EFAMA
European Fund and Asset Management Association

COMMENT PAPER

Brussels, 10 March 2023

INTERNATIONAL TAX REFORM PILLAR TWO MODEL RULES | EFAMA COMMENTS ON IASB's EXPOSURE DRAFT ON THE PROPOSED AMENDMENTS TO IAS 12

EFAMA is grateful for the opportunity to comment on the International Accounting Standards Board (IASB) Exposure Draft (ED) on the proposed amendments to IAS 12 to address the challenges arising from the implementation of the Pillar Two model rules that aim to address the tax challenges arising from the digitalisation of the economy; and provide a template for the implementation of a minimum corporate tax rate of 15% that large multinational companies would pay on income generated in each jurisdiction in which they operate.

The IASB aims to introduce a temporary exception from accounting for deferred taxes arising from legislation enacted to implement the Pillar Two model rules, as well as targeted disclosures for affected entities. The exception would apply until such time that the IASB decides to either remove it or make it permanent.

We understand in the proposed ED that the IASB is aware of the complexity of the new tax laws to be enacted in multiple jurisdictions in a short period and aims to ensure IAS 12 is applied consistently allowing stakeholders to assess how the new rules will/have been implemented in the several jurisdictions where their activities take place and learn how they will be impacted by them. At the same time, the IASB also needs to consider if further work needs to be undertaken.

As a principle, this initiative is to be welcomed by EFAMA.

When engaging with the OECD and European Commission to comment on the Model Rules as well as on Pillar Two proposal, **EFAMA expressed its support for these initiatives to ensure a global minimum level of taxation for multinational groups, provided tax neutrality in respect of investment funds is preserved**.

Our comments and concerns have been acknowledged both at the level of the OECD and European Commission and, as a principle, investment funds and investment entities should be covered by the carved-out / exclusion rules from Pillar Two.

If *"[t]he need to preserve the tax neutrality in respect of investment funds is a widely recognised principle that underpins the design of the international tax rules"*, the same need and principles should also underpin the design of international accounting standards.

The vast majority of investment funds are not required to consolidate (IFRS 10/11/12 consolidation package exemption for investment entities)[1] and **the rules drafted by the OECD establish that investment funds and investment entities should be carved out / excluded from Pillar Two**. As the tax neutrality for the industry has been acknowledged and catered for in the new rules, **at first glance we expect them would not have a significant impact on our industry (at least on the strict product/funds side)**. As to the corporate tax compliance of our members, we are monitoring the real impact of the new rules on MNE Groups in scope and **while it is still to be confirmed what will be required from asset management firms and investors investing in funds to comply with the new rules**, **it is clear the analysis is highly complex**. **It is in this context that the temporary exception is to be welcomed.**

At this stage, **EFAMA members are still monitoring the impact of the Pillar Two rules on their structures**. Some **concerns and challenges may arise** where a fund is held and consolidated under the accounts of an MNE Group in the scope of Pillar two, or in other situations where the investment vehicles/structures would unintendedly be in scope, but **the real impact of the proposals on the industry remains unclear**.

EFAMA members are also monitoring the work of the OECD Secretariat and **raising awareness on situations where more work/clarity/certainty is needed, on the challenges businesses/countries are facing on the implementation of the new rules** (with a particular focus on the discussion of specific rules (points 7.4, 7.5 and 7.6 of the Model Rules) that apply to Asset Managers and Insurance Companies). The OECD teams already recognized they need to find a solution to solve some pending issues, and this is one of the areas that may be covered in additional guidance to be released while countries implement the new legislative packages.

Some of these challenges are being addressed and acknowledged by the Inclusive Framework and the OECD Secretariat technical teams that have been working on the implementation package to ensure the new rules are implemented in a consistent and harmonised manner with a proportional impact on the compliance and administration costs both for tax administrations and businesses (with the maximum degree of tax certainty for MNEs as possible).

To achieve these goals the OECD have released the Model Rules, Commentaries, Illustrative Examples, as well as administrative guidance. To ensure that the GloBE Rules continue to be implemented and applied in a coordinated manner it was announced the Inclusive Framework will continue to release further guidance on an ongoing basis.

Stakeholders are still reviewing the GloBE information return documentation released by the OECD and our industry needs to understand what specific data the MNE Groups that have invested in funds may need to comply with the new rules. The implementation of these, in particular **the implementation of a Pillar Two strategy within these corporate groups, may require a very significant undertaking**, especially if we consider the data that will be requested may not currently exist or be available in the standard data sets being used by the industry – with some concerns being already raised that the work to get the data/information and populate these returns will most likely be difficult, expensive and to a certain extent may not be successful.

One of the concerns that are still being discussed amongst the delegates at the OECD is to what extent stakeholders will have to do the domestic filing of these reports in jurisdictions that introduced a qualified domestic minimum top-up tax but also do the same filing at a global level. **Any duplication of efforts and the possibility of having stakeholders filling the same information twice is something to be avoided**. Delegates and the OECD Secretariat are trying to find out a mechanism that would avoid this and allow the fillings to be made only once (as fundamentally the information to be reported should be the same).

[1] See here the comments delivered by EFAMA in the context of the recently concluded post-implementation review of these standards.

We are also monitoring the work of EFRAG that, in the future, may be called by the European Commission to endorse these amendments to the accounting standards applicable in the European Union (please refer to EFRAG's draft comment letter to this ED). **To a large extent, the comments made so far by EFRAG are to be supported.**

We are also broadly in agreement with the comments made by ESMA (please refer to the letters sent by ESMA to the IASB and EFRAG). Notwithstanding **the comments made by ESMA**[2] **on the need to have additional disclosures may need to be received with caution**. It is critical that **if there are to be any additional or specific disclosure requirements, these should be subject to normal materiality considerations**. For many international groups, the incremental Pillar 2 tax payable will not be material and it would therefore be highly disproportionate to require specific disclosures on each jurisdiction, where any top-up tax is likely to be immaterial – please refer to EFAMA's comments on Question 2.

To address the queries raised by the IASB in the ED and confirm if and why we agree with the proposals being drafted, **we have agreed on the following high-level comments:**

- **Question 1—Temporary exception to the accounting for deferred taxes (paragraphs 4A and 88A)**

  We agree with this proposal, under which a mandatory temporary for either recognising and disclosing information about deferred tax assets and liabilities related to Pillar Two income taxes are applicable. Notwithstanding, it should be clarified whether and how paragraph 4A applies to the subsidiary's separate financial statements level or sub-group consolidated financial statements level.

- **Question 2—Disclosure (paragraphs 88B–88C)**

  Suggestion for par. 88B: An entity with revenues above 750 Million € should disclose if it is exposed or not exposed to Pillar Two legislation. When a company is exposed to Pillar Two legislation, it shall disclose separately its current tax expense (income) related to Pillar Two income taxes.

  Requirement (b)[3] raises several concerns:

  - places an unreasonable burden on large companies, even where top-up tax may be material. The calculated ETR in the exposure draft will be different from the Globe ETR, which makes various adjustments to accounting income, and is therefore of little help to the reader as it does not quantify any incremental tax due. There is therefore a risk that the reader of the financial statements will be confused by the information provided.

  - does not comment as to what measure of accounting income is by jurisdiction. Requiring MNEs to consolidate income and tax by jurisdiction for these purposes would be disproportionate.

  If it is accepted that this disclosure requirement is flawed, it would not in the alternative be appropriate to provide a full Globe tax calculation in financial statements as this requires MNEs to perform accurate calculations significantly in advance of any tax filing. There is no existing requirement for MNEs to quantify future tax liabilities in their financial statements.

  As the rules may result in incremental tax falling due, from an accounting standpoint, the approach to be followed should not differ from any other significantly enacted tax rate change – and accounting standards already provide a framework for dealing with tax rate changes.

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[2] In ESMA's letter we can read that *"[a]lthough the specific requirements with regards to the calculation of the effective tax rate included in Pillar Two model rules differ from those in IAS 12, ESMA considers that the proposed disclosures will provide useful indications of an entity's potential exposure to top-up taxes. ESMA also agrees with the separate disclosure of current tax expense related to Pillar Two income taxes as it would enable users to understand the magnitude of these taxes"*

[3] In the ED we can read as follow: *"the jurisdictions in which the entity's average effective tax rate (calculated as specified in paragraph 86 of IAS 12) for the current period is below 15%. The entity would also disclose the accounting profit and tax expense (income) for these jurisdictions in aggregate, as well as the resulting weighted average effective tax rate."*

- **Question 3—Effective date and transition (paragraph 98M)**

  We agree with this proposal.

In general, EFAMA is very supportive of the IASB's efforts to ensure consistency in the application of IAS 12 and remains at the disposal of the technical teams to further discuss any challenges arising from the implementation of Pillar Two that would need to be addressed.

Contacts:

António Frade Correia
Senior Tax Advisor
antonio.fradecorreia@efama.org | +32 2 513 39 69