EU Directive on Pillar II

10 January 2022

This presentation is just a high level overview of the new rules in Directive compared to the Blueprint. For more information and questions please contact us (see details last page).

Agenda

1. EU Directive – timeline & changes
2. Scope and terms
3. Directive methodology & ETR calculation
4. Filing obligation
5. Transition Rules
6. Special rules
7. Co-existence with US tax reform

Timeline & Key changes

Most important changes:

- Deferred tax accounting
- Filing Requirements
- Domestic application of IIR and UTPR
- UTPR allocation on FTEs and Assets
- Alternative (domestic) minimum tax of 15%
- Transition rules
- Local accounts
- Special rules
- No credits

Clarifications:

- Scope
- Investment entities
- Acceptable accounting standard
- Portfolio dividends
- Treatment of JVs

Not included:

- Simplifications
- Pref shares
- Control other than consolidation

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Scope

The Directive applies to:

- MNE Group with Turnover of 750 mln Euro or more in 2 out of the last 4 years
  - Based on consolidated financial accounts (or deemed financial accounts)
  - Consolidated accounts to be adjusted to acceptable standard
  - Mergers & Demergers (not discussed here)

- MNE Group is all entities and PEs (Constituent Entities) in at least 2 jurisdictions related through ownership or control as defined by the (acceptable) financial accounting standard (are included or should have been included in consolidation).

- Large-scale (Turnover > 750 mln Euro) Domestic Group

- Ultimate Parent Entity (UPE) in EU (NL)
- Partially Owned Parent Entity (POPE) in EU (NL) and not controlled by another POPE
- Intermediate Parent Entity (IPE) in EU (NL) and no IIR at Ultimate Parent Entity (UPE) level

New Terms

- **Intermediate Parent Entity** (IPE) - > a Constituent Entity (CE) that owns a controlling interest in another CE and is not a Ultimate Parent Entity (UPE), Partially Owned Parent Entity (POPE) or Investment Entity

- **Partially Owned Parent Entity** (POPE) - > 20% owned outside the group

- **Investment Entity** -> an investment fund:
  - Pools assets for non-related investors
  - Is subject to regulatory regime in jurisdiction
  - Managed by fund management professionals

- **Qualifying income or loss** - > financial accounting income adjusted according to the rules of the Directive

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Pillar 2 - methodology

1 **Determine STTR impact ***

2 **Calculate jurisdictional ETR**

3 **Apply IIR allocation**

4 **Apply UTPR allocation**

* This step will not be further discussed in this presentation

Pillar 2 - methodology

1 Determine STTR impact

2 **Calculate jurisdictional ETR**

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Calculate Jurisdictional ETR

$$\textbf{Jurisdictional ETR} = \frac{\textbf{Adjusted Covered Taxes in jurisdiction}}{\textbf{Qualifying income or loss in jurisdiction}}$$

- **Qualifying income or loss** = Financial accounts income + or – adjustments
- **Adjusted covered taxes** = current tax and deferred tax in Financial accounts + or - adjustments, recaptures, top-ups, recalculations etc.
- Local stats may be used provided that this doesn't lead to a competitive distortion (tax payer to demonstrate)

Standard adjustments to qualifying income

(+/-)	**Adjustments necessary to achieve arm's length results**
(+/+)	net tax expenses;
(-/-)	excluded dividends;
(-/-)	excluded equity gains or losses;
(+/-)	included revaluation method gains or losses;
(+/-)	gains or losses from the disposal of assets and liabilities excluded pursuant to Art 33;
(+/-)	asymmetric foreign currency gains and losses;
(-/-)	policy disallowed expenses;
(+/-)	prior period errors and changes in accounting principles;
(+/+)	Qualified refundable tax credits;
(+/-)	Increases or decreases of Tier 1 capital; and
(-/-)	accrued pension expenses
(-/-)	interest paid by LT CE related to b-2-b finance arrangement with high tax CE

Standard adjustments to qualifying income

Net Tax Expense is the net amount of:

(i) covered taxes accrued as an expense;
(ii) deferred tax assets attributable to a loss for the fiscal year;
(iii) qualified domestic top-up taxes accrued as an expense;
(iv) taxes arising pursuant to the rules of this Directive; and
(v) disqualified refundable imputation taxes accrued as an expense;

Excluded dividend is a dividend on shareholdings of 10% or more; i.e. dividends on shareholdings < 10% (portfolio shareholdings) are not exempt.

Standard adjustments to qualifying income

Asymmetric foreign currency gain or loss:

(i) FX included in taxable income and caused by difference between tax and accounting functional currency;
(ii) FX included in accounting income and caused by the difference between tax and accounting functional currency;
(iii) FX included in accounting income and caused by the difference between foreign currency and accounting functional currency;
(iv) FX fluctuation between a foreign currency and the tax functional currency;

Prior period adjustments to opening equity cannot be included if these resulted in a material decrease in covered taxes in a prior year.

Elected adjustments to qualifying income

Stock based compensation (5 years) – treat as deductible from income if deductible for tax. Recapture applies

Application of consolidated accounting treatment to transactions within the tax consolidation group (5 years). Adjustments upon revocation.

Determination based on the realisation principle instead of fair value accounting (5 years). Recapture applies

Gain from sale of immovable property to 3rd party can be carried back four years to offset loss on the sale of the same (1 year).

Adjusted Covered Taxes

Calculation of the amount of **Adjusted Covered Taxes**:

	1. Covered Taxes
+/-	2. Mandatory adjustments to Covered Taxes
+	3. The total deferred tax adjustment (Allowable DTL)
-	4. Any covered tax accrued in equity or OCI (related to amounts included in qualifying income)
-	5. Accrual of Qualifying DTA on losses (election)
+	6. Use of Qualifying DTA on losses
-	7. Recapture of DTL previously recognised
-	8. Revocation of Qualifying DTA on losses

Covered Taxes - Definition

Covered tax = Net tax expense in financial accounts (excl DT), and:

Includes (add if necessary) in covered tax

- Tax accrued in the accounts (including WHT on interest and royalties)
- Tax on distributed profits (paying entity)
- Tax imposed in lieu of corporate income tax
- Tax on equity and retained earnings

Excludes (deduct if necessary) in covered tax

- IIR Top-up Tax (TUT) accrued by parent
- Qualified Domestic Top-up tax
- UTPR taxes
- Disqualified Refundable imputation tax
- Tax profit from sale of immovable property if election is made

Mandatory adjustments to Covered Taxes

Add to Covered Taxes:

- Covered tax accrued as expense
- Amount of qualifying loss DTA (election)
- Amount of UTP previously excluded and paid in the current year
- Amount of refund of refundable tax credit accrued as a reduction of tax expense

Deduct from Covered Taxes:

- Tax related to excluded income
- Amount of tax expense related to UTP
- Amount of tax expense not expected to be paid within 3 years*
- Tax refund that wasn't treated as a reduction of tax expense

* Any amount of covered tax accrued in excess of 1 mln Euro, but not paid within three years has to be deducted from the covered tax in the year it was accrued and that year has to be recomputed.

Total Deferred Tax (liability) Adjustment Amount

Total Deferred Tax Adjustment Amount = the Deferred Tax expense (liability) accrued in the financial accounts recorded at the lower of statutory rate or 15%, and subject to the following adjustments:

Deduct / eliminate

- Uncertain Tax Positions (accrued vs paid)
- Excluded income
- Generation and use of tax credits
- Valuation adjustments, Remeasurements and accounting recognition.
- Distribution tax accrual (accrued vs paid)
- Any loss DTA not accrued because recognition rules weren’t met (at 15%)

Add:

- Previously disallowed amounts paid during the year
- Amount of previously recaptured DTL paid in the current year

Recapture and recalculation:

If not paid within 5 years, except for DTL on: Depreciation of Tangibles assets, R&D expenses, FX net gains, (and other)

Deferred Tax – jurisdictional treatment of losses

High tax jurisdiction: Deferred Taxes on losses are not recognised unless election is made.

Election:

- A qualifying loss election may be made for a jurisdiction (not per CE) for each year in which there is a net qualifying loss
- The DTA shall be recognised at 15%
- Unlimited carry forward

Low tax jurisdiction:

If the there is a net qualifying loss in the jurisdiction and the adjusted covered tax amount is negative and less than 15% * qualifying loss, than the difference between these two amounts is additional top-up tax (and allocated according to article 28).

Adjusted Covered Taxes - Special rules

- Specific allocation of taxes applies to: Permanent Establishment, Transparent entities & Hybrids, Distribution Taxes, and CFC taxes (with a cap).

- Post-filing adjustments: are included in the first year if covered tax increases. If adjustment is a decrease it needs to be taken into account in a previous year and that year's income and covered tax recomputed. Upon election decreases < 1mln can be included in the current year.

- Tax rate changes and deferred tax:
  - Reduction to below 15% -> reduction of DTA accounted in years it was accrued (recompute)
  - Increase to above 15% -> account in previous year, but only after actual payment

Calculation & allocation of top-up tax (TuT)

TuT per entity if jurisdiction has net qualifying **income** - steps:

1. ETR for Jurisdiction
2. TuT percentage for jurisdiction (15% - ETR)
3. Calculate Additional TuT amount (incremental TuT caused by prior year recalculations)
4. Calculate excess profit (qualifying income -/- substance based carve out)
5. Jurisdictional TuT amount = (TuT% * Excess profit) + Additional TuT – Domestic TuT
6. Jurisdictional TuT amount * (CE's qualifying income / Total qualifying income of CEs in jurisdiction)

TuT per entity if jurisdiction has net qualifying **loss** – steps:

1. Allocate Additional TuT per jurisdiction due to current year DTA recast at 15%
   a. Identify CEs with negative ETR < 15%
   b. (Qualifying loss per entity * 15%) – adjusted covered taxes per entity = X per entity
   c. X per entity / 15% = qualifying income per entity
   d. Qualifying income per entity / Total qualifying income per jurisdiction * Add TuT = Additional TuT per entity
2. Allocate Additional TuT caused by prior year recalculations (based on prior year income)
3. Add amounts 1 and 2

Pillar 2 - methodology

1. Determine STTR impact
2. Calculate jurisdictional GloBE ETR
3. **Apply IIR allocation**
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IIR Allocation to UPE

Add:

1. TuT per CE * Parent's share in the entity (for each entity including domestic)
2. Parent's own TuT as calculated under previous rules
3. Any amount of Qualified Domestic TuT not paid within 3 years

Deduct:

1. IIR allocated to a POPE
2. Amount of Qualified Domestic TuT (can be less than #1 above)

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Apply UTPR Allocation

- Applies to CEs in MS of LT UPE (regardless of IIR)
- Applies to any TuT that is not wholly or partially subject to IIR
- Allocated to all Jurisdictions with P2 equivalent rules
- Allocation based on 2 formulas:

50% of UTPR allocated based on FTEs
50% of UTPR allocated based on Tangible Assets

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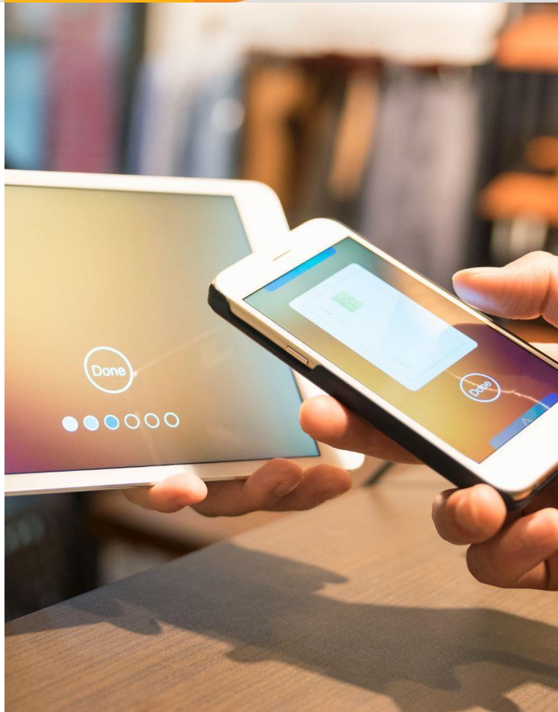
Filing obligations

Who?

UPE or other designated filing CE file a top-up tax information return with the tax authorities in its jurisdiction; for all jurisdictions with which there is an Exchange of Information agreement (!)

CEs in other jurisdictions must notify their tax administration of the identity of the filing CE and its jurisdiction



Filing obligations

What?

The top-up tax information return contains:

a) identification of the constituent entities, including their tax identification numbers, if any, the jurisdiction in which they are located and their status under the rules of this Directive;

b) information on the overall corporate structure of the MNE group, including the controlling interests in the constituent entities held by other constituent entities;

Filing obligations

What? (con'd)

c) the information that is necessary in order to compute:
   (i) the effective tax rate for each jurisdiction and the top-up tax of each constituent entity;
   (ii) the top-up tax of a member of a joint-venture group;
   (iii) the allocation of top-up tax under the income inclusion rule and the UTPR top-up tax amount to each jurisdiction; and

d) a record of the elections made in accordance with the relevant provisions of this Directive.

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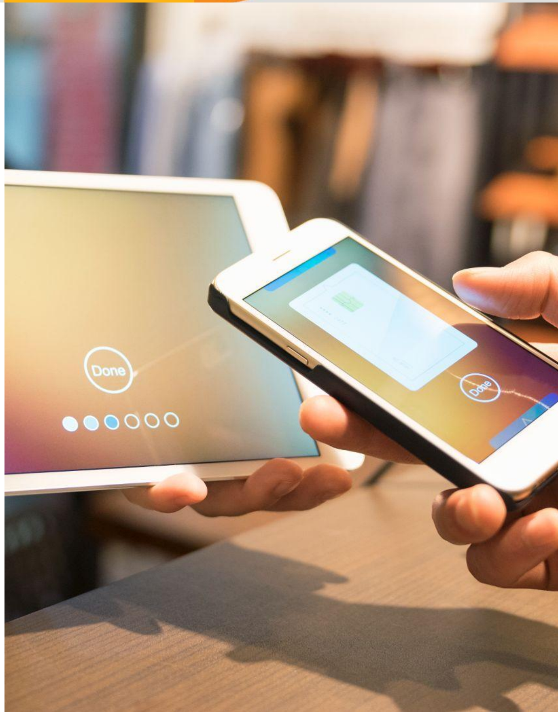
Transition rules

Deferred tax assets as disclosed in the accounts shall be taken into account with the following adjustments:

- The lower of the domestic rate and 15%
- Deferred tax on excluded items eliminated when generated after 15/12/2021
  -> DTA accrued can be recognised at 15% if attributable to qualifying loss.
- Transfers of assets between CEs after 15/12/2021 taken into account at transferring CE’s NBV.
- Impact of valuation or accounting recognition adjustment shall be disregarded.



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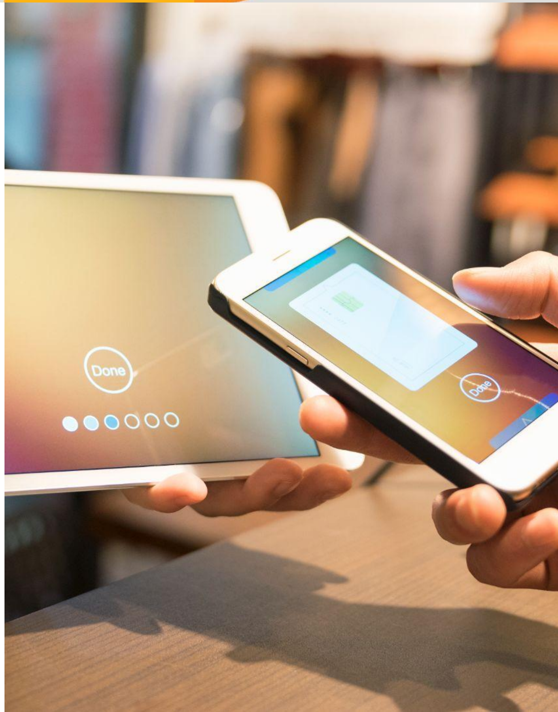
Special rules

- M&A
- Transfers of assets and liabilities
- Joint Ventures
- Multi-parented MNEs
- Flow-through entities as UPE
- Deductible distribution tax regime
- Investment Entities (aka Investment funds)
- Exclusion rules for MNEs in initial phase of international activity
- Large Domestic Groups



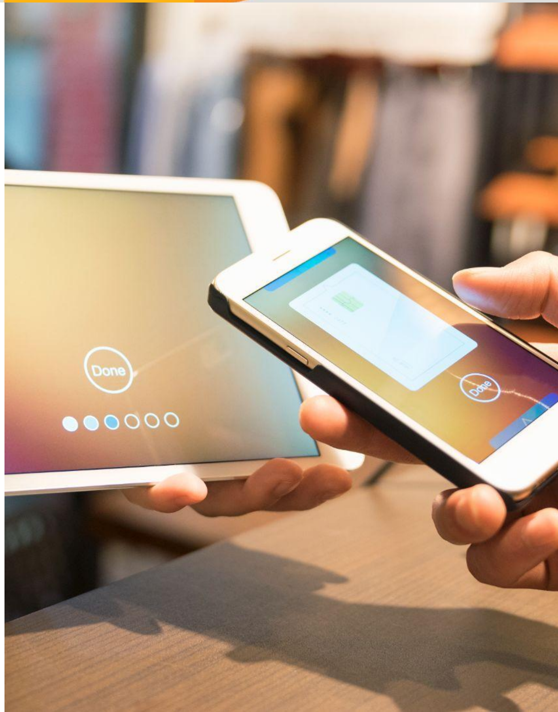
Special rules – M&A

The target entity (entities) shall be included on a pro-rata basis in the MNE(s) that consolidates it on a line by line basis.

Assets & Liabilities	- Included at historical carrying value
Carve-out	- Payroll based on what's included; tangible assets prorated for ownership period
DTA and DTL	- Restate as if arisen during ownership of acquirer
	- Qualifying loss DTA does not transfer
DTL transfer	- Deduct in seller; add in acquirer
	- Deduction leads to recalculation in the years the DTL has been accrued by seller

Special rules – transfers of assets

- Gain or loss included in qualifying income of seller; acquirer recognizes step-up based on its financial accounting standard
- Tax neutral reorganization under local rules is recognised for Pillar 2
- Where reorganization is partially taxed, seller and acquirer use tax values



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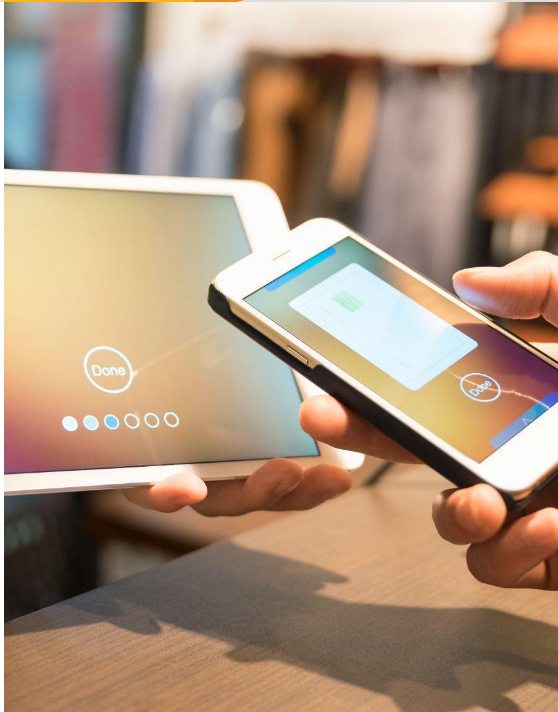
US tax reform



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