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# Revolutionizing Global Taxation: Unveiling The Two-Pillar System, Assessing Impacts, and Navigating Challenges

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## ABSTRACT

*The Two-Pillar Tax System, proposed by the Organization for Economic Co-operation and Development (OECD), represents a paradigm shift in international taxation, aiming to address the challenges posed by the digital economy and profit shifting. Pillar One of the system focuses on the digital economy, introducing the concept of Amount A, which allocates a percentage of residual profits to market jurisdictions based on a revenue-based allocation key. Pillar Two is designed to establish a global minimum tax rate to prevent profit shifting to low-tax jurisdictions. It employs a mechanism where the effective tax rate of each jurisdiction is calculated, and if it falls below the minimum, a top-up tax is charged to the head office.*

*The implications of the Two-Pillar System are far-reaching. The fair taxation of digital businesses under Pillar One levels the playing field and ensures that multinational corporations pay their fair share in the markets where they operate. However, the implementation of the Two-Pillar System is not without challenges. Enforcing the rules uniformly across diverse jurisdictions requires international cooperation, and ensuring compliance may be a complex endeavor. The system may also prompt adjustments in global investment patterns as businesses navigate the new tax landscape, raising uncertainties about its long-term impact.*

*This article delves into the concept of Two-Pillar Taxation, an emerging framework in international taxation. It critically examines the pillars, their objectives, implications, and the challenges they pose to global tax policy. Through an in-depth analysis, we assess the potential benefits and drawbacks of this approach, highlighting its impact on multinational corporations, governments, and international tax norms. Additionally, we explore the policy implications and future of the global taxation and how the OECD & G20 would implement the two-pillar taxation system.*

**Keywords:** pillar one, pillar two, tax haven.

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## I. INTRODUCTION

The expansion of digitalisation and globalisation has impacted the international taxation system to a great extent. These twin forces have reshaped the working of businesses and income generation, challenging the previous tax regimes developed for a pre-digital and less globally interconnected world. Digitalisation has transcended businesses as they can now operate in different jurisdictions without having a physical presence. This has enabled multinational corporations to shift their high-earned revenue to jurisdictions having lower tax rates, also known as tax haven jurisdictions, eroding the tax base of countries where they operate. On the other hand, globalisation has paved the way for businesses to move goods, services and capital across borders at an unprecedented scale. Transfer pricing has become a focal point for the tax authorities to prevent profit shifting. Multinational companies can use transfer pricing to manipulate prices on transactions between related entities, allowing them to shift profits to low-tax jurisdictions while reducing taxable income in high-tax areas. This practice can lead to tax minimisation and is used by companies looking to maximise their earnings in a globalised economy.

The digital and globalised economy's developments and threats triggered the need for a new international tax regime. Finally, in December 2021, the Organisation for Economic Co-operation and Development released the Global Anti-Base Erosion (GLoBE) Model Rules<sup>3</sup> as approved by the OECD/G20 Inclusive Framework on Base Erosion And Profit Shifting (BEPS) to combat the issues of profit-shifting, tax avoidance and tax competitions among different jurisdictions. To do so, GLoBE has introduced a two-pillar tax package system wherein Pillar 1 will focus on the allocation of profits to low-tax jurisdictions, and Pillar 2 will ensure that a global minimum tax rate of 15 % is implemented. The Minimum tax will be achieved through three main rules<sup>4</sup> :

- i. Income Inclusion Rule
- ii. Under taxed Payments Rule
- iii. Subject to Tax Rule

In this article, we will deal with the Two-pillar tax system under which we will analyse Pillar One and Pillar Two. Further, we will evaluate the benefits, implications and challenges that

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<sup>3</sup> *BEPS & OECD: Taxation of the Digital Economy* ,BLOOMBERG TAX (Oct. 2, 2023, 10:07 AM), <https://pro.bloombergtax.com/brief/beps-the-oecd-taxation-of-the-digital-economy/>.

<sup>4</sup> OECD, *Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy*, OECD PUBLISHING (Oct. 2021), <https://www.oecd.org/tax/beps/brochure-two-pillar-solution-to-address-the-tax-challenges-arising-from-the-digitalisation-of-the-economy-october-2021.pdf>.

would be dealt with, particularly concerning developing countries and tax havens. Additionally, the role of international organisations such as the OECD would be considered. Finally, we speculate on the future of global taxation post-implementation, offering a comprehensive understanding of the Two-Pillar tax systems.

## II. WHAT IS BEPS AND OECD'S INCLUSIVE FRAMEWORK ON BEPS ?

Base Erosion Profit Shifting (BEPS) is a tax strategy employed by multinational corporations (MNCs) to shift their profits to low-tax or no-tax jurisdictions, often through deductible payments like royalties and interests. This practice predominantly impacts developing countries that heavily depend on corporate tax revenues. According to the OECD, BEPS leads to annual global revenue losses ranging from \$100 billion to \$240 billion.<sup>5</sup>

To address the challenges posed by BEPS, the Organisation for Economic Cooperation and Development (OECD) and the G20 countries collaborated on the Base Erosion and Profit Shifting Action Plan. The need for such a plan became evident in 2012 when MNCs began exploiting gaps in international tax rules to redirect their earnings to low-tax havens. In 2013, the OECD initiated the BEPS project<sup>6</sup>, culminating in the release of the BEPS 15 action plan in 2014<sup>7</sup>, comprising various measures to combat tax avoidance.

The BEPS Action Plan covers a wide array of topics, including addressing tax challenges in the digital economy, preventing treaty abuse, and introducing country-by-country reporting (CbCR) requirements for MNCs, with Action 13 being one of the first measures widely implemented. Additionally, the Multilateral Convention to Implement Tax Treaty-Related Measures to Prevent BEPS (MLI) was created as part of BEPS Action 15, enabling countries to swiftly adapt their existing tax treaties to incorporate BEPS-related provisions.

The OECD and G20 have established an inclusive framework on BEPS, allowing countries and jurisdictions to join and commit to adopting BEPS measures. Currently, 141 countries have become part of this Inclusive Framework.<sup>8</sup> According to the OECD's statement, the new BEPS rules were to be implemented from 2021<sup>9</sup>, marking a significant global effort to combat tax

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<sup>5</sup> OECD, *OECD/G20 Base Erosion And Profit Shifting Project*, OECD PUBLISHING, (2015), <https://www.oecd.org/ctp/beps-frequently-asked-questions.pdf>

<sup>6</sup> OECD, *Action Plan on Base Erosion & Profit Shifting*, OECD PUBLISHING, (2013), [https://read.oecd-ilibrary.org/taxation/action-plan-on-base-erosion-and-profit-shifting\\_9789264202719-en#page5](https://read.oecd-ilibrary.org/taxation/action-plan-on-base-erosion-and-profit-shifting_9789264202719-en#page5)

<sup>7</sup> *Id.*

<sup>8</sup> OECD, *Members of the OECD/G20 Inclusive Framework on BEPS*, OECD PUBLISHING, (Jun.9,2023), <https://www.oecd.org/tax/beps/inclusive-framework-on-beps-composition.pdf>

<sup>9</sup> *OECD/G20 Inclusive Framework Agreement on BEPS 2.0*, KPMG, ( Oct. 3, 2023, 1:07 PM) <https://kpmg.com/xx/en/home/insights/2021/06/tax-policy-perspectives.html#:~:text=The%20statement%20provides%20that%20the,implementation%20plan%20by%20Oct ober%202021.>

avoidance and establish a fair and equitable international tax system.

### **III. PILLAR ONE : NEXUS & PROFIT ALLOCATION**

Pillar One of the new international taxation systems represents a paradigm shift in how multinational enterprises are taxed as it paves a way to address the challenges posed by the globalisation and digitalisation of the world economy, leading to the erosion of the traditional tax system. In today's digital age, businesses can efficiently operate across borders, generating significant profit even without a physical presence in that country. This has raised concerns about profit shifting, base erosion and loss of tax sovereignty of individual nations. Pillar One, developed by OECD aims to tackle these concerns by incorporating a new taxing regime. This system ensures that multinational corporations are taxed in every jurisdiction where they earn profits, irrespective of their physical presence.

Pillar one mainly covers the reallocation of taxing rights to the market jurisdictions. It aims to reallocate profits of over 100 of the world's largest and most profitable multinational enterprises, having turnover of at least 20 billion Euros, to the market jurisdiction where these enterprises have their consumer irrespective of their physical presence in that country<sup>10</sup>. The pillar uses revenue sourcing rules for determining whether it is generated from a particular market jurisdiction and profit allocation rules for allocating the profits to these market jurisdictions.

#### **(A) Fundamental Concepts Under Pillar One :**

Pillar One of the international tax framework encompasses several key criteria determining its applicability.

##### **a. Thresholds and Scope:**

Companies eligible to participate in this system must meet specific financial thresholds, including a global turnover of at least 20 billion Euros and a profit-to-revenue ratio of 10%.<sup>11</sup> These thresholds target larger multinational enterprises operating in the digital economy and highly digitalised sectors.

##### **b. Nexus Criteria:**

The concept of "nexus" is crucial in determining whether a market jurisdiction is entitled to receive tax allocations under Pillar One. In cases where a jurisdiction's gross domestic product (G.D.P.) exceeds 40 billion Euros, revenue generation must surpass 1 million Euros to establish a nexus. For smaller jurisdictions with a G.D.P. below 40 billion Euros, nexus is set at 250,000

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<sup>10</sup> *Supra*, note 2.

<sup>11</sup> *Supra*, Note 2

Euros.<sup>12</sup> This ensures that only market jurisdictions with a specific economic activity are eligible to reallocate tax revenues.

**c. Exclusions:**

Pillar One has defined specific exclusions. Expressly, extractive industries and regulated financial services are excluded from the scope of this pillar, focusing instead on businesses primarily engaged in digital and digitalised sectors.<sup>13</sup>

**d. Revenue-Sourcing Rules:**

Pillar One introduces revenue-sourcing rules that dictate how revenue is attributed to specific market jurisdictions. The underlying principle is allocating income to the jurisdictions where goods and services are consumed or used. To achieve this, detailed source rules are being developed for distinct categories of transactions, ensuring a fair and accurate distribution of tax revenues among participating countries.

**e. Profit allocation:**

Pillar One assigns 20-30% of extra profit (more than 10% of earnings) to marketplaces connected to a company's operations. A revenue-based system determines the allocation and applies to certain multinational businesses (MNEs).

**f. Unilateral Measures:**

As per the Multilateral Convention (MLC), all parties must eliminate any Digital Services Taxes and other similar measures concerning all companies and pledge not to implement such measures. No new Digital Services Taxes or similar measures will be levied on any company until 31 December 2023 or the enforcement of the MLC, whichever is earlier.<sup>14</sup>

**(B) Key Components Of Pillar One Rule :**

The two primary components of the Pillar One taxation system are Amount A and Amount B.

**1. Amount A**

Amount A represents the portion of profits of MNEs that will be reallocated to the market Jurisdictions. This guarantees that jurisdictions receive their share of profits generated by MNEs in their markets, irrespective of MNEs physical presence. Pillar One recognises two types of Profits:

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<sup>12</sup> Radhakishan Rawal & Madhu Agarwal, *Pillar One and Pillar Two*, KPMG, (Jul.2021), <https://www2.deloitte.com/content/dam/Deloitte/in/Documents/tax/in-tax-pillar-one-and-pillar-two-noexp.pdf>

<sup>13</sup> *Id.*

<sup>14</sup> *Supra*, Note 10

*Routine Profits:* Routine profits are allocated for the business's day-to-day operations. These profits are those profits that fall within the ambit of the 10 % Profitability threshold.<sup>15</sup>

*Non-routine Profits:* These profits are also known as residual profits, and they exceed the 10% profitability threshold.<sup>16</sup> These could be attributed to activities beyond routine business operations like profits from Intellectual Property Rights, goodwill, etc.

Amount A is calculated based on a fixed percentage of these residual profits and typically falls within the 20%-30% range.<sup>17</sup> Between these, 20%-30% of residual profit is treated as Amount A. This means that non-routine profits are reallocated to market Jurisdictions where the company has a significant economic presence. This mechanism ensures that market jurisdictions receive a share of the profits commensurate with the economic activity conducted by the MNE in those jurisdictions.

## 2. Amount B

It is a mechanism for remunerating MNEs for their baseline marketing and distribution activities in the market jurisdictions.<sup>18</sup> The aim is to provide a standardised form of determining profits that would be allocated for marketing and distribution activities. It ensures MNEs receive arms-length principles compensation for these activities. Amount B provides transparent and predictable guidelines for determining remuneration, thereby minimising the probability of tax disputes and improving tax certainty.

## IV. PILLAR TWO: GLOBAL MINIMUM TAX

The objective of Pillar two is to define the amount of tax MNEs need to pay in the market jurisdictions where they operate. It contains two domestic and one treaty-based rule that together are known as Global Anti-base Erosion Rules (herein will be referred to as GLoBE rules).<sup>19</sup> Pillar Two aims to ensure that a minimum of 15 per cent of tax is paid irrespective of jurisdictions where they operate or are headquartered.

Pillar Two applies to MNEs with a total consolidated group revenue of at least Euro 750 billion or more.<sup>20</sup> This consolidated group revenue theory applies to companies controlled and owned by the same Parent Company. The Inclusive Framework Members are not required to adopt

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<sup>15</sup> *Supra*, Note 10

<sup>16</sup> *Supra*, Note 10

<sup>17</sup> *Supra*, Note 2

<sup>18</sup> *Supra*, Note 2

<sup>19</sup> David O'Sullivan and Ana Cebreiro Gómez, *The Global Minimum Tax: From Agreement to Implementation*, WORLD BANK,(2022), <https://openknowledge.worldbank.org/server/api/core/bitstreams/1b42e3ec-7e6e-570d-8809-e32b21e239ae/content>

<sup>20</sup> *Id.*

GLOBE rules, but if they choose to, they have to implement them according to the outcomes provided by Pillar Two.<sup>21</sup> Suppose the ultimate Parent Company is a Government entity, Non-governmental organisation, international organisation, pension or investment fund; then, they are excluded, meaning that GLOBE rules will not apply to them. Under Pillar Two, the governments still have the power to set up their corporate tax rates, but if a MNE tries to shift its profits to tax haven jurisdictions, the countries where the company has its residence can 'top-up' taxes to a 15 per cent global minimum rate.

#### **(A) Principle Rules of Pillar Two:**

The Global Minimum Tax consists of 3 principal rules<sup>22</sup>: the first two being domestic rules, the income inclusion rules, and the undertaxed payment rule, together known as the Global Anti-Base Erosion Rules(GLOBE), and the third one is a treaty-based rule known as Subject to tax rule. The proposal focuses on other BEPS issues and allows the jurisdiction to tax the transactions where payment is subject to no tax or low tax.

Let's discuss in detail what these rules state:

##### **a) Income Inclusion Rule (IIR)**

The countries will have the option to implement IIR under the Pillar Two Tax system. Under this, a top-up tax would be imposed on the parent entity with respect to the low-taxed income of its subsidiary entity<sup>23</sup>. It is implemented and enforced in the jurisdiction where the parent company's head office is situated. It applies in every jurisdiction where the company's subsidiary or branch office is located except for the jurisdiction of the head office<sup>24</sup>. The effective tax rate is calculated based on global minimum tax rules.<sup>25</sup> This takes into account all the consolidated branches in that jurisdiction, after which the effective tax rate is calculated.

If the effective tax rate falls below the global minimum tax rate, then a top-up tax is imposed on the parent entity<sup>26</sup> to compensate the jurisdiction with a lower effective tax rate. This is achieved by adding a portion of the subsidiary company's profits to the total taxable income of the parent entity.<sup>27</sup> The aim is to discourage profit shifting by companies to low-tax jurisdictions

<sup>21</sup> *Supra*, Note 2

<sup>22</sup> *Supra*, Note 17

<sup>23</sup> Belisa Ferreira Liotti et al, *The treatment of tax incentives under Pillar Two*, UNCTAD, 2022, [https://unctad.org/system/files/official-document/diaeia2022d3a2\\_en.pdf](https://unctad.org/system/files/official-document/diaeia2022d3a2_en.pdf)

<sup>24</sup> *Id*

<sup>25</sup> Ziyang Li, *The Impact of Pillar Two rules on China's Tax Incentives Policy*, RESEARCH SQUARE, (Jun.2023), <https://doi.org/10.21203/rs.3.rs-2998454/v1>

<sup>26</sup> *Supra*, Note 21

<sup>27</sup> *Understanding The Global Minimum Effective Tax On Multinationals*, WORLD BANK, (Apr.22,2022), <https://thedocs.worldbank.org/en/doc/e95e21b019d5aaf94d37aff0ad9203c9-0350032022/original/Understanding-The-Global-Minimum-Effective-Tax-on-Multinationals-Pillar-2-General->



and ensure fair implementation of international taxation principles.

### **b) Undertaxed Payment Rule (UTPR)**

The second rule of Pillar Two is the Undertaxed Payment Rule, which complements the Income Inclusion Rule. It comes into the picture when the effective tax rate of the jurisdiction where the parent entity is situated falls below the global minimum tax rate. This rule is paramount because IIR does not apply to the head office's jurisdiction<sup>28</sup>. In this case, the top-up tax is collected by those countries where the branches or subsidiaries are located<sup>29</sup>. UTPR ensures that a minimum tax rate is paid by MNEs even if the head office jurisdiction has a low tax rate.

### **c) Subject to Tax Rule (STTR)**

The subject-to-tax rule is a treaty-based rule that operates within the context of existing treaties between countries. It is enacted bilaterally following a request from either party to a treaty<sup>30</sup>. It overrides specific treaty benefits the existing treaties provide if it does not meet a minimum tax rate in the recipient jurisdiction<sup>31</sup>. It aims to prevent income shifting to low-tax jurisdictions by requiring that payments made by an entity of one country to its related parties in another country shall be subjected to a minimum tax rate in the recipient country. The STTR applies to those payments which could lead to manipulation of tax liabilities such as interest, royalties, etc.<sup>32</sup> This rule requires that the recipient countries receive the minimum nominal tax rate, which is often set in the range of 7.5%-9%<sup>33</sup>. The STTR does not depend on the revenue of the MNE; that is to say that, a minimum threshold of Euro 750 million does not apply in cases of STTR. When STTR is triggered, it denies all the treaty benefits. It applies before IIR & UTPR<sup>34</sup>, and the calculated amount is then considered for calculating IIR and UTPR. STTR is beneficial, especially for developing countries, as it helps them to protect their tax bases from erosion by MNEs.

## **V. HOW TWO PILLAR TAXATION PACKAGE WOULD BE IMPLEMENTED ?**

### **• Implementation Of Pillar One**

The amount A in pillar one would be implemented through the *Multilateral Convention (MLC)*

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Principles-Overview-and-Scope.pdf

<sup>28</sup> *Id*

<sup>29</sup> *Supra*, Note 25

<sup>30</sup> *Supra*, Note 25

<sup>31</sup> *Supra*, Note 25

<sup>32</sup> *Supra*, Note 25

<sup>33</sup> *Supra*, Note 17

<sup>34</sup> *Supra*, Note 25

and by amending the domestic laws of the countries and would be implemented by 2023<sup>35</sup>. MLC would develop a multilateral framework for all the jurisdictions that become party to it, irrespective of existing tax treaties between the jurisdictions. MLC will consist of many rules that would resolve double taxation issues. A simplified administrative process and a robust dispute settlement mechanism will be set up for resolving the disputes binding to all jurisdictions<sup>36</sup>. If a tax treaty exists between the jurisdictions, then it would govern the cross-border taxation provided that if any inconsistency is present, then that part would be addressed by MLC to the extent necessary for reaching a practical solution concerning Amount A. If no such treaty exists, then MLC would be applied for implementing the aspects of Amount A. Parties to MLC would be required to all Digital Service Taxes and other pertinent measures. For implementing Amount A, the members are required to amend the domestic laws.

- **Implementation of Pillar Two**

The Model rules developed in December 2021<sup>37</sup> will give effect to the GLoBE rules under Pillar Two. These rules will define the scope of the GLoBE rules and will determine the mechanics through which effective tax rates would be calculated on a jurisdictional basis. An efficacious framework would be developed to facilitate the implementation of GLoBE rules. Administrative procedures and safe harbours would be developed that will benefit both the administrative authority and the MNEs.<sup>38</sup>

## VI. IMPACT OF TWO PILLAR TAX PACKAGE SYSTEM

The two-pillar tax package is a historical development in the international taxation system, eliminating the century-old tax rules and ensuring fair, efficient, and uniform tax practices. It will have an impact on Indian headquartered groups having international transactions as well as internationally headquartered groups having Indian operations.<sup>39</sup> Both groups had to analyse the transactions and determine whether the jurisdictions where they operate qualify as tax havens. If yes, they had to calculate the additional tax that must be paid in these jurisdictions. With the proper implementation of Pillar One and Two, more than \$125 billion and \$150 billion are estimated to be generated as global tax revenues every year, respectively.<sup>40</sup> The Two Pillar solution would provide a promising environment for investments and growth. By introducing this rule, multinational corporations would no longer be able to avoid taxes by using profit-

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<sup>35</sup> *Supra*, Note 2

<sup>36</sup> *Supra*, Note 2

<sup>37</sup> *Supra*, Note 2

<sup>38</sup> *Supra*, Note 2

<sup>39</sup> *Supra*, Note 10

<sup>40</sup> *Supra*, Note 2

shifting techniques, thereby ensuring fair taxation. Implementing standard international tax rules may simplify compliance and reduce administrative burdens for tax authorities.

**(A) Benefits of the two pillar solution for countries and the businesses**

The two-pillar tax system is beneficial for both countries as well as the MNEs. Each pillar addresses the challenges and fills the gap in existing rules that paved the way for companies to avoid taxes easily. Implementation of Two Pillar tax system will have several benefits:

- i. Pillar One would allow the jurisdictions to collect taxes from companies with a consumer base irrespective of their physical presence, thereby creating new taxing rights for the tax haven countries.
- ii. Under Pillar One, an effective dispute resolution mechanism would be set up with an elective tool for low-capacity countries to resolve tax avoidance issues if they arise<sup>41</sup>.
- iii. Pillar Two ensures that a global minimum tax rate of 15% is paid by the MNEs thereby preventing base erosion and profit shifting.
- iv. The global minimum tax rate prevents harmful tax competitions between countries that were practised by countries to attract Foreign Direct Investment by MNEs in their jurisdictions. This creates a more stable environment for both governments and businesses.
- v. Introducing a Global Minimum Tax rate would simplify and standardize tax regimes of different jurisdictions.
- vi. Pillar one will help prevent harmful trade disputes between countries by removing the Digital Services Tax and other similar prevalent relevant measures<sup>42</sup>.
- vii. The two-pillar system establishes a transparent and standardized framework of rules, providing businesses with greater predictability thereby reducing uncertain tax liabilities.
- viii. The two-pillar approach ensures the development of all countries, including the developing countries, by fairly allocating the revenues and applying a minimum tax rate.
- ix. Pillar Two enforces global minimum tax, enabling developing countries or tax havens to prevent profit shifting from their jurisdictions and allowing them to attract genuine substantive Foreign Direct Investment<sup>43</sup>.

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<sup>41</sup> *Supra*, Note 2

<sup>42</sup> *Supra*, Note 2

<sup>43</sup> *Supra*, Note 2

**(B) Challenges of the two pillar solution**

- i. The fundamental challenge of the two-pillar system is its consistent implementation across different jurisdictions, as it requires coordination and cooperation among countries with varying taxation systems and rules<sup>44</sup>.
- ii. Due to its complex nature, the new rules would require greater tax compliance adjustments by large and small businesses, leading to more enormous compliance costs burdening small businesses.
- iii. Though the safeguards are provided for developing countries, there are concerns regarding their practical implementation<sup>45</sup> and whether they will adequately protect the interests of smaller and less developed countries.
- iv. The successful implementation of the two-pillar tax system would depend on international cooperation and agreement between countries<sup>46</sup> with different economic and political interests, as geopolitical tensions and other national interests would hinder the system's adoption.
- v. Pillar two could disproportionately affect small and developing countries that previously relied on the low corporate tax rates and other tax incentives for attracting Foreign Direct Investment in their jurisdictions. By implementing the global minimum tax rate, the ability of the developing countries could reduce to attract FDI<sup>47</sup>.
- vi. The other primary concern is double taxation in case a dispute arises between two countries. While the two-pillar solution was introduced to prevent double taxation, there are concerns that it will lead to double taxation of MNEs income if conflicts occur between the countries, resulting in economic inefficiencies and uncertainties.
- vii. The two-pillar system captures large and small businesses that may lead to unintentional consequences, affecting those entities as well that do not engage in aggressive tax planning.
- viii. The two-pillar solution aims to eliminate destructive tax competition by establishing a harmonised international tax system. However, the challenge lies in how this harmony would be achieved; it is a simple solution to have a uniform tax system across the globe,

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<sup>44</sup> Noonan et al, *Compliance Challenges of the BEPS Two-Pillar Solution*, BRITISH TAX REVIEW (Dec 16, 2022) [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=4323926](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4323926)

<sup>45</sup> Id

<sup>46</sup> *Supra*, Note 42

<sup>47</sup> *Supra*, Note 42

but it is not realistic when each country can develop its tax system.

## **VII. IMPLICATIONS OF TWO PILLAR SOLUTION ON DEVELOPING COUNTRIES**

Developing countries having a large number of consumers of digital services have the potential to gain a lot from Pillar One as it guarantees equitable distribution of tax revenues of MNEs to the jurisdictions where these MNEs operate. This will improve the financial stability and economic growth of these countries.

Introducing a Global Minimum Tax Rate would enable developing countries to lessen the tax incentives to MNEs and prevent the shifting of profits out of developing countries, thereby ending tax havens. The two-pillar solution, being a multilaterally agreed solution, helps avoid the risk of retaliatory trade sanctions that usually arise from unilateral measures like Digital Services Taxes. When imposed by governments of different countries, these unilateral measures often turn out as full-blown trade disputes<sup>48</sup>. To a great extent, the two-pillar solution is a globally recognised framework that prevents these trade conflicts by encouraging international cooperation and coordination among the countries. The solution provides an elective dispute mechanism to help developing and small countries opt out of the mandatory dispute resolution processes<sup>49</sup>. The significant advantage these countries would have is the increase in revenues as Pillar One and Pillar Two will generate USD 125 billion and USD 150 billion in revenues yearly, respectively<sup>50</sup>. The developing countries might face challenges in adequately implementing the solution if they lack the administrative capacity and expertise. The system promotes global economic equity by addressing tax avoidance and profit shifting. It helps reduce disparities between developing and developed countries, creating a more level playing field for all nations.

## **VIII. ROLE OF INTERNATIONAL ORGANISATION IN SHAPING THE TWO PILLAR SYSTEM**

### **(A) Role of OECD**

The Organisation for Economic Cooperation and Development has played a pivotal role in introducing and implementing the Two Pillar Tax Package system. Its function is instrumental in the development of this ground-breaking system and also in its coordination and adoption. The OECD journey could be traced back to its introduction of the BEPS project, which aimed

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<sup>48</sup> *Supra*, Note 2

<sup>49</sup> *Supra*, Note 2

<sup>50</sup> *Supra*, Note 2

to tackle problems of tax avoidance, profit shifting and erosion of taxes by MNEs.<sup>51</sup> The project recognised the need to develop a coordinated international system to ensure taxes are fairly paid. This marked the beginning of the OECD's active role in implementing and reshaping a global tax regime. In 2013, the OECD launched the BEPS 15 action plan<sup>52</sup> that laid the foundation of the Two Pillar Tax system. OECD played a significant role in the global negotiations among its members and all the other stakeholders. It facilitates dialogue and negotiations between the member countries having diverse interests and tax systems, ultimately leading to the development of the Two-Pillar Tax System.<sup>53</sup> The OECD is the leading authority in developing and implementing both pillars of the solution, ensuring the proper allocation of funds and enforcement of the Global Minimum Tax. The OECD has worked tirelessly to ensure that countries from diverse economic interests reach a consensus. OECD will help the countries adapt their domestic legislation with new rules by providing technical and financial support<sup>54</sup>. The OECD's role extends to promoting transparency and cooperation in international taxation. It encourages countries to exchange information and exchange in a collaborative effort to combat tax avoidance and profit shifting. The OECD's role in fostering international consensus and promoting fair and transparent taxation is central to the success of the Two-Pillar Tax system.

### **(B) Role of G20 Stakeholders**

Recently, at the G20 summit in New Delhi, the members adopted the New Delhi Leader's Declaration, in which one issue was related to international taxation. In this Declaration, the member countries reaffirmed their commitment to continuing cooperation towards a globally fair, sustainable, modern global taxation system. Also, they committed themselves to swiftly implementing the Two Pillar International tax package.<sup>55</sup>

The involvement of G20 countries, representing the world's most influential and powerful economies, is instrumental in successfully implementing the Two Pillar Tax System. These economies are pivotal in shaping international policies and comprehensive tax reforms. Their efforts are significant, motivating other nations to participate and adhere to the inclusive framework. Collaboration between G20 countries and establishing robust monitoring and enforcement mechanisms are critical components of the Two-pillar tax solution. It facilitates

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<sup>51</sup> Sol Picciotto, The G20 and the “Base Erosion and Profit Shifting (BEPS) Project”, IDOS,(Apr.2017), [https://www.idos-research.de/uploads/media/DP\\_18.2017.pdf](https://www.idos-research.de/uploads/media/DP_18.2017.pdf)

<sup>52</sup> *Supra*, Note 45

<sup>53</sup> *Supra*, Note 45

<sup>54</sup> *Supra*, Note 2

<sup>55</sup> *New Delhi Leader's Declaration Final Adoption*, G20,(Sep.2023), [https://www.g20.org/content/dam/gtwenty/gtwenty\\_new/document/G20-New-Delhi-Leaders-Declaration.pdf](https://www.g20.org/content/dam/gtwenty/gtwenty_new/document/G20-New-Delhi-Leaders-Declaration.pdf)

cooperation and coordination among jurisdictions with diverse and distinct tax systems, leading to the abridgement of gaps between developing and developed countries, and ensures that the system is for the benefit and interests of all. The OECD, along with the G20 stakeholders, is responsible for supervising the implementation of the system<sup>56</sup>. This involves tracking the amendments that need to be incorporated into the countries' domestic legislation for a compelling adaptation of the new rules. The stakeholders of G20 recognise the system's implications and conduct engaging discussions on aligning the system with a global economic goal and ensuring that the framework aligns with sustainable economic growth and development. The G20 members advocate for fair and consistent taxation practices on taxation. They emphasise the importance of the system and the consequences of tax avoidance practices, contributing to the development of the Two-Pillar System. The stakeholders of G20 acknowledge the interdependence between trade and taxation<sup>57</sup>. They realise that unilaterally implementing digital services taxes and other tax measures can cause trade disputes and tensions. The G20 endorses the Two-Pillar System, which helps to alleviate these potential risks and helps foster a more cooperative global trade scenario.

The G20 stakeholders play a crucial role in driving the advancement of the Two-Pillar Tax System, promoting inclusive global taxation reforms, coordinating international efforts, advocating for equitable taxation practices, and encouraging adherence to the system's regulations. Their active involvement not only fosters global consensus and strengthens the international tax environment but also contributes significantly to the success of the Two-Pillar System in addressing the complexities of taxing multinational enterprises in the contemporary global economy.

## **IX. FUTURE OF GLOBAL TAXATION**

### **(A) Evolving Landscape of International Taxation**

The evolving landscape of international taxation is a dynamic arena shaped by globalisation, digitalisation and the urge to change tax policies that are more transparent and unbiased. With the rise in technological advancements, businesses can now operate from anywhere without having a physical presence. The practice of profit shifting by multinational companies to tax havens has raised concerns about tax avoidance. The resulting complexities have provoked the tax authorities to create new laws and rules to ensure that digital businesses contribute their fair share of taxes. OECD's Two-Pillar taxation system is a significant step in this direction, aiming

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<sup>56</sup> *Supra*, Note 45

<sup>57</sup> *Supra*, Note 45

to curtail these practices by imposing a global minimum tax rate. Countries are also inculcating unilateral measures like Digital services taxes (DST) to capture revenue from tech giants. DST aims to target revenues generated from digital services and advertisements, but these measures have sparked concerns about trade tensions and double taxation.<sup>58</sup> The new international taxation system is inclusive as it involves developing countries in shaping the global taxation system. The Bilateral and Multilateral agreements, which aim to address specific tax issues, have also seen a growth in fostering international cooperation between the nations. The public and stakeholders have gained a more prominent role in shaping tax policies due to the proliferation of information and advocacy groups. Consequently, there is an amplified demand for transparency and accountability from both governments and corporations, resulting in changes in tax reporting and disclosures and a more significant emphasis on responsible tax practices. Finally, international organisations like the OECD and the UN play pivotal roles in shaping international taxation by initiating frameworks that provide guidelines for countries and corporations.

### **(B) Potential for Further Reforms**

The dynamic nature of international taxation indicates significant potential for reforms responding to the emerging needs and challenges of the evolving global economic paradigm. The critical area of focus of the system is the taxation of the digital economy. The rapid growth in digital services and cross-border transactions presents complexities in determining tax liabilities. Reforms are necessary to ensure transparent and equitable taxation of profits of digital activities, addressing profit shifting issues and ensuring fair distribution of tax revenues among jurisdictions.

Environmental and sustainability issues are a significant part of global discussions and are reflected in the potential for additional tax reforms. Environmental taxes such as carbon or pollution levies could be introduced as nations seek to align taxation with broader sustainability goals. The incentives or other benefits could be offered to companies/businesses that engage in eco-friendly business practices.

A provision for adjustments in the global minimum tax could be brought in to account for economic changes, inflation or shifts in the global economic landscape. The role of taxation in funding the initiatives of different international organisations like UN sustainable development goals may be further emphasised, aligning tax policies with broader societal aspirations.

The expansion in technologies like blockchain and cryptocurrencies reminds us of the need for

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<sup>58</sup> *Supra*, Note 2



their taxation. Regulatory measures could be developed to ensure these financial instruments are taxed fairly, uniformly and transparently.

The major reform could be the expansion of the role of the public and stakeholders in shaping the tax policies, as it could involve more transparent and inclusive decision-making processes, ensuring that tax policies align with societal needs and expectations.

## **X. CONCLUSION**

In the sweeping tide of globalisation and digitalisation, the two-pillar tax system introduced by OECD emerges as a landmark solution, reshaping the contours of international taxation. Pillar One's innovative approach, realigning taxing rights to market jurisdictions, ensures that MNEs are taxed where profits are generated, challenging the traditional norms of physical presence. This groundbreaking paradigm shift responds to the challenges posed by the digital economy, curbing profit shifting and strengthening the tax sovereignty of countries. Meanwhile, Pillar Two establishes a global minimum tax rate, a crucial measure to prevent tax competition and ensure that MNEs contribute a minimum of 15 % in taxes, fostering stability in the global economic landscape.

The implications of the Two-Pillar tax system are profound and multifaceted. It offers a robust framework for fair and transparent taxation, closing gaps that facilitate tax avoidance and creating a level playing field for developed or developing nations. The system's particular significance for developing countries lies in its promise of equitable revenue distribution. The shift towards a minimum tax rate mitigates harmful tax practices, fostering a more stable environment for governments and businesses.

However, implementing such a transformative system comes with challenges, such as the need for international cooperation and consensus. The OECD and G20 stakeholders play a pivotal role in effectively enforcing and adapting the Two-Pillar tax system across nations. The system opens avenues for further reforms, addressing emerging challenges in the digital economy sustainability and incorporating the evolving role of the public in shaping tax policies.

In conclusion, the Two-Pillar Tax System catalyses a more equitable, transparent and sustainable global taxation framework, setting the stage for a new era in international fiscal governance.

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