing uncertain	Timing uncertain	Legislation enacted
Korea	January 2024	January 2025	Uncertain	Legislation enacted
Malaysia	2025	Timing uncertain	2025	Official plan
Philippines	Awaiting details	Awaiting details	Awaiting details	Commentary
Singapore	January 2025	January 2025	January 2025	Official plan
Thailand	January 2025	2025	2025	Official plan
Vietnam	January 2024	No	January 2024	Official plan

Source: KPMG (2023b); Hadnum (2023b); AMRO staff compilation
Note: (1) Official plan means Program for implementation with dates; Formal indication means a written document has been issued by the government stating an intent to implement; Commentary refers to a review of domestic tax law from a Pillar Two perspective.
(2) The dates in the table represent anticipated implementation dates.

28. **Korea becomes the first country in the world to adopt the global minimum tax rules within its domestic legal framework.** The 2023 Korean Budget Bill states that the IIR and UTPR of the GloBE Rules are to be incorporated in the existing Law for the Coordination of International Tax Affairs (LCITA). Regarding the effective date, Korea proposed the 2023 Tax Revision Bill to postpone the UTPR by one year to 2025, which would be in line with the implmentation date in other major jurisdictions, while the IIR would

be imposed in 2024. Korea has urged other countries, particularly Vietnam, given the scale of Korean investment in Vietnam, to introduce their own legislation for GloBE Rules.

29. **Among ASEAN+3 economies, Japan is the second to pass legislation on Pillar Two.** Japan's 2023 Tax Reform proposal announced in December 2022 and the Bill for the Partial Revision of the Income Tax Act enacted in March 2023 include a legislative outline to implement global minimum corporate tax that aligns with the GloBE Rules starting from April 2024.[43] In addition, several crucial detailed provisions on the application of the GloBE rules in Japan are outlined in the Cabinet Order to Partially Amend the Enforcement Order of the Corporation Tax Law (Cabinet Order No. 208). Published in the Official Gazette in June 2023, the Cabinet Order provides details on GloBE income and adjusted covered taxes, which are required for the calculation of the GloBE effective tax rate in Japan.

30. **With substantial inward foreign direct investment (FDI) and being the headquarter jurisdictions for large MNEs, Hong Kong and Singapore are preparing domestic tax systems for the implementation of global tax reforms.** Anticipating the generation of annual tax revenue of USD15 billion from GloBE rules, Hong Kong plans to incorporate IIR and UTPR into the Inland Revenue Ordinance and roll out a domestic minimum top-up tax (HKMTT), which are set to take effect in 2025. Pillar Two's effect on Singapore will be substantial since approximately 1,800 companies in the country are part of in-scope MNEs (Vasal et al., 2023). Singapore thus announced its plan in the 2023 Budget Speech to implement GloBE rules (IIR, UTPR, and QDMTT) from January 2025**.** To mitigate the impact, its industry advancement initiatives will continue to ensure that the economy remains a compelling location for attracting and retaining investment. Meanwhile, China has agreed to the Two-Pillar solution, but its domestic implementation has been unclear. A consultation was issued by the Chinese Ministry of Finance in February 2023, but the Pillar Two effective date has not yet been announced (Hadnum, 2023a).

31. **Thailand and Vietnam are aligning with the global minimum tax while exploring potential measures to maintain FDI competitiveness.** The Thai government supports the implementation of a global minimum tax and is in the process of drafting a bill for the collection of a top-up tax, targeted to come into effect in 2025.[44] To enhance Thailand's competitiveness and promote long-term investment, Thailand's Board of Investment is currently amending the National Competitiveness Enhancement Fund Act and assessing the impact in various aspects. In November 2023, the Vietnamese parliament passed a resolution to implement the Pillar Two Global Minimum Tax in Vietnam with effect from 1 January 2024. The resolution includes IIR and QDMTT that broadly align with the GloBE rules, and it is estimated that about 113 MNES in Vietnam will be affected by the global minimum tax (Vietnam News, 2023). Given the potential impact on numerous foreign enterprises under the preferential tax regime and the top-up tax under Pillar Two, Hanoi Times (2023) reports that Vietnam authorities are considering providing monetary subsidies to in-scope MNEs, which raises concerns about compliance with OECD principles in the Pillar-Two Solution and national budget utilization.

32. **Malaysia and Indonesia also have started laying the groundwork to implement global tax reforms.** Committed to adopting internationally agreed tax reforms, Malaysia

[43] This outline includes the introduction of the IIR from 1 April 2024.

[44] This draft legislation considers allocating revenues from the top-up tax to the National Competitiveness Enhancement Fund, whose details are discussed between the Board of Investment and the Revenue Department.

completed public consultations in August 2022 and announced in the 2024 Budget Statement in October 2023 that its government will implement IIR and QDMTT starting from 2025. Indonesia issued Government Regulation No. 55/2022 (GR-55) as a legal foundation to recognize the Two-Pillar Solution as an international tax agreement that it would adhere to.[45] Nonetheless, specific requirements for the implementation in Indonesia, scheduled for 2024, are yet to be determined.

European Union

33. **In December 2022, the 27 European Union (EU) member states agreed, in principle, to implement the OECD's global corporate minimum tax.**[46] The European Commission ensures that global minimum tax rules adhere to EU law and facilitates the implementation of Pillar Two rules through the EU Global Minimum Tax Directive (EU Directive).The EU Directive is expected to be transposed into member states' domestic rules by the end of 2023.[47] EU member states are required to implement the IIR from 1 January 2024, while the UTPR will take effect one year later, starting 2025. The decision to adopt the QDMTT will hinge on individual countries' assessments of potential additional tax and compliance obligations (Table 5).

Table 5. Implementing the QDMTT in EU and other countries

	QDMTT (Enacted/ Draft)	Effective Date	Annual Estimated Corporate Tax Revenue from Pillar Two (USD billion)
Czech Republic	Yes – Draft	31 December 2023	0.225
Denmark	Yes – Draft	31 December 2023	0.35
Germany	Yes – Draft	30 December 2023	2.245
Liechtenstein	Yes – Draft	1 January 2024	–
Netherlands	Yes – Draft	31 December 2023	0.5
Norway	Yes – Draft	1 January 2024	–
Sweden	Yes – Draft	31 December 2023	–
Switzerland	Yes – Draft	1 January 2024	0.6
United Kingdom	Yes – Enacted	31 December 2023	2.7

Source: Hadnum (2023b); Bunn and Weigel (2023)
Note: Pillar Two revenue estimates may not be directly comparable with one another due to variations in each country's methodology.

34. **Numerous EU members have taken substantial strides towards compliance, illustrating a collective effort to align with the new international tax standards.**

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[45] Starting on 20 December 2022, the GR-55 designates the multinational tax agreement on BEPS as one of the international tax agreements that the government will adhere with.
[46] The current Pillar Two proposal requires unanimous agreement among the 27 EU member states.
[47] EU Member States are given the option to defer IIR and UTPR implementation for six years to December 31, 2029, where there are a maximum of 12 in-scope ultimate parent entities (UPEs) located in their jurisdiction (EU countries with likely no more than 12 UPEs include Bulgaria, Croatia, Cyprus, Estonia, Hungary, Latvia, Malta, Romania, Slovenia and Slovakia) (KPMG (2023b)).

Examples of progress made in the transposition of the EU Directive into respective countries' tax systems includes the release of a draft Finance Bill for 2024 outlining the transposition of the EU Directive into French domestic law, a consultation on transposition in Hungary, the publication of draft legislative decrees in Italy and discussions in Lithuania. Additionally, the Netherlands has issued a memorandum addressing parliamentary inquiries regarding the bill on the Minimum Profit Tax Act 2024, while Sweden aligned its Ministry of Finance's draft bill with the EU Directive. Meanwhile, Switzerland has enacted a constitutional amendment enabling temporary ordinances for Pillar Two execution, and Turkey has made amendments to its accounting standards, aligning with Pillar Two Model Rules. The EU's effort to harmonize tax practices underlines a shared commitment to a fairer and more transparent international tax environment.

35. **Once Pillar Two comes into effect, EU member states need to simplify the existing anti-avoidance rules.** Prior to Pillar Two, EU member states have acknowledged BEPS actions for many years and implemented various anti-avoidance regimes to combat base erosion and profit shifting by multinationals. One such common approach is the Controlled Foreign Corporation (CFC) regime, which taxes foreign earnings of domestic companies and disincentivizes profit shifting. Given the similarity between CFC rules and the IIR under Pillar Two, CFC rules would apply first, followed by GloBE rules, while preserving the efficacy of anti-profit shifting practices. Furthermore, for small companies outside Pillar Two's scope, CFC legislation could be amended to align with the 15 percent global minimum tax rate (Bunn, Cole, & Mengden, 2023).

The United States

36. **Despite the U.S. not having adopted Pillar Two yet, its most recent major reform for taxing the foreign profits of MNEs shares some common elements with Pillar Two Model Rules.** Prior to the Pillar Two agreement taking shape, the U.S. introduced the Global Intangible Low Tax Income (GILTI)[48] through the Tax Cuts and Jobs Act of 2017 (TCJA) in an effort to discourage U.S. companies from shifting profits offshore, particularly by transferring intangible assets to low-tax countries. Although the GILTI is intended to reduce incentives for profit shifting by imposing a minimum tax rate ranging from 10.5 percent to 13.125 percent on CFC-deemed intangible income,[49] it has faced certain concerns on multiple fronts. These concerns include the GILTI's minimum tax rate being too low, as well as the calculation of the GILTI which consolidates all foreign activities on a worldwide basis (Global Blending), rather than calculating on a country-by-country basis that would more closely resemble the IIR under Pillar Two. The U.S. is currently considering the imposition of a more Pillar-Two compliant version of GILTI.

37. **Moreover, the U.S. has independently introduced an Alternative Minimum Tax (AMT) through the Inflation Reduction Act (IRA) of 2022.** Like the OECD/G20's initiatives, the IRA aims to curb corporate tax competition by taxing income reported in the financial statement rather than taxable income under tax accounting, which could hinder global efforts to standardize the tax treatment of foreign income. In addition, like Pillar Two, the AMT targets large corporations with annual revenues exceeding USD1 billion[50] and sets a corporate minimum tax rate at 15 percent. Despite these similarities, the integration of the

[48] GILTI refers to the income earned by foreign affiliates of U.S. companies from intangible assets such as patents, trademarks, and copyrights.
[49] The minimum rate will change to 13.125 percent and 16.4 percent beginning in 2026.
[50] This threshold is similar to EUR 750 million for the in-scope MNEs under Pillar Two.

AMT into GloBE rules remains uncertain due to notable differences between the AMT and Pillar Two (Table 6).

Table 6. Comparison between the U.S. AMT and Pillar Two

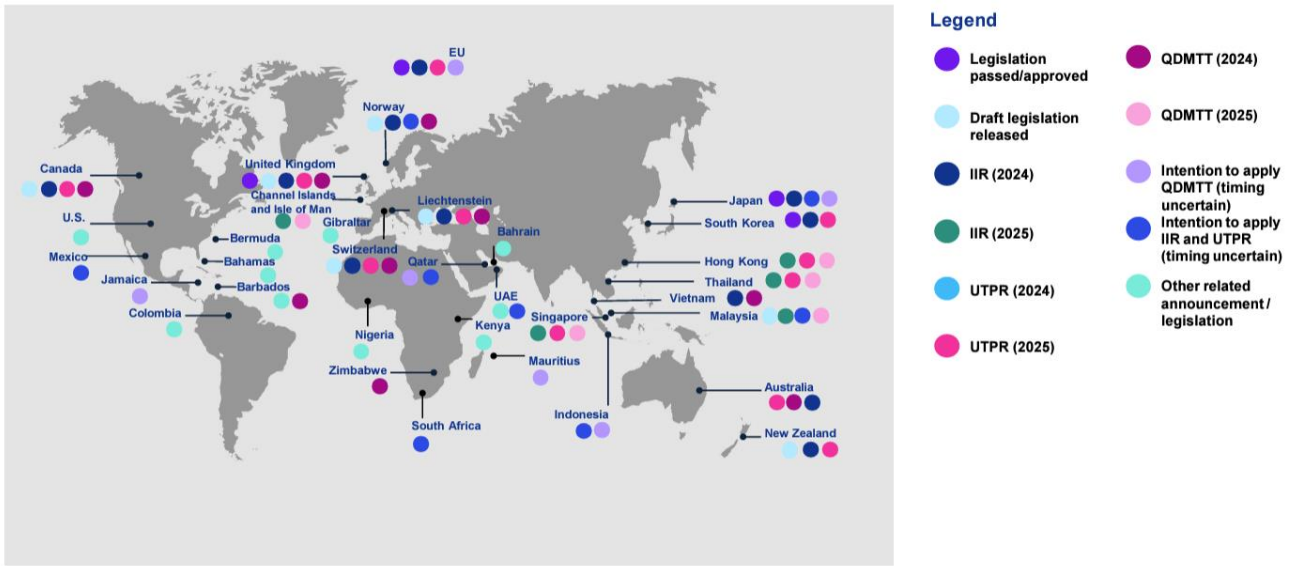
	The AMT	The GMT: Pillar Two
Tax base	Global income of U.S. companies	MNEs' disaggregated income
Tax Credits	A variety of tax credits and capital write-offs	A few defined refundable tax credits
Carve-out	Does not exclude any payroll costs, but contains an explicit carve-out for private equity	Provides 5 to 10 percent carve-out on payroll and assets
Foreign Taxes	Full credit for foreign taxes	15 percent tax rate
Exemption	Exempts research and development credits, but not stock options	Exempts stock options, but not research and development credits

Source: Lickess (2022)

38. **The OECD's top-up taxes scheme has raised concerns among U.S. policymakers, given the country's extensive use of tax incentives.** For example, the U.S. Congress has provided several business tax credits, such as the New Markets Tax Credit and the Work Opportunity Tax Credit, to support certain areas or/ and populations. The benefits of these tax credits could be nullified as the implementation of Pillar Two brings up the effective tax rate to 15 percent. Further potential outcomes include heightened tax disputes that come about as a result of trying to align Pillar Two rules and domestic tax laws, particularly in determining if certain taxes can be credited or not in the calculation of the tax base for GloBE rules. In response to these challenges, the OECD/G20 issued a guidance package in early 2023 to provide certainty on several key issues, including the protection of green tax credits, and the clear treatment of taxes paid under the GILTI regime.

39. **The U.S and the rest of the world have continued their collective efforts for the global adoption of Pillar Two.** The domestic legislative process for Pillar Two is already underway in many parts of the world. Likewise, the U.S. has consistency supported Pillar Two and proposed potential modifications to U.S. tax law to enhance compliance with Pillar Two and protect U.S. tax rights. However, given the recent unilateral tax reforms in the U.S. mentioned above, the interaction between the new U.S. tax rules and the GloBE rules will need additional considerations and this will take time before the U.S can fully implement the Two-Pillar solutions. As a result, the OECD/20 has devised a safe harbor provision for countries with a statutory corporate income tax rate of at least 20 percent, granting them relief from Pillar Two's enforcement mechanisms such as the implementation of UTPR until the end of 2026. The U.S. qualifies for this safe harbor due to its 21 percent headline tax rate, enabling U.S. policymakers to advance the implementation of the global minimum tax and create a level playing field for U.S. businesses, especially as Pillar Two is likely to increase taxes on U.S. corporations and shareholders. To mitigate the downsides of Pillar Two, the Congress and OECD/G20 may provide further guidelines for preserving tax credits while also considering the tax compliance costs for U.S. firms to avoid reduced returns to shareholders.

Figure 7. Global Progress Towards the Implementation of Pillar Two



Source: KPMG (2023b)

V. Policy and Administrative Implications for ASEAN+3 Economies

Pillar One

40. **Participating economies should have a thorough understanding of the MLC provisions and carefully assess its implications for their economies.** Under Amount A, most market jurisdictions in ASEAN+3 are expected to benefit from the taxing right allocation, but some economies with many headquartered MNEs may lose some revenues. For example, many MNEs are headquartered in Hong Kong, accounting for around 6 percent of global residual profits, Hong Kong's revenue loss is estimated at about 0.16 percent of GDP (IMF, 2022). The OECD released in October 2023 the draft text of MLC to implement Amount A of Pillar One, along with publishing an Explanatory Statement and the Understanding on the Application of Certainty of Amount A. Authorities of participating economies should familiarize themselves with these final MLC details and related publications, especially since the entry into force of the MLC will depend on ratification by 30 states, representing at least 60 percent of the Ultimate Parent Entities of MNEs initially expected to be in-scope for Amount A. In addition, jurisdictions with DSTs should assess the impact of DST removal, and those with sufficient capacity may consider imposing indirect tax, WHT or Digital PE on digital services considering their developing digital landscape and growing revenue need.

41. **The authorities need to engage in policy and administration discussions at the OECD and jurisdictional levels to apply Amount A.** To quantify the global residual profit, the OECD must first identify firms meeting the profitability and revenue thresholds and calculate each firm's residual profit. Subsequently, the revenue impact associated with residual profit reallocation will depend on various factors such as the size of the economy, the share of digital economy relative to the overall economy, the presence of MNEs and their subsidiaries operating in the economy, and the current taxation system. Authorities should participate in information exchange for Amount A calculation and closely monitor additional discussions and decisions regarding the reallocation of residual profit. The authorities should also provide mutual assistance in the collection of revenue claims and in the service of documents with respect to the taxes. At the jurisdictional level, authorities and MNEs need to collaborate to apply a set of rules to determine if an MNE is in scope, identify eligible market jurisdictions, calculate and allocate a portion of excess profits, eliminate double taxation, and prepare for tax filling and payments. Once the Amount A becomes effective, in-scope MNEs and authorities will also need to adhere to compliance and administrative obligations in the MLC. Therefore, the compliance burden on in-scope MNEs and the administrative burden on tax authorities under Amount A will be significant.

42. **The positive impacts of Pillar One extend beyond Amount A, particularly for developing countries that have already implemented or plan to implement transfer pricing rules.** Numerous OECD and some non-OECD countries have introduced transfer pricing rules into their tax legislations to ensure that MNEs report profits in accordance with internationally accepted principles and to counter abusive transfer pricing by MNEs. However, relatively few developing countries have fully effective transfer pricing regimes to address risks arising from BEPS. Amount B, scheduled for implementation when the OECD issues guidelines in 2024, aims to simplify the administration of existing transfer pricing rules by creating global transfer pricing benchmarks for common transactions. Developing

countries can leverage Amount B of Pillar One to initiate or strengthen their transfer pricing rules, resulting in less costly transfer pricing disputes, improved tax certainty, and ultimately effective transfer pricing rules crucial in protecting the tax base of developing countries.

Pillar Two

43. **The international agreement on Pillar Two is designed to raise global revenue and provide new impetus for jurisdictions to engage in tax incentive reform.** ASEAN+3 economies need to carefully assess the implications of Two-Pillar rules on their domestic laws as well as their impact on revenue and investment at the earliest, and before Two-Pillar rules fully come into effect. After clearly determine the number of in-scope MNEs, jurisdictions should start assessing tax incentives currently in place. Domestic and foreign companies falling outside the scope of Pillar Two can still enjoy existing tax incentives. However, in-scope companies paying an effective corporate tax rate of under 15 percent will see certain tax incentives no longer effective. Pillar Two thus offers a unique opportunity to reform tax incentives, especially for developing economies, to attract genuine investment and discourage incentives that allow MNEs to benefit from profit shifting and windfall gains.[51]

44. **In addition to the assessment of economic impacts and tax incentives, jurisdictions should promptly introduce top-up taxes, particularly the QDMTT.** While the transposition of GloBE's top-up taxes into domestic laws can be intricate, delaying the imposition of these top-up taxes may lead to foregone tax revenues flowing to other jurisdictions that enforce Pillar Two's top-up taxes. To tackle this legislative challenge, the GloBE Model Rules serve as a template that can be used as a basis for domestic legislation to apply QDMTT, IIR and UTPR. The adoption of the QDMTT is highly recommended to preserve country's tax base since the implementing jurisdictions would be the first in line to receive any top-up tax revenue from MNE's excess profit that is being taxed below 15 percent. The IF members expect that a QDMTT could eventually reduce the top-up tax to zero (Lipeles, et. Al., 2022).

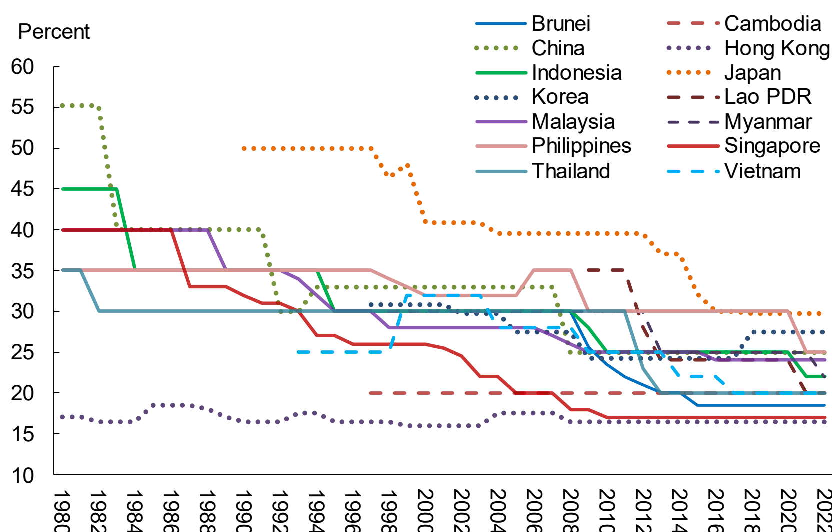
45. **Nonetheless, the top-up taxes should not be treated as a substitute for in-depth tax reform.** Pillar Two's main goals are to curb the risk of tax base erosion and profit shifting, and prevent a race to the bottom by jurisdictions offering the lowest effective tax rates to attract investment. Revisiting tax incentives is imperative for developing ASEAN+3 economies since they widely used CIT incentives such as reduced CIT rates and preferential tax regimes (Figure 8). The OECD categorizes tax incentives into two main groups: 'income-based tax incentives' that are likely to significantly impact top-up taxes under GloBE rules and should be reviewed; and 'expenditure-based tax incentives' that are expected to have less of an impact on GloBE top-up tax and could be retained as is. 'Income-based tax incentives', such as tax holidays, reduced CIT rates on total income, and broad-based tax incentives applicable to all types of income, are highly likely to reduce the tax liability within a jurisdiction. This reduction is comparable to the decrease in GloBE-adjusted covered tax, resulting in a low jurisdictional ETR and a higher top-up tax rate. Nevertheless, 'expenditure-based tax incentives' such as accelerated depreciation on tangible assets, tax credits, and targeted tax incentives have relatively less impact on GloBE-adjusted covered tax and jurisdictional ETR. On the tax administration front, some ASEAN+3 economies can make

[51] Windfall gains refer to the investment that would have been undertaken even without tax incentives.

use of their well-developed digital landscape and digital technology to digitalize tax administration, simplify administrative processes, and strengthen revenue collection.

46. **ASEAN+3 economies should revisit and redesign their tax incentives to put greater focus on expenditure-based and targeted tax incentives, which demand a larger administrative capacity.**[52] Expenditure-based incentives are generally preferred over income-based tax incentives because they can target specific activities and have a higher likelihood of attracting investments that would not have been made without such incentives. Although the expenditure-based tax incentives tend to reduce redundancy and exploitation of incentive benefits and brings a greater predictability in terms of revenue loss, they require higher tax administration capacity compared to income-based tax incentives. This could pose operational challenges for low-income countries, which often face limited administration capability. As a result, the revision of tax policies, incentives, and administration should strike a balance between ensuring the right to tax and minimizing adverse effects on competitiveness, administrative capacity, and the ability to attract investments.

Figure 8. Top Statutory Corporate Income Tax Rates of ASEAN+3 economies from 1980 to 2020



Source: Enache (2022); AMRO staff compilation

47. **Imposing Pillar Two rules in domestic laws is an unprecedented tax reform and the authorities must keep close communications with businesses and international organizations.** The promulgated legislation and procedures should be communicated to the business community in a timely manner to minimise compliance cost. Tax authorities should also provide training for officials and businesses to ensure an efficient implementation and minimise any disputes. To ensure a swift and proper implementation of legal adjustments,

[52] Andriansyah, Hong, & Nam (2021)

seeking technical assistance from the OECD[53] and relevant international organizations[54] is also considered, especially in areas of GloBE rules and their interaction with domestic regimes such as tax incentives. Improving clarity, communication, and transparency between tax authorities and taxpayers fosters a more favourable investment environment and helps companies in planning and compliance in advance. Given the different stages of Pillar Two implementation across ASEAN countries, a region-wide effort, such as the ASEAN Forum on Taxation (AFT), could help facilitate implementation, capacity building, and dispute resolution mechanisms in the region. Moreover, in countries with limited capacity, the OECD's Forum on Tax Administration (FTA) can provide additional support for the digitalization of tax administration in developing countries.

48. **With the global minimum tax under Pillar Two, member economies will need to focus more on non-tax measures to uphold their competitiveness and firms will experience higher relevance of non-tax factors in making location decision.** As the global minimum tax under Pillar Two will decrease tax competition, boosting MNE investment will require a more emphasis on non-tax investment attraction policies, including macroeconomic and political stability, competitive human capital and labor costs, strong rule of law, institutional consistency, and efficient hard and digital infrastructure. In addition, the OECD's formulaic substance-based carve-out is designed to affect MNEs engaging in profit shifting. MNEs' location choice will become less dependent on tax gains and more relying on the non-tax factors. The investment in tangible capital assets and payroll in a jurisdiction is therefore particularly important as it will increase the substance carve-out, which in turn reduces the Pillar Two top-up tax even when there is a low jurisdictional ETR.

49. **Pillar Two, despite concerns about implementation costs and uncertain revenue gains, will ultimately enhance countries' revenues through improved tax policies and stronger tax administration.** The escalating layers of complexity of Pillar Two have raised concerns among ASEAN+3 economies about the expected income gains. Quantifying the revenue and investment impact of Pillar Two in ASEAN+3 remains challenging due to a lack of detailed data to identify the number of in-scope MNEs with operations in each jurisdiction and the income generated by these operations. Moreover, in the absence of low-taxed incomes or a few entities in the jurisdiction falling under the global minimum tax rules, the implementation costs may outweigh benefits. However, the OCED/G20's new international tax rules along with the capacity-building efforts undertaken by ASEAN+3 economies will raise countries' revenues through better tax policy and stronger tax administration. Pillar Two will eventually harmonize base erosion rules across many countries and increase tax certainty in the international tax system for taxpayers and tax authorities, which can help maximise the mobilization of government revenues, especially for developing and emerging economies.

[53] The OECD Secretariat has provided various outreach activities, developed training programs and seminars, offered courses, and provided targeted support to build capacity on the Two-Pillar Solution. By the end of 2023, the OECD Secretariat, in collaboration with relevant regional and international organizations, will develop a plan aimed to provide additional support and technical assistance to enhance the capacity required for the full implementation of the Two-Pillar Solution.

[54] Tax Inspectors Without Borders (TIWB), a joint OECD/UNDP initiative, has been providing tax capacity building guidance/ services since 2015 through hands-on learning by deploying experts to work alongside tax administration officials. There is growing demand and potential for the TIWB initiative to expand its scope, including a broader range of international tax capacity building, such as effective implementation of the global minimum tax, auditing VAT on digital trade and effective use of country-by-country reporting data.

Table 8. Summary of Key Policy Responses and Administrative Implications in Preparation for the Implementation of the Two-Pillar Solution

<table>
<tr><th></th><th>Preparation</th><th>Tax Policy/ Non-tax Policy</th><th>Tax Administration</th></tr>
<tr><td>Pillar One</td><td>➢ Consider final details of the MLC and its implications to the country
➢ Identify revenue impact from Amount A</td><td>➢ Implement VAT, WHT and Digital PE on cross-border digital services
➢ Apply basic transfer pricing rules if capacity allowed</td><td rowspan="2">➢ Engage in capacity building and exchange of information
➢ Digitalize tax administration
➢ Seek support from International Organization
➢ Consider joining Inclusive Framework to benefit from exchange of information and other supporting tools</td></tr>
<tr><td>Pillar Two</td><td>➢ Analyse revenue and investment implications of the global minimum tax
➢ Assess tax incentives currently in place</td><td>➢ Implement QDMTT
➢ Improve non-tax measures
➢ Implement IIR and UTPR
➢ Redesign income-based tax incentives to expenditure-based tax incentives</td></tr>
</table>

Source: González et al. (2023), OECD (2022, 2023b, 2023c, 2023e, 2023i); AMRO staff compilation

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